

an OBO or Post Director, the period of time when RAES is unavailable should be very brief, lasting fewer than five minutes. Even then, orders will continue to be delivered to the trading crowd via the Exchange's electronic order routing system ("ORS") and the trading crowd will remain obligated to fill customer orders in accordance with Exchange rules, including the firm quote rule.<sup>5</sup> Accordingly, orders that would have been routed to RAES will be automatically re-routed to a Public Automated Routing System ("PAR") workstation,<sup>6</sup> a floor broker printer in the trading crowd, or to the appropriate member firm booth, where they can be immediately executed at the then current price.

Members will be notified of any deactivation of RAES in particular classes of options by an OBO or a Post Director pursuant to proposed Rule 6.6(e) by means of a message that is printed to each trading post on the floor and is transmitted to terminals throughout the floor over the Exchange's TextNet system.

### III. Commission Finding and Conclusions

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(b)(5) of the Act.<sup>7</sup> Specifically, the Commission finds that the Exchange's proposal strikes a reasonable balance between the Commission's mandates under Section 6(b)(5) to remove impediments to and perfect the mechanism of a free and open market and a national market system, while protecting investors and the public interest.

The Commission believes that the proposed rule change is reasonable in that it provides Post Directors and OBOs the limited authority to suspend RAES for no more than five minutes in a particular options classes during unusual market conditions. The Commission believes that Post Directors

and OBOs are appropriate parties, to exercise this limited authority, in part, because of (1) their knowledge of assigned options classes, (2) their close proximity with the trading crowd, and (3) their clearly defined administrative role with the Exchange. Accordingly, the Commission believes that Post Directors and OBOs should be able to initially assess market conditions and deactivate RAES for this limited period, thereby reducing the potential for orders being executed at inaccurate prices until Floor Officials can further assess the market conditions. The Commission notes that the standard for OBOs and Post Directors to deactivate RAES is the same standard used by Floor Officials to declare a fast market, which in turn, authorizes Floor Officials to deactivate RAES if they determine that such action is in the interest of maintaining a fair and orderly market.

The Commission notes that two Floor Officials, once immediately notified by the OBO or the Post Director of the RAES deactivation, must promptly determine whether to (1) immediately reactivate RAES pursuant to Rule 6.6(c); or (2) declare a fast market pursuant to Rule 6.6(b) in order to continue the deactivation of RAES for that particular options class.<sup>8</sup> Under no circumstances, can the deactivation of RAES continue for more than five minutes, unless two Floor Officials declare a fast market pursuant to Rule 6.6(b).<sup>9</sup>

Additionally, the Commission believes that the proposed rule change is reasonable because during this limited five-minute period when RAES is deactivated by the Post Director or OBO, orders that would have been routed to RAES will be automatically re-routed to a PAR workstation, a floor broker printer in the trading crowd, or to the appropriate member firm booth, where they can be immediately executed at the then current price. Accordingly, the Commission believes that the Exchange's electronic ORS should provide small investors an efficient and effective method for order execution in circumstances where RAES is turned off pursuant to this proposed rule change.

The Commission expects that such authority as proposed herein, will only be exercised when unusual market conditions exist, and for the shortest time possible. As a general matter, the commission prefers that automated systems such as RAES remain operational at all times. While extreme circumstances may call for the deactivation of the system, it should only be done when absolutely necessary.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>10</sup> that the proposed rule change (File No. SR-CBOE-96-36) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

Margaret H. McFarland,

*Deputy Secretary.*

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### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to the Universal Trading System's Morning Session

September 4, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on April 29, 1996, the Philadelphia Stock Exchange, Inc. ("Phlx" 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 self-regulatory organization. On July 26, 1996, the Exchange submitted to the Commission Amendment No. 1 to the proposed rule change.<sup>1</sup> 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 Phlx, pursuant to Rule 19b-4 of the Act, proposes to implement a daily pre-opening order matching session

<sup>5</sup> The firm quote rule, which obligates the trading crowd to fill public orders for up to 10 contracts at published quotes, remains in effect unless suspended by two Floor Officials acting under Rule 6.6(b) in the event of a fast market. The proposed rule change would not authorize an OBO or DPM to declare a fast market or suspend the firm quote rule.

