

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

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43516; File No. SR-Amex-95-45]

Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 1 and 2 to the Proposed Rule Change by the American Stock Exchange LLC Relating to the Maximum Size of Option Orders That May Be Executed Automatically

November 3, 2000.

I. Introduction

On October 25, 1999, the American Stock Exchange LLC ("Amex" or "Exchange") filed with 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 amending its rules regarding the automatic execution of options orders to increase the maximum number of contracts that may be designated for automatic execution from fifty contracts to seventy-five contracts. Notice of the proposal was published in the **Federal Register** on June 21, 2000.³ The Commission received no comments on the proposal. On November 1, 2000, the Exchange submitted Amendment No. 1 to the proposal.⁴ On November 3, 2000, the Exchange submitted Amendment No. 2 to the proposal.⁵ This order

approves the proposal and grants accelerated approval of Amendment Nos. 1 and 2.

II. Description of the Proposal

The Exchange's AUTO-EX system automatically executes public customer market and marketable limit orders in options at the best bid or offer displayed at the time the order is entered into the order is entered into the Amex Order File ("AOF"). Generally, public customer market and marketable limit orders for up to fifty options contracts may be automatically executed through the Exchange's AUTO-EX system.⁶ Recently, AOF, which handles limit orders routed to the specialist's book as well as those orders routed to AUTO-EX, was increased to allow for the entry of orders of up to 250 option contracts.⁷ Because AUTO-EX is only allowed to execute equity option orders and index orders of up to fifty contracts, any market and marketable limit orders for between fifty and 250 option contracts are generally routed by the AOF to the specialist's book.

The Exchange proposes to increase the maximum AUTO-EX order size eligibility for equity and index option contracts orders from fifty contracts to seventy-five contracts.⁸ The proposed increase in permissible order size will be implemented on a case-by-case basis for an individual option class or for all option classes when two floor governors or senior floor officials deem such an increase appropriate.

The Exchange represents that it has sufficient systems capacity to accommodate implementation of the proposed increase in permissible order size and that AUTO-EX has been extremely successful in enhancing execution and operational efficiencies during emergency situations and during other non-emergency situations for certain options classes. The Exchange believes that automatic executions of orders for up to seventy-five contracts will enhance its overall operational

efficiency and give the Exchange better means of competing with other options exchanges for order flow.

III. Discussion

After careful review, 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 and, in particular, the requirements of section 6 of the Act.⁹ Among other provisions, section 6(b)(5) of the Act requires that the rules of an exchange be designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating securities transactions; remove impediments to and perfect the mechanism of a free and open market and a national securities system; and protect investors and the public interest.¹⁰

While increasing the maximum order size limit from fifty contracts to seventy-five contracts for AUTO-EX eligibility by itself does not raise concerns under the Act,¹¹ the Commission believes that this increase raises collateral issues that the Amex will need to monitor and address. Increasing the maximum order size for particular option classes will make a larger number of option orders eligible for the Exchange's automatic execution system. These orders may benefit from greater speed of execution, but at the same time create greater risks for market maker participants. Market makers signed onto the AUTO-EX system will be exposed to the financial risks associated with larger-sized orders being routed through the system for automatic execution at the displayed price. When the market for the underlying security changes rapidly, it may take a few moments for the related option's price to reflect that change. In the interim, customers may submit orders that try to capture the price differential between the underlying security and the option. The larger the orders accepted through AUTO-EX, the greater the risk market makers must be willing to accept. The Commission does not believe that, because Amex

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 42931 (June 13, 2000), 65 FR 38615 (June 21, 2000).

⁴ See letter from Scott Van Hatten, Legal Counsel, Derivative Securities, Amex, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission dated October 31, 2000 ("Amendment No. 1"). In Amendment No. 1, the Amex proposes to codify its rules regarding the AUTO-EX parameters for option contracts under Amex Rule 933, Commentary .02.

⁵ See letter from Scott Van Hatten, Legal Counsel, Derivative Securities, Amex to Nancy Sanow, Assistant Director, Division of Market Regulation Commission dated November 2, 2000 ("Amendment No. 2"). In Amendment No. 2, the Amex corrects the language in Amex Rule 933, Commentary .02 to state that the eligible orders for options on the Institutional, Japan and S&P MidCap 400 Indices must be for "fewer than 100 contracts" for series subject to AUTO-EX.

⁶ See Securities Exchange Act Release No. 42094 (November 3, 1999), 64 FR 61675 (November 12, 1999). Although the maximum permissible number of contracts in an option order executable through AUTO-EX is generally fifty contracts, there are three exceptions that allow ninety-nine contract orders; the Institutional, Japan and S&P MidCap 400 Indexes.

⁷ See Securities Exchange Act Release No. 42128 (November 10, 1999), 64 FR 63836 (November 22, 1999).

⁸ The Exchange is codifying its rules, under Amex Rule 933, Commentary .02, regarding the maximum option order size eligibility for its AUTO-EX system. See Amendment No. 1, *supra* note 4. Order size maximum levels for the Institutional, Japan, and S&P MidCap 400 Indexes would remain at ninety-nine contracts under this proposal. See Amendment No. 2, *supra* note 5.

⁹ The Commission has considered the proposed rule's impact of efficiency, competition and capital formation. 15 U.S.C. 78c(f).

¹⁰ 15 U.S.C. 78f(b)(5).

