

INFORMATIONAL

OTCBB Trading Halts

SEC Approves Trade Halt Rule For OTCBB;
Effective Date: June 26, 2000

SUGGESTED ROUTING

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- Legal & Compliance
- Operations
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KEY TOPICS

- OTC Bulletin Board
- Trading Halts

Executive Summary

On May 22, 2000, the Securities and Exchange Commission (SEC) approved a rule change that allows The Nasdaq Stock Market, Inc. (The Nasdaq Stock Market®) to impose trading and quotation halts in securities quoted in the OTC Bulletin Board® (OTCBB). Under the rule change, Nasdaq® will halt trading in OTCBB issues in the following three instances:

- the OTCBB security is dually listed on a foreign market or is registered with a foreign regulatory authority and a foreign regulatory authority or market halts trading in the security;
- the OTCBB security is a derivative or component of a Nasdaq or an exchange-listed security and Nasdaq or the exchange halts trading in the underlying security; and
- the OTCBB issuer does not timely provide the NASD with information required by SEC Rule 10b-17.

The rule change goes into effect on June 26, 2000. The rule change is included with this *Notice* in Attachment A.

Questions/Further Information

Questions regarding this rule change can be directed to the following:

For operational issues:

Sheila Dagucon, Vice President,
Nasdaq MarketWatch Department,
at (301) 590-6435;

For general questions about the

OTCBB: Liz Heese, Market Specialist, Nasdaq Trading and Market Services, at (202) 728-8191;

For issues related to Rule 10b-17

halts: Dorothy Kennedy, Director, Nasdaq Market Operations, at (203) 385-6243; or

For legal issues: John Malitzis, Assistant General Counsel, Nasdaq Office of General Counsel, at (202) 728-8245; or Mary Revell, Associate General Counsel, Nasdaq Office of General Counsel, at (202) 728-8203.

Background

The OTCBB is a National Association of Securities Dealers, Inc. (NASD®) system which, pursuant to delegated authority, is operated by The Nasdaq Stock Market. While Nasdaq has authority to halt trading in Nasdaq-listed securities and exchange-listed securities traded over-the-counter (*i.e.*, in the third market), until now Nasdaq has not had authority to impose trading or quotation halts in OTCBB securities. Additionally, unlike the Nasdaq market, there is no listing agreement between Nasdaq and OTCBB issuers, and thus Nasdaq has not had the ability to compel such issuers to disclose information. Accordingly, it was difficult for Nasdaq to unilaterally impose halts in the OTCBB since, in most cases, information from the issuer is necessary to assess the situation and determine if a halt and/or resumption of trading is appropriate.¹

Trading Halts

In light of this, on May 22, 2000, the SEC approved NASD Rule 6545 which permits Nasdaq to halt trading and quotations in OTCBB issues in three instances:

1) **Foreign Regulatory Authority Halts.** The OTCBB security is dually listed on a foreign market or is registered with a foreign

regulatory authority and a foreign regulatory authority or market halts trading in the security;

2) OTCBB Derivative Securities

Halts. The OTCBB security is a derivative or component of a Nasdaq or an exchange-listed security and Nasdaq or the exchange halts trading in the underlying security; and

3) Failure To Comply With SEC

Rule 10b-17 Halts. The OTCBB issuer does not timely provide the NASD with information required by SEC Rule 10b-17.

Foreign Regulatory Authority Halts

Nasdaq may impose trading and quotation halts in OTCBB eligible securities when a foreign market or regulatory authority has imposed a halt in the security in its market for regulatory reasons. Under the new rule, Nasdaq may halt an OTCBB security or OTCBB American Depositary Receipt (ADR) when a foreign market on which the OTCBB issue is also traded, or a regulatory authority which has oversight authority for the OTCBB security, halts trading for “regulatory” reasons in the security or the security underlying the ADR. (Nasdaq currently has similar trading-halt authority for Nasdaq-listed securities.²⁾

Specifically, upon receipt of information from a foreign securities market on which the OTCBB security, or the security underlying the OTCBB ADR, is listed or registered or from a regulatory authority overseeing such issuer, exchange, or market, the Nasdaq StockWatch section will evaluate the information (generally a trade-halt order issued by the foreign market or regulatory authority) and determine whether a halt in the

OTCBB security is appropriate. Nasdaq will impose such a halt only when the foreign market or regulatory authority has imposed its halt because of potential fraudulent conduct or other public interest concerns. Nasdaq will not impose a halt if the foreign entity's halt is based on the dissemination of material news, an issuer's failure to meet regulatory filing requirements imposed by a foreign market or regulatory authority, or for operational reasons (e.g., order imbalance in the foreign market).³

OTCBB Derivative Securities Halts

Under the rule change, Nasdaq will have authority to halt trading and quotations in OTCBB securities when an OTCBB security is a derivative or component of a Nasdaq or exchange-listed security and the exchange or Nasdaq imposes a trading halt in the underlying listed security. Thus, in instances where Nasdaq or an exchange halts trading in a security listed on that market, Nasdaq will halt trading in an OTCBB issue that is a derivative or component of the security. This is because the trading price of the OTCBB derivative may be dependent on the price of the underlying Nasdaq or exchange-listed security, and thus it may be difficult to accurately price the OTCBB derivative security when there is no current pricing information on the underlying Nasdaq or exchange-listed security.

