

6.64, Commentary .03(c)–(d) to replace fractional references with decimal references. The Exchange is also proposing to amend PCX Rule 6.47(a)(2) and (b)(2), governing non-facilitation crosses, to require floor brokers to bid above the highest bid or below the lowest offer by at least the MPV before crossing orders.

Finally, the PCX proposes to adopt new Rule 6.72 to explicitly state and give effect to the minimum price increments for options mandated by the Plan. Thus, to the extent an option class is pricing in decimals, the MPVs would be as follows: For options quoting under \$3 a contract, the MPV would be \$.05; and for options quoted at \$3 a contract or greater, the MPV would be \$.10.<sup>10</sup> This rule would replace current Rule 6.72, which requires bids and offers above \$3 to be expressed in eighths of the one dollar and bids and offers below \$3 to be expressed in sixteenths of one dollar.

## 2. Statutory Basis

The PCX believes that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.<sup>11</sup> In particular, the PCX believes that the proposed rule change is consistent with Section 6(b)(5)<sup>12</sup> in that it is designed to promote just and equitable principles of trade, to remove impediments to and 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.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The PCX does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

<sup>10</sup> The Plan contemplates that the options exchanges may wish to consider a pilot program for one-cent minimum price variations for quoting in a limited number of options ("Penny Pilot") at some point in the implementation process. The Commission expects that, before implementing a Penny Pilot, the options exchanges will carefully coordinate on such issues as the selection and number of options to be included in the pilot to ensure the continued orderly operation of the markets and clearing organizations. In particular, the Commission expects that the options exchanges will consult with the Commission regarding the impact on market-wide capacity. Before implementing a Penny Pilot, each options exchange should also submit appropriate rule filings to the Commission under Section 19(b) of the Exchange Act.

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

The Exchange did not solicit or receive written comments on the proposed rule change.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate,<sup>13</sup> it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>14</sup> and Rule 19b-4(f)(6)<sup>15</sup> thereunder. At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

The PCX has requested that the Commission accelerate the operative date. The Commission believes that it is consistent with the protection of investors and the public interest and therefore finds good cause to designate the proposal to become immediately operative upon filing. Acceleration of the operative date will ensure that the PCX is able to operate in accordance with the terms and conditions of the Plan. For these reasons, the Commission finds good cause to designate that the proposal, as amended, become operative immediately upon filing.<sup>16</sup>

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent

<sup>13</sup> The Exchange requested the Commission to waive 5 day pre-filing notice requirement and the 30-day operative period.

<sup>14</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>15</sup> 17 CFR 240.19-4(f)(6).

<sup>16</sup> For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of PCX. All submissions should refer to the File No. SR-PCX-00-23 and should be submitted by October 26, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>17</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43384; File No. SR-PCX-00-31]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Pacific Exchange, Inc. Relating to PACEX Reports for Options Order Flow Providers**

September 29, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 18, 2000, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the PCX. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The PCX proposes to begin furnishing Pacific Exchange Customer Execution ("PACEX") Reports to its order flow providers on a daily basis. PACEX Reports are designed to provide objective data on option order executions so that PCX order flow

<sup>17</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

providers can assess the quality of the executions they receive on the PCX. The text of the proposed rule change is available at the principal offices of the PCX.

## II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the PCX included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The PCX has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of the statements.

### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

The Exchange is adopting a new procedure to provide PCX order flow providers with objective data so that they can assess the quality of the executions they receive on their option orders at the PCX.<sup>3</sup> This rule filing is intended to provide a description of the data to be furnished and to provide a general summary of the PCX's electronic systems involved in transmitting and executing option orders.

#### 1. Pacific Exchange Customer Execution Reports

The PCX intends to begin furnishing PACEX Reports to its order flow providers on a daily basis. The PACEX Reports will provide objective data on the quality of execution that order flow providers receive at the PCX. Specifically, the Reports will include statistical information on:

- Price Improvement—this shows the number of trades and option contracts receiving improved pricing on the PCX; and
- Turnaround Time—this shows the time it took to execute a given customer's order on the PCX.

