Analyst shall notify applicants in writing that such information need no longer be submitted).

For the Commission, by the Division of Investment Management, under delegated authority.

Jonathan G. Katz,

Secretary.

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[Release No. 34–37273; File No. SR–NYSE–95–47]

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Granting Approval to Proposed Rule Change Relating to the Exclusion of Competing Market Maker Orders From Trading at No Charge

June 4, 1996.

I. Introduction

On December 29, 1995, the New York Stock Exchange, Inc. (''NYSE'' or ''Exchange'') submitted to the Securities and Exchange Commission (''SEC'' or ''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] a proposed rule change to exclude orders of nonmember competing market makers from the NYSE's no charge provision for system orders of 100 to 2,099 shares.

The proposed rule change was published for comment in the Federal Register on January 5, 1996.[3] The Commission initially received a total of four comment letters opposing the proposal.[4] On April 26, 1996, the NYSE submitted its response to these comment letters.[5] After receiving the NYSE's response, the Commission received four additional comment letters.[6] For the reasons discussed below, the Commission, after careful consideration, has decided to approve the NYSE's proposal.

II. Background and Description of the Proposal

A. Transaction Credits

On November 7, 1995, the NYSE, pursuant to Section 19(b)(3)(A) of the Act,[7] filed a rule change with the Commission that made a series of revisions to the Exchange's equity[8] transaction fee schedule, including the exclusion of nonmember competing market makers from the NYSE's no charge provision for system orders of 100 to 2,099 shares.[9] Prior to such filing, the NYSE's transaction fee schedule imposed on all public agency,[10] equity transactions the following charges:

$0.00265 per share for the first 5,000 shares;

$0.00010 per share for 5,001 to 672,500 shares; and no charge for all shares in excess of 672,500.

The NYSE's transaction fee schedule also provided for a credit of $0.30 per order for all orders of 100 to 2,099 shares that were placed through the NYSE's Common Message Switch (''CMS'')[11] and an additional credit of $1.30 for all Individual[12] or Agency[13] market orders of 100 to 2,099 shares placed through the NYSE's CMS. Orders executed by members and member organizations for the account of a competing market maker,[14] however, were not eligible for the additional system credit. This additional system credit was applied on a monthly basis against the member or member organization's total transaction charges.

B. Payment for Order Flow

On October 27, 1994, the Commission adopted Rule 11Ac1–3[15] and amendments to Rule 10b–10[16] under the Act concerning payment for order flow practices.[17] These provisions were designed to improve the information available to investors about their broker-dealer's order routing practices and disclose to investors whether the broker-dealer received market center[18] inducements for routing unspecified order flow to a particular market.[19] In defining payment for order flow, the Commission took a very broad approach so that all forms or arrangements whereby a broker-dealer received compensation for directing order flow to a particular market were included. Specifically, payment for order flow was designed to include any credit, rebate, or discount against execution fees that exceeds the fee charged for executing the order.[20] As a result, credits received by NYSE members under the NYSE's transaction fee schedule constituted

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[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Securities Exchange Act Release No. 36658 (Dec. 29, 1995), 61 FR 436.

[4] *See* letter from John I. Fitzgerald, Executive Vice President, Legal Affairs and Trading Services, Boston Stock Exchange, Inc. (''BSE''), to Jonathan G. Katz, Secretary, SEC, dated February 21, 1996 (''BSE February 21, 1996 Letter''); letter from George T. Simon, Foley & Lardner, on behalf of the Chicago Stock Exchange, Incorporated (''CHX''), to Jonathan G. Katz, Secretary, SEC, dated March 4, 1996 (''CHX March 4, 1996 Letter''); letter from William W. Uchimoto, First Vice President and General Counsel, Philadelphia Stock Exchange, Inc. (''Phlx''), to Jonathan G. Katz, Secretary, SEC, dated February 23, 1996 (''Phlx February 23, 1996 Letter''); letter from David P. Semak, Vice President, Regulation, Pacific Stock Exchange Incorporate (''PSE''), to Jonathan G. Katz, Secretary, SEC, dated March 4, 1996 (''PSE March 4, 1996 Letter'').

[5] *See* letter from James E. Buck, Senior Vice President and Secretary, NYSE, to Jonathan Katz, Secretary, SEC, dated April 25, 1996 (''NYSE April 25, 1996 Letter''). Previously, the NYSE had granted the Commission an extension of 30 days after the date of the Commission's receipt of the Exchange's response within which to act on the NYSE's proposal. *See* letter from James E. Buck, Senior Vice President and Secretary, NYSE, to Glen Barrentine, SEC, dated March 13, 1996.

[6] *See* letter from George W. Mann, Jr., Senior Vice President and General Counsel, BSE, to Jonathan G. Katz, Secretary, SEC, dated April 23, 1996 (''BSE April 23, 1996 Letter''); letter from John I. Fitzgerald, Executive Vice President, Legal Affairs and Trading Services, BSE, to Jonathan G. Katz, Secretary, SEC, dated May 6, 1996 (''BSE May 6, 1996 Letter''); letter from J. Craig Long, Foley & Lardner, on behalf of the CHX, to Jonathan G. Katz, Secretary, SEC, dated May 6, 1996 (''CHX May 6, 1996 Letter''); letter from William W. Uchimoto, First Vice President and General Counsel, Phlx, to Jonathan G. Katz, Secretary, SEC, dated May 3, 1996 (''Phlx May 3, 1996 Letter'').

[7] 15 U.S.C. 78s(b)(3)(A). Pursuant to Section 19(b)(3)(A), a proposed rule change may take effect upon filing with the Commission if designated by the self-regulatory organization as, among other matters, establishing or changing a due, fee, or other charge imposed by the self-regulatory organization.

[8] The NYSE's transaction fee schedule defines the term ''equity'' to include shares, rights, and warrants.

[9] Securities Exchange Act Release No. 36465 (Nov. 8, 1995), 60 FR 57473 (publishing SR–NYSE–95–38.

[10] Equity public agency transaction fees and credits do not apply to principal transactions by NYSE members for their own accounts. *See* NYSE Transaction Fee Schedule n.1.