Failure To Comply With SEC Rule 10b-17 Halts

Finally, Nasdaq will have authority to halt quotations and trading in an OTCBB security if the issuer fails to comply with the requirements of SEC Rule 10b-17 (Rule 10b-17) regarding untimely announcements of record dates.

Rule 10b-17 generally requires issuers to timely give the NASD information relating to:

- (1) a dividend or other distribution in cash or in kind;
- (2) a stock split or reverse split; and
- (3) a rights or other subscription offering.

Under Rule 10b-17, the issuer is required to provide this information to the NASD no later than 10 days prior to the record date or, in case of a rights subscription or other offering if such 10 days advance notice is not practical, on or before the record date.

For both Nasdaq-listed and OTCBB securities, Nasdaq publishes the record date of the action and the ex-date in its “Daily List” on Nasdaq Web Sites. (The OTCBB Daily List is published on www.otcbb.com; the Nasdaq Daily List is available on www.nasdaqtrader.com.) This provides information to broker/dealers, clearing agencies, and the public regarding the record date and settlement of such trades. For Nasdaq-listed securities, if an issuer does not provide the information in a timely manner, Nasdaq may request the 10b-17 information from the issuer and halt trading pending receipt of such information.⁴ Nasdaq may then issue a Uniform Practice Code (UPC) notice informing members of the status of the record date and underlying event in order to clarify any confusion in the marketplace regarding the pricing or settlement of these trades.

While OTCBB issuers are also required to timely give the NASD information prescribed by Rule 10b-17, until now Nasdaq has not had authority to institute trading

halts in an OTCBB security when such information has not been timely provided. If an OTCBB issuer fails to provide the NASD with the information required by Rule 10b-17, such as a stock split or the payment of a cash dividend, this may cause confusion in the marketplace because the information may be disseminated unevenly. Thus, some market participants may become aware of the information (which impacts the pricing of the security) and adjust their quotes and/or trading activity accordingly, while others may be unaware of this information and not adjust their quotes and/or trading activity. This, in turn, may result in anomalous pricing. With the new rule, when these situations occur, Nasdaq will have the ability to halt trading, gather information, and issue a clarifying UPC notice to members. Nasdaq believes this will minimize the potential for disorderly markets and investor confusion.

Thus, if Nasdaq initiates a trade and quotation halt in an OTCBB issue, it would be inconsistent with NASD Rule 6545 for a member to continue to quote and/or trade that security through the NQB Pink

Sheets or an electronic communications network while the halt is still in effect.

Dissemination Of Trade And Quote Halt Information

For all of the trade and quote halts described above, as well as for SEC imposed halts of OTCBB issuers, Nasdaq will notify market participants and the public of halts through the OTCBB Web Site, www.otcbb.com. Nasdaq will notify market data vendors of halts via an administrative message on the Level 1 Service, which is currently used to disseminate all OTCBB quotation information (see Vendor Alert No. 2000-07).

If Nasdaq issues a trade and quotation halt for an OTCBB security, the member may not quote and/or trade the halted security through any quotation medium which includes:

- **any system of general circulation to broker/dealers that regularly disseminates quotations of identified broker/dealers; or**

- **publication, alternative trading system, or other device that is used by broker/dealers to disseminate quotations to others.**

An OTCBB halt will be lifted if Nasdaq determines the basis of the halt no longer exists or upon the passage of five trading days, whichever occurs first.⁵ If a stock is halted for five days and then lifted, Market Makers will then be required to fulfill their obligations under SEC Rule 15c2-11 prior to initiating a priced or unpriced quotation in the security.⁶

Beginning June 26, 2000, market participants can receive automated notification of OTCBB trade halts and resumptions via e-mail from the OTCBB Web Site. To subscribe to trade halt notifications, from the homepage at www.otcbb.com, click on the e-mail button and create an e-mail profile, then check the "Trade Halts" box under Subscriptions. If a market participant already has an e-mail profile, the market participant can access its profile and then update the Subscription list to receive this information.

ATTACHMENT A

Text Of Amendments

*(Note: New language is underlined.
Deletions are bracketed.)*

Rule 6545. Trading and Quotation Halt in OTCBB-Eligible Securities

(a) Authority for Initiating a Trading and Quotation Halt

In circumstances in which it is necessary to protect investors and the public interest, Nasdaq may direct members, pursuant to the procedures set forth in paragraph (b), to halt trading and quotations in the over-the-counter ("OTC") market of a security or an American Depositary Receipt ("ADR") that is included in the OTC Bulletin Board ("OTCBB") if:

(1) the OTCBB security or the security underlying the OTCBB ADR is listed on or registered with a foreign securities exchange or market, and the foreign securities exchange, market, or regulatory authority overseeing such issuer, exchange, or market, halts trading in such security for regulatory reasons because of public interest concerns ("Foreign Regulatory Halt"); provided, however, that Nasdaq will not impose a trading and quotation halt if the Foreign Regulatory Halt was imposed solely for material news, a regulatory filing deficiency, or operational reasons; or

(2) the OTCBB security or the security underlying the OTCBB ADR is a derivative or component of a security listed on or registered with a national securities exchange, The Nasdaq

Stock Market, or foreign securities exchange or market ("listed security") and the national securities exchange, The Nasdaq Stock Market, or foreign securities exchange or market, imposes a trading halt in the listed security.