<sup>6</sup> A PAR workstation is an automated, computer-based workstation that provides users with the ability to execute trades, transmit trade reports, and enter other data and commands at the touch of a screen, thereby eliminating the delay inherent in a keyboard-based system.

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

<sup>8</sup> The Commission understands that if two Floor Officials declare a fast market, they have the authority to, among other things, continue the deactivation of RAES, suspend the firm quote requirement of Rule 8.51(a), or take such other actions as are deemed necessary in the interest of maintaining a fair and orderly market. See CBOE Rule 6.6(b).

<sup>9</sup> The Commission notes that the five-minute period is an absolute time limit imposed by the Exchange on Post Director and OBO directed RAES deactivations. Accordingly, the Commission expects that in most situations, two Floor Officials should be able to exercise their authority under Rule 6.6 before the five-minute period has expired.

<sup>10</sup> 15 U.S.C. 78s(b)(2).

<sup>11</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> See letter from Gerald D. O'Connell, Senior Vice President, Market Regulation and Trading, Operations, Phlx, to Jennifer Choi, Division of Market Regulation, SEC, dated July 26, 1996. The Exchange clarifies that it does not propose to trade Nasdaq securities through the Universal Trading System ("UTS") without a computer-to-computer interface to the National Association of Securities Dealers for reporting purposes.

("Morning Session" or "session") for the execution of large-sized stock orders on a volume weighted average price ("VWAP") basis on its equity floor. The VWAP shall be derived from transactions executed during the trading day and reported to the appropriate reporting authority. The Morning Session has been designed to provide institutional investors with the means to execute large-sized stock orders in Exchange securities anonymously and at fair market prices approximately 15 minutes prior to the opening of the "regular trading session" (i.e., 9:30 A.M.–4:00 P.M. (ET)). The price of Morning Session transactions will be determined at approximately 4:15 P.M. (ET). At that time, the Exchange shall assign the applicable VWAP and report each such trade to the appropriate reporting authority, the Consolidated Tape or other, as VWAP trades.

The receipt and matching of orders for the Morning Session will be handled electronically through the Exchange's Universal Trading System ("UTS" or "System"). The UTS is a system that was devised for facilitating the operational aspects of the Morning Session.

Each of the approximately 2,500 equity securities currently available for trading on the Exchange, both listed and traded pursuant to Unlisted Trading Privileges ("UTP") (including over-the-counter securities) will be eligible for the Morning Session.

The present proposal consists of changes to existing Exchange rules to accommodate the Morning Session and the adoption of a new rule applicable solely to the Morning Session, Rule 237—UTS Morning Session. In addition, Rule 101 is proposed to be amended to add the Morning Session as an exception to regular trading hours.<sup>2</sup>

Proposed Rule 237 is organized as follows: an introductory paragraph, followed by paragraphs: (a) explaining reporting; (b) defining the UTS; (c) governing who the participants are; (d) explaining order entry; (e) specifying order priority; (f) defining the VWAP; (g) governing short sales in the UTS; (h) concerning disputes; (i) containing provisions relating to limitation of liability; and (j) pertaining to trading halts.

UTS trades will be subject to transaction fees as established in the Exchange's fee schedule.

<sup>2</sup> The Exchange also proposes several minor amendments to Rule 101, including placing A.M. and P.M. in capital letters, adding a heading to each commentary, and deleting reference to two specific index options.

### *The Universal Trading System*

The UTS will operate as a separate Exchange system made available to Phlx member organizations and their non-member customers for the purpose of participating in the Morning Session. UTS will link off-floor and on-floor computer terminals to an Exchange communications base unit. UTS access is accomplished through dial-up into the UTS system, utilizing software provided to users and a log-on procedure dependent upon whether the user is accessing UTS through a personal computer or main-frame system.