¹¹ The Commission notes that it is concurrently approving similar proposals filed by the Chicago Board Options Exchange, Inc. ("CBOE"), the Pacific Stock Exchange, Inc. ("PCX") and the Philadelphia Stock Exchange, Inc. ("Phlx"). See Securities Exchange Act Release No. 43517 (November 3, 2000) (SR-CBOE-99-51); Securities Exchange Act Release No. 43518 (November 3, 2000) (SR-PCX-00-32); and Securities Exchange Act Release No. 41515 (November 3, 2000) (SR-Phlx-99-32).

governors and senior floor officials determine to approve orders as large as seventy-five contracts as eligible for AUTO-EX, those officials or any other Amex officials or Amex committee should disengage AUTO-EX more frequently by, for example, declaring a "fast" market. Disengaging AUTO-EX can negatively affect investors by making it slower and less efficient to execute their option orders. It is the Commission's view that the Exchange, when increasing the maximum size orders that can be sent through AUTO-EX, should not disadvantage all customers—the vast majority of which enter orders for less than seventy-five contracts—by making the AUTO-EX system less reliable.

Finally, the Commission finds good cause for approving Amendment Nos. 1 and 2 prior to the 30th day after notice of the Amendment is published in the **Federal Register** pursuant to section 19(b)(2) of the Act.¹² Amendment No. 1 codifies the proposed increase in the AUTO-EX parameters from fifty contracts to seventy-five option contracts. Amendment No. 2 corrects the rule language in Amex Rule 933, Commentary .02. The Commission finds that accelerated approval of Amendment Nos. 1 and 2 is appropriate in order to allow the Amex to increase its AUTO-EX eligibility limits so that it may better compete with the other option exchanges.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment Nos. 1 and 2, including whether they are 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 in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. SR-Amex-99-45 and should be submitted by December 6, 2000.

Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with section 6(b)(5).¹³

It is Therefore Ordered, pursuant to section 19(b)(2) of the Act,¹⁴ that the proposed rule change (SR-Amex-99-45) is approved, and Amendment Nos. 1 and 2 are approved on an accelerated basis.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43525 File No. SR-BSE-98-11]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to an Amendment to the Proposed Rule Change by the Boston Stock Exchange, Inc. Relating to Its Competing Specialist Initiative

November 7, 2000.

I. Introduction

On November 23, 1998, the Boston Stock Exchange, Inc. ("BSE" or "Exchange") filed with the Securities and Exchange Commission ("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 modify the procedures by which a regular specialist may object to competition in a stock.

The proposed rule change was published for comment in the **Federal Register** on January 12, 1999.³ The Commission received no comments on the proposal. The Exchange filed amendments on March 26, 1999⁴ and

¹³ 15 U.S.C. 78f(b)(5).

¹⁴ 15 U.S.C. 78s(b)(2).

¹⁵ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 40883 (January 5, 1999), 64 FR 1839 (January 12, 1999).

⁴ See Letter from Karen Aluise, Vice President, BSE, to Richard Strasser, Assistant Director, Division of Market Regulation ("Division"), Commission, dated March 25, 1999, with attachments ("Amendment No. 1"). Amendment

April 13, 2000.⁵ The Exchange filed a third amendment to the proposed rule change on August 25, 2000, which superseded the earlier amendments.⁶ This order approves the proposed rule change, and grants accelerated approval to the third amendment to the proposed rule change.

II. Description

The Exchange's Competing Specialist Initiative permits multiple specialists to make a market in individual securities traded on the BSE. The Exchange has proposed a rule change to modify the process that governs objections to competition in a security.

The Procedures for Competing Specialists, which are set forth in chapter XV, section 18 of the Exchange's Rules, currently provide that a regular specialist in a security may object to any application by another specialist to act as a competing specialist in that security. The Exchange's Market Performance Committee will consider the regular specialist's objections as one factor in reviewing applications to act as a competing specialist in a security. The Market Performance Committee may not deny applications based solely on such an objection, but only in circumstances wherein the stock at issue requires special treatment such that an entering competitor could jeopardize the fair and orderly market maintained by the regular specialist.⁷

No. 1 proposed to eliminate the right to appeal rulings by the Market Performance Committee regarding applications to serve as a competing specialist.

⁵ See Letter from William Cummings, Manager of Legal and Regulatory Affairs, BSE, to Nancy Sanow, Senior Special Counsel, Division, Commission, dated April 12, 2000, with attachments ("Amendment No. 2"). Amendment No. 2 superseded Amendment No. 1. Amendment No. 2 generally sought to revert the proposed rule change back to a form that was similar to the version that the BSE originally proposed, but which differed from the BSE's original proposal in a few ways: by clarifying that an applicant competing specialist could appear before the Market Performance Committee to respond to issues raised by the regular specialist regarding competition, by omitting language which provided that competition could begin during an appeal of a Market Performance Committee ruling in favor of competition, and by making other changes regarding the appeal process.

⁶ See Letter from John Boese, Assistant Vice President, BSE, to Nancy Sanow, Assistant Director, Division, Commission dated August 24, 2000, with attachments ("Amendment No. 3"). Amendment No. 3, which superseded Amendment No. 2, clarified that competition could begin pending the outcome of an appeal of a pro-competition ruling by the Market Performance Committee, which is consistent with the rule change as it was originally proposed by the BSE.

⁷ See Securities Exchange Act Release No. 37045 (March 29, 1996), 61 FR 15318 (April 5, 1996) (order permanently approving Competing Specialist Initiative).

¹² 15 U.S.C. 78s(b)(2).