PACEX Reports provide data on all option orders routed to the PCX

<sup>3</sup> The PCX recently adopted a new fee on market makers' transactions in designated equity option issues. The funds are made available to Lead Market Makers, who may use the funds to pay order flow providers for their options order flow. In publishing the PCX's proposed rule change, the Commission stated its concerns that brokers who are paid to send their customers' orders to one exchange have a conflict of interest that may reduce their commitment to the duty they owe the customers to obtain the best execution available. See Securities Exchange Act Release No. 43290 (Sept. 13, 2000), 65 FR 57213 (Sept. 21, 2000).

electronically that remain in an electronic environment. This includes all orders sent through the member firm interface and executed automatically via an automatic execution system ("Auto-Ex"), as well as all option orders routed to a floor broker hand-held terminal, executed by open outcry, and reported electronically.

The Exchange will provide PACEX Reports to order flow providers on a daily basis, whether electronically or in "hard" copy. Upon request, the Exchange will also send the raw data from the Reports to order flow providers so that they may analyze the data in a manner that suits their own requirements.

*a. Price Improvement Statistics.* PACEX Reports show the dollar amount by which order flow providers improved upon the PCX's prevailing best bid or offer ("BBO") in executing their orders at the PCX. Specifically, PACEX Reports provide data on price improvement for each of the following four classifications: (1) Orders executed via Auto-Ex; (2) orders executed by a hand-held terminal; (3) market orders; and (4) marketable limit orders. Within each of these four categories, the PACEX Reports show the percentage of trades that were executed at prices: (1) where the PCX improved the national best bid or offer ("NBBO"); (2) where the PCX set the NBBO; (3) where the PCX matched the NBBO; (4) where the NBBO was set by another market; and (5) where the PCX was the BBO. With regard to category (5), where the PCX was the BBO, the Reports show the amount by which an execution via a hand-held terminal was less favorable than the then-prevailing NBBO. The Reports do not cover orders that were executed during the opening rotation—whether by automated opening rotation or manually—or during a "fast market," as described in PCX Rule 6.28.

PACEX Reports also provide summary information with respect to: (1) Orders executed via Auto-Ex; (2) orders executed by a hand-held terminal; (3) market orders; and (4) marketable limit orders. The Report shows, for each classification, the aggregate dollar amount that the customer saved per contract, the average trade size (in numbers of option contracts), and the average turnaround time during a specific time period.

*b. Details on Turnaround Time.* Turnaround time shows how quickly orders were executed on the PCX. The Report provides data on turnaround time for each of the following four classifications: (1) Orders executed via Auto-Ex; (2) orders received and reported by a hand-held terminal; (3)

market orders; and (4) marketable limit orders. PACEX shows within each of these four categories the percentage of trades that were executed within: (a) 0 to 1 seconds; (b) 1 to 5 seconds; (c) 5 to 15 seconds; (d) 15 to 60 seconds; (e) 1 minute to 3 minutes; (f) 3 to 10 minutes; (g) 10 to 15 minutes; and (h) 15 to 30 minutes.

For each of these eight time frames, PACEX Reports also show the percentage of trades that were executed during the regular session and the percentage of trades that were executed during the opening session, *i.e.*, during the opening rotation, which may include executions during the Automated Opening Rotation or during a manual opening rotation.

#### 2. PCX Electronic Trading System

*a. POETS.* The Pacific Options Exchange Trading System ("POETS") is the PCX's automated options trading system, which includes an options routing system, an automatic execution system ("Auto-Ex"), an on-line limit order book system, and an automatic market quote update system. Option orders may be sent to POETS via the Exchange's Member Firm Interface ("MFI"). Market and marketable limit orders that are sent through the MFI first check the limit order book for an eligible contra side.<sup>4</sup> Any unfilled portion of an inbound order will be executed by Auto-Ex, subject to the maximum Auto-Ex size parameters. Non-marketable limit orders may be directed to the limit order book either electronically or manually, subject to established order type and maximum size parameters. Prior to the opening, market orders may be directed to the limit order book so that they may participate in the Automated Opening Rotation. Orders in the limit order book executed in strict price/time priority sequence.