The UTS base unit will: (i) accept orders and commitments, (ii) match buyers with sellers, (iii) give execution reports to matched participants (iv) calculate the VWAP for each traded security, (v) report trades to the central processor for tape reporting, and (vi) create the necessary audit trail, recording order entry and execution of Morning Session orders.

The UTS was developed by Universal Trading Technologies Corporation ("UTTC"), who will assist the Exchange in its operation of the System in accordance with its agreement with the Exchange.

### *Participation and Clearing Requirements*

Participation in the Morning Session may occur by way of a commitment from a Committer or an order from a User (collectively, "Participants").

Phlx Floor Traders and Off-Floor Liquidity Providers (collectively, "Committers") will each day commit on a proprietary basis to provide contra-side liquidity in eligible securities for the execution of Morning Session orders placed by non-committer members and their customers (collectively, "Users"). UTS commitments may only be made by Exchange members. Committers may be either Phlx Floor Traders or Off-Floor Liquidity Providers, who must register with the Exchange in a prescribed manner prior to acting in the capacity of a Committer. Phlx Floor members qualify as Floor Traders if they are either the Specialist or Alternate Specialist in the security on the Phlx. Off-Floor Liquidity Providers must be members and may only engage as Committers for their proprietary accounts. Committers will be able to choose which, if any, issues they wish to make commitments, but for each chosen issue must provide a minimum volume guarantee of 2,500 shares on each side of the market.

Commitments may be entered and modified in the UTS during the Order

Entry Time Period and also during any other periods which the Exchange may make available for that purpose. Committers may make such contra-side liquidity commitments through the UTS as day-commitments or good-till-cancelled ("GTC") commitments.

UTS orders may only be placed by approved Users. Users may be either members or non-members; however, individual orders placed directly by non-members will require a Stock Clearing Corporation of Philadelphia ("SCCP") member's give-up to ensure that a Phlx clearing member, who must also be a Phlx member, has assumed responsibility for the order. Specifically, the Exchange member must agree to be jointly and severally liable for actions of the non-member through the UTS and the non-member must agree to adhere to all applicable by-laws and rules of the Exchange. Give-up agreements with non-members must be approved in advance by the Exchange, including a delineation of the credit limits for the respective customer.<sup>3</sup> The "three way agreement" between the Exchange, the member and the non-Member User is in addition to the give-up agreement.<sup>4</sup>

### *UTS Order Entry*

Users will enter orders directly and anonymously into the UTS from computer terminals, which may include various types of computer hardware and handheld devices. Only those orders and commitments placed through UTS will be eligible for execution during the Morning Session and orders entered into the UTS are only eligible for execution through UTS.<sup>5</sup> UTS orders will only be accepted during the UTS order entry time period, 5:00 a.m. to 9:15:00 a.m. (ET), and will only be eligible for a UTS execution on the day the order has been placed. UTS orders and commitments may be cancelled (order condition CXL) until 9:15 a.m. (ET). Confirmation of order placement and cancellation is electronically confirmed throughout the UTS.

<sup>3</sup> A draft of a sample three way agreement was submitted to the Commission by letter dated February 7, 1996. Since that time, the Exchange has added a provision relating to the Exchange's ability to terminate a User's access to the System. The draft, including this new provision, will be re-submitted to the Commission.

<sup>4</sup> Telephone conversation between Jennifer S. Choi, Division of Market Regulation, SEC, and Edith Hallahan, Special Counsel, Regulatory Services, Phlx, on August 15, 1996.

<sup>5</sup> Commitments also are only eligible for execution through UTS and do not migrate to any other trading session. Telephone conversation between Jennifer S. Choi, Division of Market Regulation, SEC, and Edith Hallahan, Special Counsel, Regulatory Services, Phlx, on May 22, 1996.

Morning Session trading interest may be entered into UTS in the form of either: (i) An order to trade as a User; or (ii) as a commitment to provide contra-side liquidity to User orders. The minimum order size for individual User orders shall be 5,000 shares, while Committers will be permitted to commit in sizes of 2,500 or greater.