[11] The Common Message Switch is a data communications application that accommodates a wide variety of member firm computer and technical connections, enabling a member firm to send orders directly to the appropriate floor booth for execution by the firm's floor broker or by SuperDot to the appropriate specialist post. Accordingly, the NYSE's transaction fee schedule provided credits for SuperDot orders. *See* Securities Exchange Act Release No. 28655 (Nov. 29, 1990), 55 FR 50260, at n.1 (publishing SR–NYSE–90–54).

[12] An Individual order is an order for the account of any customer who is an individual as defined by NYSE Rule 80A. *See* Securities Exchange Act Release No. 29866 (Oct. 28, 1991), 56 FR 56432. That rule, in turn, cites Section 11(a)(1)(E) of the Act, which defines an individual investor as a natural person. *See* Securities Exchange Act Release No. 32377 (May 27, 1993), 58 FR 31568, at n.7 (approving NYSE's limitation on the additional system credit concerning nonmember competing market makers).

[13] An Agency order is an order for the account of any customer, other than a natural person, who is a nonmember of nonmember organization. *Id.* at n.8.

[14] The proposed rule change defines a competing market maker as ''a specialist or market maker registered as such on a registered stock exchange (other than the NYSE), or a market maker bidding and offering over-the-counter in a New York Stock Exchange-traded security.''

[15] 17 CFR 240.11Ac1–3.

[16] 17 CFR 240.10b–10.

[17] *See* Securities Exchange Act Release No. 34902 (Oct. 27, 1994), 59 FR 55006 [hereinafter Payment for Order Flow Release].

[18] *See* 17 CFR 240.11Ac1–2(a)(14) (defining ''reporting market center'').

[19] *See* Payment for Order Flow Release, *supra* note 17.

[20] *See* Payment for Order Flow Release, *supra* note 17.

payment for order flow where such credit exceeded the transaction charged associated with such order.[21] In response to these new disclosure requirements, the NYSE decided to revise its transaction fee schedule so that its members would not be required to comply with Rule 11Ac1–3[22] and Rule 10b–10[23] regarding disclosure of the receipt of payment for order flow.[24]

C. SR–NYSE–95–38

On November 7, 1995, the NYSE submitted a rule filing pursuant to Section 19(b)(3)(A) of the Act[25] that revised its equity transaction charges, effective January 2, 1996.[26] Among other things, this filing: (1) eliminated all SuperDot system credits, (2) reduced the equity transaction fees on orders for 5,000 shares and under from $0.00265 per share to $0.0019 per share,[27] (3) eliminated the equity transaction charges for SuperDot system orders of 100 to 2,099 shares, except for orders of competing market makers, and (4) capped monthly equity transaction fees at $400,000. The Commission published the notice of filing and immediate effectiveness of this rule change on November 8, 1995.[28] Subsequently, the Commission received three comment letters regarding this rule change.[29]

D. SR–NYSE–95–46

In response to these comment letters, the Commission requested that the NYSE withdraw that portion of the filing concerning the exclusion of competing market maker orders from the NYSE's no charge policy and resubmit it pursuant to Section 19(b)(1)[30] for notice and action pursuant to Section 19(b)(2).[31] This would provide sufficient time for the Commission to consider, and interested parties to comment on, that portion of the filing.[32] In complying with the Commission's request, on December 29, 1995, the NYSE submitted two related rule filings: SR–NYSE–95–46 and the current proposal, SR–NYSE–95–47.

In SR–NYSE–95–46, the NYSE revised its equity transaction charges, effective January 2, 1996,[33] to eliminate the exclusion of competing market maker orders from the no charge provision for SuperDot system orders of 100 to 2,099 shares. The Exchange, however, also reserved the right to collect, retroactive to January 2, 1996, the fees on such trading in the event the Commission approved SR–NYSE–95–47.[34] The Commission published the notice of filing and immediate effectiveness of this rule change on December 29, 1995.[35]

E. The Current Proposal

The Exchange now proposes to amend its fee schedule to re-institute the exclusion of competing market maker SuperDot system orders of 100 to 2,099 shares from the NYSE's no charge policy. This change, in effect, would impose a charge of $0.0019 per share on competing market maker SuperDot system orders of 100 to 2,099 shares and, furthermore, allow the Exchange to collect equity transaction charges on all such orders that have been executed on the NYSE since January 2, 1996.[36]

III. Summary of Comments

The Commission received a total of eight comment letters from the BSE, the CHX, the PHlx, and the PSE (collectively referred to herein as the ''commenters'') regarding the exclusion of competing market maker system orders from the Exchange's no charge provision.[37] In its response, the NYSE supports its proposal and responds to the first four comment letters.[38] The issues raised by the commenters are discussed below.

A. Equitable Allocation of a Reasonable Fee

The commenters believe that the proposal is inconsistent with Section 6(b)(4) of the Act[39] because it constitutes an inequitable allocation of fees[40] and further assert that the proposal is inconsistent with Section 6(b)(5)[41] because it unfairly discriminates among certain brokers, dealers, and customers,[42] as well as compromises the existence of a free and open market.[43]

To support its opposition to the proposal, the CHX explains that nonmember competing market makers do not receive any trading advantage on the NYSE Floor that justifies this disparate treatment, and that this proposal does not provide any benefit to

[21] For example, under the NYSE's transaction fee schedule, NYSE members and member organizations were receiving payment for order flow for certain system orders of 100 to 603 shares. For orders greater than 603 shares, the NYSE equity transaction charges exceeded the $1.60 credit granted.

[22] 17 CFR 240.11Ac1–3.

[23] 17 CFR 240.10b–10.

[24] On October 13, 1995, the Commission issued a letter to the Securities Industry Association granting all registered broker-dealers a temporary exemption from the confirmation disclosure requirements of Rule 10b–10(a)(2)(C) and a no-action position regarding the account opening provisions of Rule 11Ac1–3. This exemption and no-action position expired on November 5, 1995. Subsequently, the Commission issued another similar letter to the NYSE effective from November 6, 1995 to December 31, 1995. *See* letter from Brandon Becker, (then) Director, Division of Market Regulation, SEC, to Edward A. Kwalwasser, Group Executive Vice President, Regulation, NYSE, dated November 8, 1995.