*b. Auto-Ex.* Market and marketable limit orders sent through the MFI will be executed by Auto-Ex if they meet the order type and size requirements designated by the Exchange. Orders executed on Auto-Ex receive the PCX's disseminated market price or better. Pursuant to PCX Rule 6.87, Lead Market Makers ("LMMs") may set Auto-Ex to provide automatic price improvement when the national best bid or offer ("NBBO") is better than the PCX's BBO by one trading increment. In addition, LMMs may set Auto-Ex to execute inbound orders at the NBBO price regardless of whether it is only one trading increment better than the PCX's

<sup>4</sup> The Exchange notes that this procedure has been in effect since the inception of POETS in 1989.

BBO, *i.e.*, orders may be executed at prices that may be multiple trading increments better than the PCX's then-prevailing BBO. Furthermore, LMMs may execute improved prices regardless of whether the NBBO is locked or crossed. Auto-Ex prevents inbound orders from being executed at prices inferior to the NBBO. Pursuant to PCX Rule 6.87, only non-broker-dealer customer orders are eligible to be executed by Auto-Ex. The PCX designates the eligible order size, which may be between 20 and 50 option contracts, on an issue-by-issue basis.

*c. Hand-Held Terminals.* Member firms may electronically route orders to the PCX via the floor broker hand-held terminal system pursuant to PCX Rule 6.88. The system allows member firms to route their orders directly to POETS, to a member firm booth on the trading floor, or to a floor broker who is operating a hand-held terminal located in a trading crowd (or elsewhere) on the options floor. Accordingly, orders sent through MFI may be transmitted to a floor broker almost instantaneously for immediate representation in the trading crowd. In the event that option prices have changed to make an order immediately executable, the floor broker can submit the order to POETS for automatic execution (subject to the Exchange's order size requirements). The Exchange notes that the Report uses an extreme measurement standard—the NBBO at the time an order reaches the Exchange. Consequently, the Exchange believes that the reporting process may be subject to some positive or negative price movement. This will occur, for example, if there are changes in the price of the underlying security or there are other orders reaching the trading crowd between the time the original order reaches the trading floor and the time it is executed.

*d. AOR.* Option orders executed at the opening of trading are eligible for execution via the Exchange's Automated Opening Rotation ("AOR"). The AOR permits the Exchange to establish electronically, for eligible option series, a single price opening for executing eligible market and marketable limit orders in the POETS system. Under AOR, various series in an option issue may be opened simultaneously, so that orders in POETS in that issue are executed within seconds. Once the market in an underlying stock has opened, the PCX can open the market in the overlying option almost simultaneously. AOR also allows automated openings when trading in an issue has been halted and then reopened.

The PCX represents that the PACEX Reporting program is designed to provide member firms with greater assurance that they have acted in a manner consistent with the fulfillment of their duty of best execution when they direct orders to the PCX. Accordingly, the Exchange believes that the proposed rule change is consistent with and in furtherance of the objectives of the Act, including specifically Section 6(b)(5) thereof,<sup>5</sup> which requires that the rules of exchanges promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

#### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

#### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

No written comments were solicited or received with respect to the proposed rule change.

#### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Because the PCX has designated this proposed rule change as constituting a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of existing Exchange rules and procedures, it has become effective pursuant to Section 19(b)(3)(A)(i) of the Act<sup>6</sup> and Rule 19b-4(f)(1) thereunder.<sup>7</sup> At any time within 60 days of the filing of this proposed rule change, the Commission may summarily abrogate the rule change if it appears to the Commission that the action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange

Commission, 450 Fifth Street, N.W., Washington, D.C. 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written Communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing will also be available for inspection and copying at the principal office of the PCX. All submissions should refer to File No. SR-PCX-00-31 and should be submitted by October 26, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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#### **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-43376; File No. SR-Phlx-00-79]

#### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to the Prohibition on the Entry of Certain Electronically Generated Orders into the Exchange's AUTOM System**

September 28, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 15, 2000, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comment on the proposed rule change.

<sup>5</sup> 15 U.S.C. 78f(b)(5).

<sup>6</sup> 15 U.S.C. 78s(b)(3)(A)(i).

<sup>7</sup> 17 CFR 240.19b-4(f)(1).

<sup>8</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.