In placing orders and commitments on the System, Participants will be required to provide order/commitment description and account identification information necessary for UTS to establish the priority and eligibility of orders on the System. Specifically UTS orders and commitments are to be placed with the following designations:

- (i) buy/sell;
- (ii) volume;
- (iii) stock symbol;
- (iv) Participant status: C (Committer) or U (User);
- (v) Committer account "commit" status: T (Floor Trader) or L (Off-Floor Liquidity Provider); and GTC or Day;
- (vi) User account "order" status: F (member firm), C (public customer or Registered Investment Adviser); order type (basic, cross, facilitation, etc.);
- (vii) Exchange clearing member organization number;
- (viii) give-up of Phlx floor broker (required for each User order);
- (ix) User identification number; and
- (x) restrictions, if any, on matching against member accounts.

#### Order Types

Eligible order types for the Morning Session include the following: basic, all-or-none, minimum size, facilitation, facilitation-only, facilitation-if-necessary, facilitation-minimum and cross.

In addition to the size-related order types—including basic orders (*i.e.*, fill-order-to-extent-possible), all-or-none orders and minimum size orders—the UTS also permits Users to place orders with "cross" and "facilitation" instructions. A cross order is a two-sided order, with both sides comprised of non-member interest, placed by one User with instructions to match the identified buy-side with the identified sell-side. Facilitation orders, on the other hand, are two-sided orders where one side is comprised of non-member interest and the other side of member interest, with the instruction to cross the non-member interest with the facilitating member interest; a facilitation order may also consist of both sides comprised of member interest with the instruction to cross the members' orders.

Participants may place simple-facilitation orders or may attach

contingency instructions on facilitation orders, whereby certain conditions must be met for execution, as indicated below:

- Simple-facilitation: match the facilitator as contra-side to the accompanying order to the full extent permissible for the facilitator under the Morning Session's priority rule for facilitation-cross orders, but to also, nonetheless, allow any other order(s) with priority over the facilitator to be matched as the contra-side to the accompanying order.
- Facilitation-only: only execute the cross if the facilitator can be completely matched with the accompanying order; otherwise both sides of the facilitation-only order are cancelled.
- Facilitation-minimum: only execute if the facilitator can be matched on a specified minimum number of shares with the accompanying order.
- Facilitation-if-necessary: only match the facilitator to the accompanying order if no other orders or commitments can be matched with the order.

#### Execution and Priority of Orders

Orders for the Morning Session will be matched at approximately 9:16 A.M. (ET). Trades executed through the UTS are printed and cleared as Phlx transactions, executed on the Exchange and cleared through SCCP. In matching VWAP orders for execution during the Morning Session, the following execution priority will apply:

- (1) Match non-member User orders (public customers and Registered Investment Advisers acting on behalf of non-member accounts) with other non-member User orders;
- (2) Match non-member User orders (not matchable with other non-member User orders) with Member User orders;
- (3) Match non-member User orders (not matchable with each other or with member User orders) with commitments;
- (4) Match member User orders (not matchable with non-member User orders) with other member User orders; and
- (5) Match member User orders (not able to be matched with other User orders) with commitments.

The System will not, however, match commitments with other commitments.

User orders are afforded priority as follows: first by account type, in accordance with the five steps described above; then by order size (largest first, etc.); and then, for orders of the same size and account type, on a chronological basis by time-of-entry. Similarly, commitments are prioritized,

as follows: first, on the basis of sub-account types, with Off-Floor Liquidity Providers receiving priority over Floor Traders; then, on the basis of commitment size (largest first, etc.); and finally, on a rotational basis among those of the same size and sub-account type.<sup>6</sup>

Notwithstanding the above, cross orders for the accounts of non-members have absolute priority to trade with each other regardless of size or time priority considerations respecting other orders in the security. The non-member side to a facilitation order will have absolute priority to participate regardless of size or time priority of other orders (other than customer-to-customer cross orders), but the member firm side to a facilitated cross, though it will have priority to trade with its customer over other member firm interest, will not have priority over non-member orders.

Participants are allowed to place instructions stipulating that their orders and commitments only be matched with non-member account orders. Orders and commitments must, however, be available for matching against all non-member orders.