[25] 15 U.S.C. 78s(b)(3)(A). *See supra* note 7 (detailing which rule filings may be submitted pursuant to this section for immediate effectiveness).

[26] Securities Exchange Act Release No. 36465 (Nov. 8, 1995), 60 FR 57473 (publishing the notice and immediate effectiveness of SR–NYSE–95–38).

[27] *See supra* note 10 (noting that the fees and credits concerning equity public agency transactions do not apply to principal transactions by members for their own accounts).

[28] Securities Exchange Act Release No. 36465 (Nov. 8, 1995), 60 FR 57473.

[29] *See* letter from Samuel F. Lek, Chief Executive Officer, Lek, Schoenau & Company, Inc., to Secretary, SEC, dated November 14, 1995 (opposing the monthly equity transaction fee cap); letter from William W. Uchimoto, First Vice President and General Counsel, Phlx, to Jonathan Katz, Secretary, SEC, dated November 27, 1995 (opposing the disparate treatment of competing market maker orders and requesting that the NYSE withdraw that portion of the filing and refile it for notice and action pursuant to Section 19(b)(2) of the Act); letter from David P. Semak, Vice President of Regulation, PSE, to Jonathan Katz, Secretary, SEC, dated December 7, 1995 (opposing the disparate treatment of competing market maker orders and requesting that the NYSE withdraw that portion of the filing and refile it for notice and action pursuant to section 19(b)(2) of the Act).

[30] 15 U.S.C. 78s(b)(1).

[31] 15 U.S.C. 78s(b)(2).

[32] Section 19(b)(2) requires that a notice be published in the Federal Register for the statutory comment period and provides that changes pursuant to this section are not effective until the Commission issues an approval order.

[33] This rule change became effective upon filing with the Commission pursuant to Section 19(b)(3)(A) of the Act.

[34] The effect of this rule change was to require members and member organizations to report competing market maker system orders of 100 to 2,099 shares to the Exchange. The amount of fees due would be $0.0019 per share for all such competing market maker orders executed by NYSE members on the Exchange from January 2, 1996 to the present.

[35] Securities Exchange Act Release No. 36659 (Dec. 29, 1995), 61 FR 432.

[36] Currently, the NYSE waives the equity transaction fees for all SuperDot system orders of 100 to 2,099 shares.

[37] *See supra* notes 4 and 6.

[38] *See supra* note 5.

[39] 15 U.S.C. 78f(b)(4). Section 6(b)(4) requires that the rules of an exchange provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities.

[40] *See* BSE February 21, 1996 Letter, *supra* note 4; PSE March 4, 1996 Letter, *supra* note 4.

[41] 15 U.S.C. 78f(b)(5). Among other things, Section 6(b)(5) requires that the rules of an exchange be designed to promote just and equitable principles of trade, to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. Section 6(b)(5) also requires that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

[42] *See* BSE February 21, 1996 Letter, *supra* note 4; BSE April 23, 1996 Letter, *supra* note 6; CHX March 4, 1996 Letter, *supra* note 4; Phlx February 23, 1996 Letter, *supra* note 4; PSE March 4, 1996 Letter, *supra* note 4.

[43] *See* BSE February 21, 1996 Letter, *supra* note 4.

the public.[44] Therefore, the CHX argues, there is no valid justification or legally sufficient rational basis why nonmember competing market makers should pay more than all other nonmembers for such orders.[45]

Separately, the Phlx contends that competing market makers will be required to subsidize all of the NYSE's other system orders of this size and, therefore, this fee should be cost based.[46]

In its response, the NYSE charges that the commenters fundamentally misread the provisions of the Act dealing with competition in the national market system (''NMS''). The NYSE argues that the proposal does not constitute either an inequitable allocation of fees or unfair discrimination among brokers and dealers because the affected parties are in direct competition with each other. This competition, the Exchange asserts, justifies the disparate treatment in this instance because to require otherwise would obligate the NYSE to subsidize its competitors.

The CHX characterizes the NYSE's logic as specious. The CHX asserts that the proposal does not achieve one of its stated purposes, to avoid subsidizing the NYSE's competitors, because proprietary orders of regional exchange specialists and third market makers that are affiliated with a NYSE member are included in the NYSE's no charge policy. Therefore, the CHX argues that the NYSE's justification is inadequate because the proposal does subsidize some NYSE competitors.[47]

B. Burden on Competition

The commenters also argue that the proposal is inconsistent with Section 6(b)(8)[48] and Section 11A(a)(1)(C)[49] of the Act because it raises the costs of competing market makers without sufficient justification and, therefore, places an unnecessary and inappropriate burden on competition.[50] The commenters contend that raising the costs of competing market makers in this case will harm the depth and liquidity of the market.[51] One commenter also believes that it will reduce price improvement opportunities, impair the ability of competing market makers to perform their required market making functions, and, in general, disrupt the equilibrium of the NMS.[52]

Several commenters also claim the impetus for this filing is similar to a prior American Stock Exchange, Inc. (''Amex'') competing dealer rule proposal that was eventually withdrawn. In analogizing the NYSE proposal to the prior Amex proposal, the commenters claim the NYSE is seeking to implement rules that disadvantage its competition for purely competitive reasons.[53]

The NYSE argues that the proposal does not impose an inappropriate burden on competition because competing market makers already have cost-free access to the NYSE through the Intermarket Trading System (''ITS'').[54] The NYSE characterizes ITS as a carefully-constructed[55] market linkage that has evolved over the past twenty years to successfully balance the goals enumerated in Section 11A(a)(1)(D) of the Act.[56]

By utilizing ITS, the NYSE explains, competing market makers still can lay off their excess positions and interact with trading interest on the NYSE. In support of this argument, the NYSE states that the commenters' ITS commitments executed on the Exchange during the first three months of 1996 accounted for over twenty-one percent of the total share volume reported by the commenters during this time period.

As further support that the filing does not impose an inappropriate burden on competition, the NYSE notes that this proposal seeks to maintain the prior relationship between member proprietary and nonmember competing market maker activities in Exchange-listed securities.[57] The Exchange asserts that although the proposal replaces the credit system with a discount system, it maintains the status quo because the economic effect is unchanged.

