

MEMO# 11630

February 11, 2000

SEC ISSUES ORDERS DIRECTING THE EXCHANGES AND THE NASD TO SUBMIT A DECIMALIZATION IMPLEMENTATION PLAN

1 Securities Exchange Act Release No. 42360 (January 28, 2000). 2 The order states that six months is the maximum time period for phasing in decimal pricing and that after discussions with the industry, the SEC believes that six months provides adequate time for the exchanges and the NASD to make an orderly transition to decimal pricing while responding to changes in the markets that could result from the conversion from fractions to decimals. [11630] February 11, 2000 TO: COMPLIANCE ADVISORY COMMITTEE No. 9-00 RE: SEC ISSUES ORDERS DIRECTING THE EXCHANGES AND THE NASD TO SUBMIT A DECIMALIZATION IMPLEMENTATION PLAN

The Securities and Exchange Commission has issued an order¹ directing the exchanges and the NASD to act jointly in discussing, developing, and submitting to the SEC a plan, no later than 45 days after issuance of the order, to implement decimal pricing beginning no later than July 3, 2000 ("Decimals Implementation Plan"). The order also directs each exchange and the NASD to submit for notice, comment and SEC consideration the rule changes necessary to implement the Decimals Implementation Plan no later than 60 days after the issuance of the order. The order states that in light of the technical and legal issues raised by the conversion to decimal pricing, a coordinated industry effort is necessary to ensure that the markets continue to operate in an efficient, orderly, and fair manner during the conversion process. In particular, the order states that the exchanges and the NASD will need to convert the systems governing the quotation, trading, reporting and surveillance of securities traded on their marketplaces and may need to discuss the market-wide impact of small minimum price variations, such as one penny, on trading rules, such as priority and trade-through rules. While the SEC is not mandating the details of the Decimals Implementation Plan, the plan must provide that decimal pricing of at least some equities (and options on those equities) trading on the exchanges and the NASD will begin no later than July 3, 2000, and decimal pricing of all equities and options will be completed within six months of that date.² If the exchanges and the NASD adopt a phase-in plan for implementing decimal pricing, rather than pricing all equities and options on their markets in decimals on July 3, 2000, the plan must provide specific dates by which each phase will be completed and identify which securities will be priced in decimals during each phase. The Decimals Implementation Plan may fix the minimum increment during the phase-in period, provided that the minimum increment is no greater than five cents for any equity

priced in decimals. The order also states that the SEC believes that the securities industry should study the impact of quoting and trading in increments smaller than a nickel on trading patterns and capacity. Therefore, in the event that the exchanges and the NASD adopt a phase-in plan using a minimum increment greater than a penny, they also should concurrently establish a pilot program that provides for selected securities to be traded in penny increments. Finally, the order states that thirty days after the end of the phase-in period, the exchanges and the NASD must submit (1) a study to the SEC regarding the impact of decimal pricing on trading and capacity, including the impact of the pilot program, and (2) a recommendation regarding the need for uniform minimum increments, if any. The recommendation should discuss whether one uniform minimum increment should be adopted or whether different minimum increments should be applied and the criteria by which the exchanges and the NASD would select securities to be traded in those various minimum increments. Ari Burstein Assistant Counsel Attachment

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