#### VWAP

The VWAP that the Exchange shall assign to each eligible security, which shall be derived daily and publicly disseminated promptly following calculation at 4:15 P.M. (ET) for each of the Exchange's 2,500 eligible equity issues, will be calculated on the basis of those transactions reported during the regular trading session to the appropriate reporting authority, Consolidated Tape or other reporting authority. Generally, consistent with Rule 111, all UTS matches create a binding contract. However, in the case where a transaction occurs in the Morning Session in a security that has not opened for trading by 3:00 P.M. (ET) on the primary market, the respective Morning Session transaction will be voided and a report to that effect will be sent immediately to all matched Participants.

In general, the VWAP for each eligible security shall be calculated by: (i) utilizing all regular way trades (including sold sales and late sales<sup>7</sup>)

<sup>6</sup>For commitments of the same subaccount type and size, the System will choose commitments to be matched on a random basis. Telephone conversation between Jennifer S. Choi, Division of Market Regulation, SEC, and Edith Hallahan, Special Counsel, Regulatory Services, Phlx, on May 22, 1996.

<sup>7</sup>A late sale is an option transaction that is a correct last sale but is publicly disseminated later than is generally required. Generally, each option

effected from the opening of the regular trading session and printed prior to 4:15:00 P.M. (ET) by the appropriate reporting authority,<sup>8</sup> (ii) multiplying each respective reported price by the total number of shares traded at that price; (iii) adding together each of these calculated values, compiling an aggregate sum, and (iv) dividing the aggregate sum by the total number of reported shares for that day in the security. The resulting VWAP will be reported in the form of a fraction, rounded to the nearest  $\frac{1}{256}$ th.

### Reporting

Although the UTS will become available for all Exchange securities, different reporting schemes will be employed for exchange-listed securities and for Nasdaq National Market securities. All UTS transactions will first be reported to the respective reporting authorities at approximately 9:20 A.M. (ET) as a single volume print including all matches in all securities. The morning print for listed securities will occur by way of an administrative message over the Consolidated Tape reflecting total volume in exchange-listed securities. The morning print for Nasdaq securities will occur in similar fashion by way of a direct linkage to the National Association of Securities Dealers, Inc. ("NASD"). The morning prints are intended to notify investors regarding pre-opening volume.

Participants, under normal circumstances, will also be notified of their levels of participation by 9:20 A.M. (ET). UTS transactions will be reported to the User and the Committer in the form of automated reports reflecting the number of shares traded by the Participant through the UTS in each issue.

Promptly following calculation of the final VWAP, at approximately 4:20 P.M. (ET), trades are assigned that day's VWAP for that security and will, at that time, be reported to the appropriate reporting authority. The Exchange will continuously calculate the VWAP throughout the trading day, on a minute-by-minute basis, for each issue available for trading. The intra-day VWAP as well as the final VWAP will be available to all UTS Participants through the UTS. Each Morning Session match, once a VWAP is assigned,

constitutes a completed transaction for the purpose of reporting the trade to the appropriate reporting authority.

End-of-day prints will normally be reported promptly following calculation of the final VWAP at 4:15 P.M. (ET) and, unlike the morning prints, the end-of-day prints will be printed on a trade-by-trade basis for each individual interested which was matched that morning. Each print will reflect a matched trade and the corresponding VWAP. These trades will be reported to the Consolidated Tape with the sale condition "B" indicating average weighted pricing, which will distinguish VWAP trades from other transactions that may possibly be reported after the close (such as after-hours, crossing session or late sales transactions). With respect to Nasdaq National Market securities, the "W" indicator will likewise be utilized to indicate average weighted pricing. Reporting to the NASD will occur automatically via computer interface once such interface is completed. The Exchange states that it does not propose to trade Nasdaq securities through the UTS without a computer-to-computer interface to the NASD for reporting purposes.<sup>9</sup>

The UTS will not disseminate orders or commitments, including UTS bid/ask sizes, prior to the Morning Session match or UTS imbalances remaining after the Morning Session match. The purpose of this anonymity is to safeguard against dissemination to any other participant the existence of executed or unexecuted block orders, which, in turn, could, if disseminated, influence the market after the opening of the regular trading day.