Finally, the NYSE argues that the proposed fee for competing market maker orders is lower than the fee structure previously in effect and, therefore, does not impose an inappropriate burden on competition. The NYSE emphasizes that the proposal lowers the fee charged from $0.00265 per share to $0.0019 per share[58] and, in any event, the amount charged is nominal.[59]

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[44] *See* CHX March 4, 1996 Letter, *supra* note 4.

[45] *See* CHX March 4, 1996 Letter, *supra* note 4.

[46] *SEE* Phlx February 23, 1996 Letter, *supra* note 4.

[47] *See* CHX May 6, 1996 Letter, *supra* note 6.

[48] *See* BSE February 21, 1996 Letter, *supra* note 4; BSE April 23, 1996 Letter, *supra* note 6; CHX March 4, 1996 Letter, *supra* note 4; CHX May 6, 1996 Letter, *supra* note 6; Phlx February 23, 1996 Letter, *supra* note 4; PSE March 4, 1996 Letter, *supra* note 4.

[49] *See* BSE February 21, 1996 Letter, *supra* note 4; BSE April 23, 1996 Letter, *supra* note 6; PSE March 4, 1996 Letter, *supra* note 4.

[50] *See* 15 U.S.C. 78f(b)(8) and 78k–1(a)(1)(C). Section 6(b)(8) prohibits the rules of a national securities exchange from imposing any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. In Section 11A(a)(1)(C), Congress found that, among other things, it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to ensure fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets.

[51] *See* CHX March 4, 1996 Letter, *supra* note 4; PSE March 4, 1996 Letter, *supra* note 4.

[52] *See* PSE March 4, 1996 Letter, *supra* note 4.

[53] *See* BSE February 21, 1996 Letter, *supra* note 4; CHX March 4, 1996 Letter, *supra* note 4; Phlx February 23, 1996 Letter, *supra* note 4; Phlx May 3, 1996 Letter, *supra* note 6. In its competing dealer filing, the Amex proposed that orders for a competing dealer would: (1) yield priority and parity to all other off-floor orders, (2) accept parity with orders for an account of an Amex specialist, and (3) be excluded from the Amex's order routing system, the Post Execution Reporting System (''PER''). The Amex subsequently amended this proposal in December 1991, among other things, to: (1) provide that orders for the account of a competing dealer that better the existing market do not have to yield priority and parity to off-floor orders, (2) withdraw the portion of the proposal that would have placed orders for the account of a competing dealer on parity with orders for the account of an Amex specialist, and (3) request that the Commission temporarily defer its consideration of the proposed prohibition of competing dealer access to PER. *See* Securities Exchange Act Release No. 30161 (Jan. 7, 1992), 57 FR 1502 (File No. SR–Amex–90–29). The Amex thereafter withdrew this filing at the request of Commission staff. *See* Division of Market Regulation, SEC, Market 2000, An Examination of Current Equity Market Developments Study III–11 (Jan. 1994) [hereinafter Market 2000] (recommending that the Amex amend or withdraw SR–Amex–90–29).

[54] ITS provides facilities and procedures for: (1) the display of composite quotation information at each participant market so that brokers can readily determine the best available price for a particular security, (2) the execution of orders between broker-dealers at respective ITS market centers, and (3) the coordination of market openings among the linked markets.

Brokers may execute orders in other ITS market centers by entering a ''commitment to trade'' into their ITS computer terminal. Currently, the Amex, the BSE, the Chicago Board Options Exchange, Incorporated, the CHX, The Cincinnati Stock Exchange, the National Association of Securities Dealers, Inc., the NYSE, the Phlx, and the PSE are all ITS participants. *See* Market 2000, *supra* note 53, at Appendix II (providing the history of ITS).

[55] The NYSE notes that, in addition to itself and other markets, all of the commenters were involved in the development of ITS and that this development was supervised by the Commission. *See also* Market 2000, *supra* note 53, at Appendix II.

[56] 15 U.S.C. 78k–1(a)(1)(D) (finding that the linking of all markets will foster efficiency, enhance competition, increase the information available to brokers, dealers, and investors, facilitate the offsetting of investors' orders, and contribute to the best execution of such orders).

[57] According to the prior fee schedule, neither order type was eligible for the NYSE's additional system credit. *See supra* note 10.

[58] Without adjusting for the lost system credit, the NYSE represents this as a reduction of 28%. *See* NYSE April 25, 1996 Letter, *supra* note 5.

[59] The greatest differential exists between a nonmember competing market maker system order of 2,099 shares and another system order of 2,099 shares that qualifies for the NYSE's no charge policy. Under these circumstances, the competing market maker order would incur a charge of $3.99 (2,099 shares * $0.0019 per share), while the other order would incur no fees at all. In underscoring its argument that this fee is nominal, the NYSE points out that for a $30 stock the $3.99 fee would

In commenting further on the proposal, the BSE, the CHX, and the Phlx refute the NYSE's claim that ITS provides adequate access to the NYSE's market.[60] They claim that ITS is too limited in its capabilities. The CHX adds that its specialists choose to ignore free ITS access and pay for access to the NYSE's SuperDot system simply because SuperDot is better;[61] while the BSE asserts that its specialists are forced to use SuperDot because ITS commitments do not have the same status as orders on the NYSE and do not have any standing in the trading crowd.[62]

C. Proposed Order Handling Rules[63]

Finally, the BSE urges the Commission to consider the possible impact this proposal will have in conjunction with the Commission's ''Proposed Limit Order Rule''[64] and ''Proposed Price Improvement Rule.''[65] The BSE is concerned that a NYSE specialist availing itself of the proposed rules' exceptions concerning the immediate delivery of an Order to another market maker or system would be charged a different fee than a BSE specialist doing likewise.

The NYSE did not address this issue in its response.

D. Antitrust Considerations[66]

The Phlx also requests the Commission to consider the possible antitrust implications this proposal presents.[67] The Phlx contends that the NYSE enjoys a ''strategic dominance'' and that the antitrust law's ''essential facility'' doctrine is germane to the Commission's analysis of this proposal. In support of this argument, the Phlx claims the proposal effectively and inappropriately excludes competing market makers equal access to the primary market simply because they are competitors.