(3) the issuer of the OTCBB security or the security underlying the OTCBB ADR fails to comply with the requirements of SEC Rule 10b-17 regarding Untimely Announcements of Record Dates.

(b) Procedure for Initiating a Trading and Quotation Halt

(1) When a halt is initiated under subparagraph (a)(1) of this rule, upon receipt of information from a foreign securities exchange or market on which the OTCBB security or the security underlying the OTCBB ADR is listed or registered, or from a regulatory authority overseeing such issuer, exchange, or market, Nasdaq will promptly evaluate the information and determine whether a trading and quotation halt in the OTCBB security is appropriate.

(2) Should Nasdaq determine that a basis exists under this rule for initiating a trading and quotation halt, the commencement of the trading and quotation halt will be effective simultaneous with the issuance of appropriate public notice.

(3) Trading and quotations in the OTC market may resume when Nasdaq determines that the basis for the halt no longer exists, or when five business days have elapsed from the date Nasdaq initiated the trading and quotation halt in the security,

whichever occurs first. Nasdaq shall disseminate appropriate public notice that the trading and quotation halt is no longer in effect.

(c) Violation of OTCBB Trading and Quotation Halt Rule

If a security is subject to a trading and quotation halt initiated pursuant to this rule, it shall be deemed conduct inconsistent with just and equitable principles of trade and a violation of Rule 2110 for a member:

(i) to effect, directly or indirectly, a trade in such security; or

(ii) to publish a quotation, a priced bid and/or offer, an unpriced indication of interest (including "bid wanted" and "offer wanted" indications), or a bid or offer accompanied by a modifier to reflect unsolicited customer interest, in any quotation medium. For purposes of this rule, "quotation medium" shall mean any: system of general circulation to brokers or dealers that regularly disseminates quotations of identified brokers or dealers; or publication, alternative trading system or other device that is used by brokers or dealers to disseminate quotations to others.

Plan Of Allocation And Delegation Of Functions By NASD To Subsidiaries

I - III. No Change

IV. Stockwatch

The Stockwatch section handles the trading halt functions for The Nasdaq Stock Market securities [and], exchange-listed securities traded in the over-the-counter market (i.e., the Third Market), and

securities quoted in the Over-the-Counter Bulletin Board. Review of all questionable market activity, possible rule infractions or any other matters that require any type of investigative or regulatory follow-up will be referred to and conducted by NASD Regulation, which will assume sole responsibility for the matter until resolution. This responsibility will include examinations, investigations, document requests, and any enforcement actions that NASD Regulation may deem necessary. NASD Regulation staff at all times will have access to all records and files of the Stockwatch function.

Endnotes

¹Under Section 12(k) of the Act, the SEC may impose trading suspensions in the U.S. securities markets. Additionally, NASD Rule 3340 prohibits members from trading any security as to which a trading halt is in effect.

²See NASD Rule 4210(a)(4).

³Nasdaq does not have authority to halt trading for material news because Nasdaq does not have a formal listing agreement with OTCBB issuers, and thus cannot compel the full disclosure and dissemination of material news. Additionally, Nasdaq does not have authority to halt trading if an OTCBB issuer fails to meet filing/disclosure requirements imposed by a foreign regulatory authority or market, because Nasdaq would, in essence, be importing filing obligations of a foreign regulatory authority on OTCBB issuers when such requirements may not currently exist in the United States for such issuers. Lastly, Nasdaq will not halt trading based on a foreign exchange's operational halt, such as an order imbalance, because Nasdaq generally does not halt for operational reasons.

⁴See NASD Rule 4210(a)(5).

⁵Of course, if an issuer failed to meet the eligibility requirements contained in NASD Rule 6530, which impose certain regulatory filing requirements for securities to be included in the OTCBB, the security would be ineligible for quotation on the OTCBB.

⁶That is, if Nasdaq directs all members to cease quoting a security for more than five days, pursuant to NASD Rule 6740 and SEC Rule 15c2-11, members shall be required to file a Form 211 prior to the resumption of quotations in the OTCBB. The NASD and Nasdaq note that the SEC recently issued for comment a re-proposal of amendments to SEC Rule 15c2-11. See Release 34-41110 (Feb. 25, 1999). The NASD and Nasdaq will monitor developments regarding SEC Rule 15c2-11 and plan to make any necessary changes to conform the rules proposed in this filing with any changes to SEC Rule 15c2-11.

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