### Other Provisions

Pursuant to proposed paragraph (h), disputes respecting UTS Morning Session participation, or eligibility of orders or participants, are to be resolved by the Exchange. The Exchange's liability respecting the UTS is limited pursuant to By-Law Article 12-11. Thus, the Exchange is not liable for any damage arising from the use of the UTS. With respect to trading halts, Rule 237 is not intended to limit the ability of the Exchange to otherwise halt or suspend trading in any stock traded through the UTS. The Exchange may determine, due to extraordinary circumstances to adjust or modify any of the times referenced by this rule respecting the order entry period, order matching period or any

aspect of the transaction reporting procedures. Lastly, short sales are governed by proposed paragraph (g), which states that UTS Morning Session orders and commitments are not subject to the short sale restrictions of Rule 455.<sup>10</sup> Further, positions resulting from UTS Morning Session transactions are effective for the purpose of determining long or short status, immediately upon notification to the participant of a UTS execution, notwithstanding that the VWAP has not yet been determined.

The specific text of the proposed rule change is available at the Exchange and the Commission.

## 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 self-regulatory organization 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 self-regulatory organization 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

During the past ten years, listed equities trading volume has experienced explosive growth, from 31.9 billion shares in 1985 to 98 billion shares in 1995. At the same time, Nasdaq volume grew at an even greater pace, from 20.6 billion shares in 1985 to 102 billion shares in 1995. Together, for 1995, the listed exchange markets and Nasdaq (collectively, "the markets") traded in excess of 200 billion shares. A contributing factor to this volume surge is the increasing presence of institutional trading. The Exchange expects that over ten million trades of 5,000 shares or more will be executed in the markets during this year.

Although institutional trading of block orders often consists of member firms trading for their proprietary accounts, the vast majority of such trading is for the benefit of non-member accounts. The common thread among most of these non-member block orders is that the investment focus is long-term, rather than short-term. When the investment focus is long-term, intra-day

transaction is required to be publicly disseminated within 90 seconds after the execution. A sold sale designates a transaction appearing on the tape out of its proper sequence.

<sup>8</sup> However, prints representing trades executed after regular trading hours (9:30 A.M. to 4:00 P.M. (ET)), such as the Phlx's Post Primary Session ("PPS") as well as the Pacific Stock Exchange, Inc. ("PSE"), will not be utilized in the VWAP calculation after 4:02 P.M. (ET).

<sup>9</sup> The Exchange notes that Nasdaq issues traded on the Exchange during regular trading hours would currently be reported directly to the NASD utilizing Nasdaq terminals.

<sup>10</sup> For short sales, orders will be marked pursuant to Rule 455. See proposed Phlx Rule 237(g).

price drops occurring when positions are purchased or sold are problematic "bumps" in the road. Many long-term investors prefer to avoid such drops, even though an opportunity to buy at the low or sell at the high may be lost. Smoothing over these bumps would be beneficial to long-term investors. In this vein, long-term investors often link the ability to secure fair prices to the ability to retain anonymity while "working" large orders.

On the other hand, member firms typically use intra-day volatility as an opportunity to trade in the short term. Such firms do so either as facilitators for their customer orders, arbitrageur or as registered floor traders. Many of these traders welcome the opportunities presented by additional volume and volatility. Thus, diverting such intra-day risks from long-term investors (who seek to avoid such risks) to proprietary traders (who seek to assume such risks) is the primary goal of the Phlx's proposal to adopt a Morning Session for the execution of large-sized securities on a VWAP basis.

By placing intra-day price risks on those most willing, and most suited, to accept such risks, the Morning Session will serve both institutional investors and proprietary traders. The advantages of the Morning Session will be available to all qualified market participants for eligible sized orders. Institutions, which will particularly benefit from the session, however, include corporate pension funds, state and municipal pension funds, major money managers and mutual funds. In addition to offering fair pricing, the session will also be cost effective, as it will often replace the costs of "working" an order over the course of a day or longer, with the ease of a single execution and single transaction charge.