The NYSE disputes the Phlx's premise that the NYSE is an essential facility. The NYSE supports its position by asserting that: (1) the NYSE is not a monopoly (as evidenced by the existence of multiple other securities markets in the United States) and (2) competing market makers will continue to have two forms of access to the NYSE's market—''one free and another at near-zero price.''[68]

IV. Discussion

Under Section 19(b)(2) of the Act,[69] the Commission must approve the NYSE's proposed rule change if it finds that the proposed rule change is consistent with the requirements of the Act and the rules thereunder applicable to a national securities exchange. If the Commission is unable to make that finding, it must institute proceedings to consider whether to disapprove the proposed rule change.

The statutory requirements relevant to such a determination are found, for the most part, in Section 6(b) of the Act.[70] That section delineates the purposes the NYSE's rules should be designed to achieve. Those purposes or objectives, which take the form of positive goals, such as investor protection, or prohibitions, such as those against unfair discrimination or inappropriate burdens on competition, are stated in the form of broad and elastic concepts. They afford the Commission considerable discretion to use its judgment and knowledge in determining whether a proposed rule complies with the requirements of the Act.[71] Furthermore, the subsections of Section 6(b)[72] must be read with reference to one another and to other provisions of the Act.[73] Within this legal framework, the Commission must weigh and balance the strengths and weaknesses of a proposed rule, assess the views and arguments of others, and make predictive judgments about the consequences of approving the proposed rule.[74]

With this in mind, and after careful consideration of all of the comments received, the Commission has determined to approve the proposed rule change. For the reasons discussed below, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.

In particular, the Commission finds that the proposal is consistent with the Section 6(b)(4) requirement that the rules of an exchange provide for the equitable allocation of reasonable fees among its members;[75] the Section 6(b)(5)[76] requirements that the rules of an exchange be designed to perfect the national market system, and, in general, to protect investors and the public interest; and not designed to permit unfair discrimination between brokers, dealers, and customers; as well as the Section 6(b)(8)[77] requirement that the rules of an exchange not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

A. The Proposal

The NYSE's original proposal, SR–NYSE–95–38, instituted a discount fee system that excluded orders of nonmember competing market makers from the NYSE's no charge provision for system orders of 100 to 2,099 shares. Instead, these orders would have been subject to a fee of $0.0019 per share.

This modified the NYSE's previous system—a credit fee system. The credit system imposed a charge of $0.00265 per share for the first 5,000 shares on all equity public agency transactions.[78] If such an order was for 100 to 2,099 shares and was placed through the NYSE's CMS, it earned the NYSE member a credit of $0.30 per order. If this also was an Individual or Agency market order, the NYSE member was granted an additional credit of $1.30.[79] Orders executed by members and member organizations for the account of

represent .006% of the $62,970 value of the trade. *See* NYSE April 25, 1996 Letter, *supra* note 5.

[60] *See* BSE May 6, 1996 Letter, *supra* note 6; CHX May 6, 1996 Letter, *supra* note 6; Phlx May 3, 1996 Letter, *supra* note 6.

[61] *See* CHX May 6, 1996 Letter, *supra* note 6.

[62] *See* BSE May 6, 1996 Letter, *supra* note 6.

[63] On October 10, 1995, the Commission proposed two rules and amendments to a rule to improve the handling and execution of customer orders. The Proposed Limit Order Rule, Proposed Rule 11Ac1–4, would require covered market makers to immediately reflect in their bid or offer the price and size of each customer limit order they hold in a covered security at a price that would improve their bid or offer in the security unless an exception applies. The Proposed Price Improvement Rule, Proposed Rule 11Ac1–5, would require each specialist or OTC market maker in a covered security that accepts a customer market order to provide that order with an opportunity for price improvement unless an exception applies. Both of these rules contain an exception for orders that are delivered immediately to a market maker or system that complies with the requirements of the applicable rule with respect to that order. *See* Securities Exchange Act Release No. 36310 (Oct. 10, 1995), 60 FR 52792 (publishing File No. S7–30–95 for comment); Proposed 11Ac1–4(c)(5); Proposed 11Ac1–5(e)(4).

[64] *See* BSE February 21, 1996 Letter, *supra* note 4.

[65] *See* BSE April 23, 1996 Letter, *supra* note 6.

[66] *See infra* notes 101, 102 (discussing the applicability of the antitrust laws and the essential facility doctrine).

[67] *See* Phlx February 23, 1996 Letter, *supra* note 4.

[68] *See* NYSE April 25, 1996 Letter, *supra* note 5.

[69] 15 U.S.C. 78s(b)(2).

[70] 15 U.S.C. 78f(b).

[71] *Bradford National Clearing Corp.* v. *Securities and Exchange Commission*, 590 F.2d 1085 (D.C. Cir. 1978).

[72] 15 U.S.C. 78f(b).

[73] *See* Securities Exchange Act Release No. 17371 (Dec. 12, 1980), 45 FR 83707, 83715–19 (interpreting identical provisions of Section 15A(b)).

[74] *Id.*

[75] 15 U.S.C. 78f(b)(4).

[76] 15 U.S.C. 78f(b)(5).

[77] 15 U.S.C. 78f(b)(8).

[78] *See supra* note 10 (noting that the fees and credits concerning equity public agency transactions do not apply to principal transactions by members for their own accounts).

[79] *See supra* notes 12 and 13 (defining Individual and Agency orders).

a competing market maker, however, were not eligible for the additional system credit.

Prior to the effective date of the discount system, the NYSE suspended the effectiveness of the exclusion concerning competing market maker orders.[80] Publication of the exclusion for public comment provided additional time for the Commission to consider, and interested parties to comment on, that portion of the filing. With this filing, the NYSE seeks approval to implement the discount system as originally filed.

B. Section 6(b)(4)[81]

Several commenters have argued that the proposal violates section 6(b)(4).[82] The Commission disagrees and finds that the proposal constitutes an equitable allocation of a reasonable fee.

The Commission believes the proposed fee is reasonable because it generally is a fee reduction. The Commission notes that the NTSE's new discount system generally grants competing market maker orders a cost savings over the prior credit system.[83] The Commission believes the fee is an equitable allocation within the meaning of Section 6(b)(4) because, although the fee distinguishes between the orders of nonmember competing market makers and all other orders executed on the NYSE, it does not do so in a manner that imposes a significant cost burden on the nonmember competing market maker orders. In addition, the Commission is unable to conclude that the fee is not reasonable because nonmember competing market makers will be able to continue the same level of trading activity on the NYSE as before this fee was implemented, except that it now will be at a lower cost.

