

transactions, to remove impediments 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 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 either solicited or received.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) By order approve such proposed rule change, or
- (B) Institute proceedings to determine whether the proposed rule change should be disapproved.

### 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 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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No.

SR-BSE-00-12 and should be submitted by December 4, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>5</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43508; File No. SR-ISE-00-09]

### Self Regulatory Organizations; Notice of Filing of Proposed Rule Change by the International Securities Exchange LLC Relating to Chinese Wall Procedures

November 2, 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 12, 2000, the International Securities Exchange LLC ("ISE" 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 Exchange. 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 Exchange is proposing to amend ISE Rule 810 relating to Chinese Wall procedures. Proposed new language is *italicized*.

#### 810. Limitations on Dealings

(a) General Rule. A market maker on the Exchange may engage in Other Business Activities, or it may be affiliated with a broker-dealer that engages in Other Business Activities, only if there is a Chinese Wall between the market making activities and the Other Business Activities. "Other Business Activities" means:<sup>3</sup>

- (1) conducting an investment or banking or public securities business;
- (2) making markets in the stocks underlying the options in which it makes markets; or

<sup>5</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.

<sup>3</sup> The ISE corrected a typographical error that appeared in the proposed rule language. Telephone conversation between Michael J. Simon, Senior Vice President and General Counsel, ISE, Katherine A. England, Assistant Director, and Susie Cho, Attorney, Division of Market Regulation, Commission, October 31, 2000.

(3) functioning as an Electronic Access Member.

(b)-(e) No changes.

(b) *Exception to Chinese Wall Requirement.* A market maker shall be exempt from paragraph (a)(3) of this Rule to the extent the market maker complies with the following conditions:

(1) such member functions as an Electronic Access Member solely in options classes (i) contained in Groups to which the member is not appointed as a market maker pursuant to Rule 802 or (ii) in which the member is prohibited from acting as a market maker pursuant to regulatory requirements; and

(2) the member enters orders as an Electronic Access Member only for (i) the proprietary account of the member or (ii) the account of entities that are affiliated with the member.

### 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 Exchange 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 Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

##### 1. Purpose

ISE Rule 810 requires that ISE market makers erect a "Chinese Wall" between their market making activity and certain other business activities, including their trading as an Electronic Access Member ("EAM"). The wall is intended to prevent any real-time communication between the various business lines. The ISE believes that this is especially critical to the integrity of the ISE market with respect to EAM activities. Without the wall, a trader entering an order as an EAM could potentially inform the person making markets about the pending order. The market maker could then, based on this knowledge, move its quotation either (i) to "intercept" an order against which the firm wants to trade, or (ii) to avoid an order against which it does not want to trade. The Exchange adopted ISE Rule 810 because such behavior would be inconsistent with the agency auction market structure of the Exchange.

The ISE believes that although ISE Rule 810 generally has worked well, its broad restrictions limit the ability of

certain market makers to send proprietary order flow to the ISE in options outside of their assigned groups of options ("bins").<sup>4</sup> In particular, many market makers do not have the facilities to establish a "Chinese Wall", which requires physical separation of functions (generally on separate floors), between their proprietary traders and individuals performing ISE market making activities. The ISE notes that several of its market maker members do a significant amount of proprietary trading.

The ISE represents that the purpose of the proposed rule change is to ease ISE Rule 810 to allow members to conduct proprietary trading in the same physical space as their market making activities, but only: (i) in options that are not within their market making assignments or (ii) in options which, pursuant to regulatory requirements, the member is prohibited from making markets. This latter provision is intended to apply to market makers that are specialists in the underlying stock on the New York Stock Exchange, Inc. ("NYSE"), whose rules limit the options trading of specialists and affiliated firms to "hedging activities," thus prohibiting them from making markets in options.<sup>5</sup> In addition, the proposed rule change would permit only proprietary trading without the Chinese Wall and would not permit the market maker to enter agency orders (except with respect to proprietary orders for its affiliates) without complying with the full restrictions of ISE Rule 810.

In these narrow circumstances, the Exchange does not believe that there is the potential for the type of harm against which ISE Rule 810 is intended to protect. Since the member will not be making markets in the stocks in which they are engaging in proprietary trading, there is no opportunity for using the dual roles either to manipulate the market or take unfair advantage of market information. Thus, the ISE believes that relaxing this rule will help attract proprietary order flow to the ISE, without any adverse regulatory implications.

<sup>4</sup> The ISE assigns market makers to bins of options. There are 10 bins, and each bin has one Primary Market Maker ("PMM") and up to 10 Competitive Market Makers (CMM) assigned to each.

<sup>5</sup> See NYSE Rule 105. This applies solely to CMMs. Because CMMs are required to provide continuous quotes in only 60 percent of the options in a bin, it is possible that a CMM could be assigned a bin in which it is not permitted to make markets in certain options classes. Such a CMM simply would not quote in these "restricted" options. PMMs must provide continuous quotes in all options in a bin and thus were not assigned bins where these regulatory restrictions apply.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>6</sup> in general, and furthers the objectives of Section 6(b)(5)<sup>7</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for 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 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

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such long period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

- (A) by order approve such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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 amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-ISE-00-09 and should be submitted by December 4, 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. 34-43509; File No. SR-PCX-00-12]

### Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Pacific Exchange, Inc. Relating to Disciplinary Jurisdiction of the Ethics and Business Conduct Committee

November 2, 2000.

## I. Introduction

On March 26, 2000, the Pacific Exchange, Inc. ("PCX" or "Exchange") submitted to the Securities and Exchange Commission ("Commission" or "SEC") pursuant to Section 19(b)(1) of Securities Exchange Act 1934 ("Act")<sup>1</sup> Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change relating to the disciplinary jurisdiction of the Ethics and Business Conduct Committee ("EBCC"). On September 12, 2000, the PCX filed Amendment No. 1 to the proposed rule change.<sup>3</sup>

The proposed rule change, including Amendment No. 1, was published for comment in the **Federal Register** on September 27, 2000.<sup>4</sup> No comments were received on the proposal. This order approves the proposal.

## II. Description of Proposal

In its proposed rule change, the Exchange seeks to broaden the

<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.

<sup>3</sup> See Letter from Cindy L. Sink, Senior Attorney, Regulatory Policy, PCX, to Jennifer L. Colihan, Attorney, Division of Market Regulation, Commission, dated September 11, 2000 ("Amendment No. 1").

<sup>4</sup> See Securities Exchange Act Release No. 43312 (September 20, 2000), 65 FR 58139.