The Phlx believes that the UTS is an innovative new automated system, which complements the existing auction market. By integrating order entry functions for customer orders into an automated matching system with floor traders as well as off-floor traders serving as facilitators, and then executing such orders on a VWAP basis in a manner designed to facilitate customer interests first, the UTS incorporates the principles of an auction market with the automation benefits of an electronic execution system. Thus, the Exchange believes that the UTS, as a new data processing and communication technique, creates the opportunity for more efficient and effective market operations, consistent with Section 11A(a)(1)(B) of the Act, by providing increased execution alternatives to investors. By combining

pricing in terms of a VWAP with the ability to access block-sized liquidity commitments, and by providing the ability to anonymously effect such block-sized orders prior to the opening of the regular session, the Exchange's Morning Session should particularly accommodate institutional customer interests.

The Exchange proposes to adopt Rule 237 to establish and govern the UTS. In general, the UTS will accept orders and commitments of established minimum volumes (*i.e.*, 5,000 shares for orders and 2,500 shares for commitments), executing orders against other orders and commitments at the VWAP. The VWAP will be assigned to each matched trade and reported to the appropriate reporting authority, Consolidated Tape or directly to the NASD, including trade-by-trade volume and the VWAP. Consistent with Rule 11Aa3-1 under the Act, the Exchange will thereby provide for the collection and dissemination of transaction reports containing, among other things, the price of the security. Because the System's matching process should be completed prior to the time of the opening of the Phlx market at 9:30 A.M. (ET), the issue of the integration of UTS orders into the auction market is not raised by the proposal.

The Exchange recognizes that Section 11Ac1-1 under the Act bids/offers will not be utilized in the UTS within the meaning of the rule because all orders are executable only at the VWAP, rendering bids/offers meaningless.<sup>11</sup> Further, UTS orders do not raise price priority issues because all orders have been entered for execution at the VWAP. The UTS will execute orders bases on the priority principles enumerated in Rule 237, which is consistent with Section 11(a) of the Act, in that members yield priority to non-members. Off-Floor Liquidity Providers receive priority over Floor Traders to encourage commitments. Because Floor Traders' priority is last-in-line, no issue of Specialists trading ahead of customers is raised by the UTS.

The Exchange believes that the proposed reporting scheme provides transparency to Morning Session executions, specifically identifying the total volume executed before the opening, first as a single print and, once the VWAP is calculated, trade-by-trade. With respect to Nasdaq National Market

securities, the Exchange believes that reporting UTS transactions to the NASD by computer interface is consistent with the Joint Industry Plan<sup>12</sup> ("Plan") adopted pursuant to Section 12(f) of the Act, which governs the collection, consolidation and dissemination of quotation and transaction information for Nasdaq National Market securities listed or traded pursuant to UTP on an exchange. The Exchange does not believe that the Plan precludes VWAP trading, but rather that the Plan focuses on assuring adequate reporting of covered securities. The Exchange's proposal to report directly to the NASD is thus consistent with the Plan.

The UTS will operate as a facility of the Exchange within the meaning of Section 3(a)(2) of the Act, in that the UTS utilizes Phlx equipment and personnel, floor trader participation, and SCCP to clear UTS trades. Thus, Morning Session trades will be appropriately regulated and reported as Exchange trades. The Phlx notes that this is similar to the regulatory treatment afforded to after-hours trading sessions on the Exchange as well as other exchanges.<sup>13</sup>

As previously stated, the VWAP will be calculated on the basis of those transactions reported by the appropriate reporting authority for the respective security from the beginning of the regular trading session to 4:15 P.M. (ET). In the case where a transaction occurs in the Morning Session in a security that has not opened for trading that day for any reason in the primary market by 3:00 P.M. (ET), the respective Morning Session transaction will be voided and a report to that effect will be immediately sent. The Exchange believes that establishing a specific time frame by which a security must trade gives further assurance that the VWAP will consist of a representative sample of trades from which to derive a calculation. Additionally, this provision will also serve the important function of prompt notice that the Morning Session transaction will be voided if the primary market has not yet opened in a particular issue. Although written confirmation will follow, Users will be aware that this rare exception to the creation of a binding contract through the UTS may occur by observing that an issue failed to open on its primary market. The 3:00 P.M. (ET) cut-off provides an objective limitation on the

<sup>11</sup> The Exchange has requested exemptive relief from the requirements of this Rule. See letter from Gerald D. O'Connell, First Vice President, Phlx, to Larry E. Bergmann, Assistant Director, Division of Market Regulation, SEC, dated February 28, 1996. In this letter, the Exchange has also requested interpretive relief regarding Rule 11A2-2(T) under the Act.