The following illustrates this fact:

Shares	Credit System	Discount System	Savings
100	$(0.04)	$0.19	$ − 0.23
400	0.76	0.76	0.00
500	1.03	0.95	0.08
1,000	2.35	1.90	0.45
1,500	3.68	2.85	0.83
2,099	5.26	3.99	1.27

The Commission emphasizes, however, that whether a proposed fee can be deemed an equitable allocation of a reasonable fee depends on the facts and circumstances under which the proposal is being made. In evaluating such a proposal, the Commission necessarily would weigh and balance all of the relevant factors. These may include, among others, whether the proposed fee is an increase or a decrease, who is subject to the fee, the basis for any classification being drawn, the potential impact on competition, and how any disparate treatment will impact the goals of the Act.[84]

C. Section 6(b)(5)[85] *and Section 6(b)(8)*[86]

The commenters also argue that it is inappropriate for the NYSE to exclude competing market maker orders from the NYSE's no charge policy because it will deny the Exchange's competitors effective access to the NYSE's market, harm the depth and liquidity of the market, disrupt the balance of competition in the NMS, and hamper competing market makers' ability to compete.

1. National Market System

The commenters allege that ITS, although providing them with free access to the NYSE, is not an effective substitute for access to SuperDot. In evaluating the role of ITS in the NMS, the Commission recognizes that the design of ITS is limited in scope. ITS is not a complete intermarket linkage.[87] ITS does not provide order-by-order routing of customer orders, a consolidated limit order book, or automated or default based execution systems; it does not guarantee price and time priority. Rather, ITS utilizes communications and technological components of other NMS facilities so that trading interest in various market centers can be identified and accessed. It also provides uniform trading rules governing transactions in exchange-listed securities.[88] These functionalities benefit the markets, broker-dealers, and investors by reducing fragmentation, increasing opportunities to secure the best execution of customer orders, ensuring effective competition among qualified markets, and, in general, furthering the purposes of the NMS established by Congress in Section 11A of the Act.[89]

ITS provides an avenue for competing market makers to lay off their excess positions and interact with trading interest on the NYSE, fee-free. The Commission believes that ITS will continue to provide an alternative means by which competing market makers can access the NYSE. In addition, competing market makers will continue to have access to the NYSE through SuperDot.

Because access to the NYSE will not be more restrictive under the proposed rule change, and because competing market makers can avail themselves of ITS, the Commission does not believe the proposal will harm the depth and liquidity of the market. Moreover, the Commission notes that the depth and liquidity of any particular security is dependent on numerous variables, such as the degree of customer buying and selling interest in the security and the quality and capitalization of the issuer.[90] Hence, the Commission believes it is unlikely that the cost imposed on competing market makers under the NYSE fee schedule will have

[80] *See* (publishing the notice and immediate effectiveness of SR–NYSE–95–46).

[81] *See surpa* note 39 (listing the requirements of Section 6(b)(4)).

[82] 15 U.S.C. 78f(b)(4).

[83] Under most circumstances, the fee imposed on competing market maker orders has been reduced.

[84] Of course, any fee proposal must be found to meet all applicable statutory standards.

[85] *See supra* note 41 (listing the requirements of Section 6(b)(5)).

[86] *See supra* note 50 (listing the requirements of Section 6(b)(8)).

[87] *See* Market 2000, *supra* note 53, at Appendix II–12. The Commission previously has encouraged all ITS participants to continue to improve the system.

[88] *See* 15 U.S.C. 78k–1(a)(1)(D) (finding that the linkage of all markets will foster efficiency, enhance competition, increase the information available to brokers, dealers, and investors, facilitate the offsetting of investors' orders, and contribute to the best execution of such orders).

[89] *See* Market 2000, *supra* note 53, at Appendix II–11.

[90] *See* Market 2000 *supra* note 53, at Study II 8–10 (discussing quote competition between the regional exchanges and the NYSE). *See also* Market 2000, *supra* note 53, at Study II–8 (finding that in 1992 over 92% of the regional exchanges' volume derived from issues traded pursuant to unlisted trading privileges, rather than in issues where the regional exchanges are the primary market).

a significant impact on the willingness of these market makers to contribute to the depth and liquidity of NYSE listed securities.

2. Disparate Treatment of Competing Market Maker Orders [91]

In determining that disparate treatment of competing market makers is not inconsistent with the Act in this instance, the Commission believes three aspects of the proposal are particularly significant. First, the new fee schedule generally represents a fee reduction. Second, the NYSE is attempting to maintain the status quo that existed under the previous fee structure. Third, the parties are competitors in the NMS.

First, as noted previously, this proposal generally reduces the fee heretofore imposed on competing market maker orders.[92] The Commission is unable to conclude that reducing competing market makers' fees on most of their SuperDot system orders will have a significant, negative impact on the competitors' ability to perform their market making functions.

Second, the Commission has due regard for the NYSE's proffered intent to maintain the status quo. The Exchange decided to change from a credit system to a discount system in response to the Commission's regulatory initiatives addressing the practice of payment for order flow, and the NYSE has stated that excluding orders of competing market makers from its no charge policy is intended ''to maintain the current relationship between member proprietary and nonmember market maker activities in Exchange-listed securities.'' [93] Orders of competing market makers were not entitled to the same fee treatment as other orders in the prior fee schedule. This proposal does not alter this result.[94]

Finally, the Commission does not believe that this fee change imposes an unnecessary burden on competition. Fair competition in the NMS does not require free access in all instances to a competitor's systems.[95] Fair competition must take into consideration all of the relevant facts and circumstances. To find otherwise would negate the benefits of belonging to a membership organization. Also, it is important to note that membership carries with it certain duties, responsibilities, and costs not applicable to nonmembers.[96] Thus, in the circumstances presented by this filing, it is not inconsistent with fair competition for the NYSE to charge competing market maker orders a reasonable fee when utilizing systems whose development has been financed by NYSE members.

For all of the above reasons, the Commission finds that the NYSE proposal is consistent with Section 6(b)(5) [97] and Section 6(b)(8) [98] of the Act.

D. Proposed Order Handling Rules [99]

The BSE is concerned that BSE specialists availing themselves of exceptions in the Proposed Limit Order Rule and in the Proposed Price Improvement Rule concerning the immediate delivery of an order to a market maker or system complying with the applicable rule would be charged a different fee than a NYSE member complying with the same exception.[100]

The BSE's comments in this connection are premature inasmuch as the Commission has not taken final action on the proposed rules referred to by the BSE. The Commission notes, however, that the Proposed Limit Order Rule would allow a specialist or market maker to display the limit order in its own quote; execute the limit order; or send the order to another market maker or system that would display the order in conformity with the rule. Thus, a competing market maker would have two alternatives to sending the order to another market or system. Similarly, the Proposed Price Improvement Rule provides market makers with an alternative to sending their orders to another market center.

E. Antitrust Law's Essential Facility Doctrine [101]

The Phlx urges the Commission to apply the antitrust law's essential facility doctrine because, in the Phlx's opinion, the NYSE is an essential facility.[102] The Commission declines to do so in this case because, as noted previously, the NYSE is not denying the use of its facilities to its competitors.[103] Competing market makers still have two forms of access to the NYSE—one free (ITS) and the order at a reduced rate (SuperDot).

In addition, the Commission notes the competitive environment in which

[91] The Commission does not intend this proposal to establish a precedent to permit a primary market to make distinctions in the treatment of orders on its Floor as a means to discriminate unfairly against its competitors. Orders for the account of nonmember competing market makers will continue to be treated in the same way as other Agency orders. *See supra* note 13 (defining Agency order). For example, the proposal does not effect any change in routing to the NYSE market; in the priority such orders receive on the Floor; or in surveillance by the NYSE. Therefore, this proposal is distinguishable from the one proposed by the Amex in SR–Amex–90–29. *See* Securities Exchange Act Release No. 32377 (May 27, 1993), 58 FR 31568 (utilizing similar reasons for distinguishing SR–Amex–90–29 from the NYSE's limitation of its additional system credit).

[92] *See supra* note 83.

[93] *See* NYSE April 25, 1996 Letter, *supra* note 5.

[94] Given that the fee imposed on competing market maker orders is being reduced from its prior level in most instances, the Commission does not believe that a predatory motive is the impetus for this filing. *Contra* Phlx February 23, 1996 Letter, *supra* note 4.

[95] This is especially true in light of the fact that other means of access to the NYSE market exist.

[96] *See* Securities Exchange Act Release No. 32377 (May 27, 1993), 58 FR 31568 (noting that the NYSE Specialist System Charge was used to partially fund the NYSE's credit system).

[97] 15 U.S.C. 78f(b)(5).

[98] 15 U.S.C. 78f(b)(8).

[99] *See supra* note 63 (describing the Commission's proposed order handling rules).

[100] The fifth exception to the Proposed Limit Order Rule applies to any customer limit order ''that is delivered immediately to an exchange or association sponsored system that displays limit orders and complies with the requirements of [the Proposed Limit Order Rule] with respect to that order.'' The fourth exception to the Proposed Price Improvement Rule applies to any customer market order ''that is delivered immediately to another specialist or OTC market maker that complies with the display requirements of [the Proposed Price Improvement Rule] with respect to that order.'' *See* Securities Exchange Act Release No. 36310 (Oct. 10, 1995), 60 FR 52792 (publishing File No. S7–30–95 for comment).

[101] In *Silver* v. *New York Stock Exchange,* the Supreme Court ruled that certain instances of self-regulation that fall within the scope and purposes of the Act could protect an exchange against an antitrust claim. *Silver,* 373 U.S. 341, 360–61 (1963). In *Thill Securities Corporation* v. *New York Stock Exchange,* the U.S. Court of Appeals for the Seventh Circuit interpreted this ruling to allow the securities laws to act as an implied repealer of the antitrust laws, but only to the minimum extent necessary to make the securities laws work. *Thill,* 433 F.2d 264, 268 (7th Cir. 1970), *cert. denied,* 401 U.S. 994 (1971). In determining when such antitrust immunity is applicable, one court explained, ''Where the concededly self-regulatory rule or practice complained of is within the explicit mandate of the Exchange Act and also is actively reviewed by the Commission, that body may and appropriately should itself consider the policies of both the antitrust and the securities laws.'' *Jacobi* v. *Bache & Co., Inc.,* 377 F. Supp. 86, 92 (S.D.N.Y. 1974), *aff'd,* 520 F.2d 1231 (2d Cir. 1975), *cert. denied,* 423 U.S. 1053 (1976).

[102] The essential facility doctrine, also called the ''bottleneck principle,'' requires the owner of a facility that cannot practicably be duplicated by would-be competitors to share this facility on fair terms. *Hecht* v. *Pro-Football, Inc.,* 570 F.2d 982, 992 (D.C. Cir. 1977), *cert. denied,* 436 U.S. 956 (1978). In determining if a facility is ''essential'' under the Sherman Act, courts look to whether ''duplication of the facility would be economically infeasible'' and if ''denial of its use inflicts a severe handicap on potential [or current] market entrants.'' *Twin Laboratories, Inc.* v. *Weider Health & Fitness,* 900 F. 2d 566, 568–69 (2d Cir. 1990) (citing *Hecht*); *MCI Communications Corp.* v. *American Telephone & Telegraph Co.,* 708 F.2d 1081, 1132–33 (7th Cir.) (requiring ''(1) control of the essential facility by a monopolist; (2) a competitor's inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility''), *cert. denied,* 464 U.S. 891 (1983).

[103] In finding that the NYSE is not denying the use of its facilities to its competitors, the Commission does not reach the issue of whether the NYSE is, in fact, an essential facility.

today's market makers operate.[104] For example, the NYSE faces significant competition for orders in NYSE stocks from the regional stock exchanges,[105] third market makers,[106] proprietary trading systems (''PTSs''),[107] and foreign markets.[108] Modern technology has facilitated this competition and should continue to do so in the future.[109]

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[110] that the proposed rule change (SR–NYSE–95–47) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[111]

Margaret H. McFarland

Deputy Secretary

[FR Doc. 96–14590 Filed 6–7–96; 8:45 am]

BILLING CODE 8010–01–M

[104] *See* Market 2000, *supra* note 53, at 6–12 (providing an overview of the intense competition that exists in the U.S. equity market); Market 2000, *supra* note 53, at Exhibit 18 (charting the NYSE's percentage of Consolidated Tape trades in NYSE stocks from 1976 to 1992).

[105] The regional stock exchanges captured 20% of the orders in NYSE stocks during the first six months of 1993. Market 2000, *supra* note 53, at 8.

[106] OTC trading of exchange-listed securities is commonly known as the ''third market.'' In 1989, the third market garnered 3.2% of reported NYSE share volume and 5% of reported trade volume. By 1993, third market volume had more than doubled to 7.4% of reported NYSE reported share volume and 9.3% of reported trade volume. Market 2000, *supra* note 53, at 9.

[107] A PTS is a type of automated trading system that typically is a screen-based system sponsored by broker-dealers. PTSs are not operated as or affiliated with self-regulatory organizations but instead are operated as independent businesses. Participation in these systems may be limited to institutional investors, broker-dealers, specialists, and other market professionals.

Although most PTS volume is in Nasdaq securities, PTSs handled about 1.4% of the volume in NYSE stocks in the first six months of 1993. Market 2000, *supra* note 53, at 8, Study II 12–13.

[108] Although exact numbers are not available, the Commission estimates that foreign market trading in NYSE stocks amounts to approximately seven million shares per day. *See* Market 2000, *supra* note 53, at 10–11.

[109] *See* Market 2000, *supra* note 53, at 8–10 (noting that automated systems allow the regional stock exchanges, third market makers, and PTSs to compete for order flow with the primary markets).

[110] 15 U.S.C. 78s(b)(2).

[111] 17 CFR 200.30–3(a)(12).

DEPARTMENT OF STATE

[Pubic Notice No. 2399]

Notice of Briefing

The Department of State announces the second 1996 briefing on U.S. foreign policy economic sanctions programs to be held on Thursday, July 11, 1995, from 2:00 p.m. until 3:30 p.m., in the State Department Loy Henderson auditorium, 2201 C Street NW., Washington, D.C.

This briefing, a follow-on session to the March 6 briefing hosted by Under Secretary for Economic, Business and Agricultural Affairs Joan Spero, will be hosted by Ambassador Bill Ramsay, Deputy Assistant Secretary for Energy Sanctions and Commodities, who will present an overview of the sanctions regimes overseen by the State Department's Bureau of Economic and Business Affairs. State Department desk officers will be on hand to discuss country-specific sanctions issues following Mr. Ramsay's briefing.

Please Note: Persons intending to attend the July 11 briefing must announce this not later than 48 hours before the briefing, and preferably further in advance, to the Department of State by sending a fax to 202–647–3953 (Office of the Coordinator for Business Affairs). The announcement must include name, company or association name, Social Security or passport number and date of birth. The above includes government and non-government attendees. One of the following valid photo ID's will be required for admittance: U.S. driver's license with picture, passport, U.S. government ID (company ID's are no longer accepted by Diplomatic Security). Enter from the C Street Main Lobby.

Dated: May 22, 1996.

David A. Ruth,

Senior Coordinator for Business Affairs.

[FR Doc. 96–14011 Filed 6–7–96; 8:45 am]

BILLING CODE 4710–07–M

OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE

Notice of Meeting of the Investment and Services Policy Advisory Committee

AGENCY: Office of the United States Trade Representative.

ACTION: Notice that the June 18, 1996 meeting of the Investment and Services Policy Advisory Committee will be held from 10:00 a.m. to 2:00 p.m. The meeting will be closed to the public from 10:00 a.m. to 1:30 p.m. The meeting will be open to the public from 1:30 p.m. to 2:00 p.m.

SUMMARY: The Investment and Services Policy Advisory Committee will hold a meeting on June 18, 1996, from 10:00 a.m. to 2:00 p.m. The meeting will be closed to the public from 10:00 a.m. to 1:30 p.m. The meeting will include a review and discussion of current issues which influence U.S. trade policy. Pursuant to Section 2155(f)(2) of Title 19 of the United States Code, I have determined that this portion of the meeting will be concerned with matters the disclosure of which would seriously compromise the development by the United States Government of trade policy, priorities, negotiating objectives or bargaining positions with respect to the operation of any trade agreement and other matters arising in connection with the development, implementation and administration of the trade policy of the United States. The meeting will be open to the public and press from 1:30 p.m. to 2:00 p.m. when trade policy issues will be discussed. Attendance during this part of the meeting is for observation only. Individuals who are not members of the committee will not be invited to comment.

DATES: The meeting is scheduled for June 18, 1996, unless otherwise notified.

ADDRESSES: The meeting will be held at the Jefferson Hotel at 16th and M Streets, N.W., Washington, D.C., unless otherwise notified.

FOR FURTHER INFORMATION CONTACT: Suzanna Kang, Office of the United States Trade Representative, (202) 395–6120.

Charlene Barshefsky,

Acting United States Trade Representative.

[FR Doc. 96–14464 Filed 6–7–96; 8:45 am]

BILLING CODE 3190–01–M

Identification of Priority Foreign Country Practices; Request for Public Comment

AGENCY: Office of the United States Trade Representative.

ACTION: Request for written submissions from the public.

SUMMARY: Executive Order 12901 of March 3, 1994, as amended by Executive Order 12973 of September 27, 1995, requires the United States Trade Representative (USTR) to review United States trade expansion priorities and to identify priority foreign country practices, the elimination of which is likely to have the most significant potential to increase United States exports, either directly or through the establishment of a beneficial precedent. USTR is requesting written submissions from the public concerning foreign country practices that should be considered by the USTR for this purpose.

DATES: Submissions must be received on or before 12:00 noon on Tuesday, July 2, 1996.

ADDRESSES: 600 17th Street, NW., Washington, D.C. 20508.

FOR FURTHER INFORMATION CONTACT: Questions concerning the filing of submissions should be directed to Sybia