<sup>12</sup> This Plan was recently amended and extended by the Commission. See Securities Act Release No. 36481 (Nov. 13, 1995) (File No. S7-24-89).

<sup>13</sup> See *e.g.*, Securities Exchange Act Release No. 29237 (May 24, 1991) (File No. SR-NYSE-90-52 and SR-NYSE-90-53 establishing an off-hours trading facility).

VWAP calculation, which notifies the User that a representative VWAP cannot be calculated for that day. The Exchange has determined that the 3:00 P.M. (ET) provision is preferable to calculating a VWAP based on the previous day's pricing, because an important purpose of the VWAP is to incorporate and average that day's price movement.

With respect to trading halts, if a security opens for trading but is the subject of a halt and does not resume trading for the remainder of the day, the Morning Session transaction is based on the prints that occurred before the halt. The Exchange realizes that a security may only be open for a short time before it is halted; however, the Exchange believes that for the purposes of the UTS VWAP calculation, trading that occurs prior to a halt forms a reasonable basis for calculating a VWAP for that day, even if the security does not reopen that day. A significant amount of price discovery is involved in an opening print, such that it provides an appropriate VWAP measure, which is preferable to voiding that day's UTS trades.

Nevertheless, the Exchange maintains that the Morning Session execution is an executed Exchange contract, with only one unusual circumstance enumerated above. The Exchange notes that although utilizing the VWAP as a pricing mechanism is new to exchange trading, block trades as well as certain Nasdaq trades are currently reported as average weighted pricing trades.

With respect to access to the System, as stated above, Participants may be either Users, who may enter orders, or Committers, who must be Exchange members. Because Users may be non-members of the Exchange, limited non-member access to the UTS is proposed. The Exchange believes that the UTS provides adequate controls regarding limited non-member access to the System. Specifically, orders placed directly by non-members will require a give-up agreement between the non-member and a SCCP member, which must be approved in advance by the Exchange, including a delineation of the credit limits for the respective customer. Thus, the clearing member will agree to clear trades for the non-member User up to specified dollar amount.

In addition, a separate "three way agreement" concerning disciplinary jurisdiction is also required. The purpose of this arrangement is to ensure that a Phlx clearing member, who must also be a Phlx member, has assumed responsibility for the order. The Exchange member must agree to be jointly and severally liable for all actions of the non-member through the

UTS and the non-member must acknowledge its responsibility to all applicable by-laws and rules of the Exchange to the same degree as if the order were placed directly with the give-up firm, providing a jurisdictional basis for disciplinary action against such non-member. The required agreement with the non-member User provides that the Exchange has the right to terminate the User's access to the UTS, without prior notice for any reasons, or no reason whatsoever. In addition, termination of the agreement or clearing arrangement necessarily results in the Exchange's ability to terminate access to the UTS. The Exchange believes that these requirements ensure adequate controls over non-member access, including Exchange supervision of and jurisdiction over non-member Users. The Exchange notes that similar non-member access has been afforded to other exchange systems.<sup>14</sup> Utilizing SCCP facilities and requiring Exchange-approved agreements with non-members are intended to facilitate coordination with persons engaged in clearing and settling these transactions, consistent with Section 6(b)(5).

The Exchange notes that Section 10(a) of the Act governs short sales in securities, while Rule 3b-3 defines the term "short sale" as "any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller." Further, Rule 3b-3 provides that if a person has "purchased, or has entered into an unconditional contract, binding on both parties thereto, to purchase" a security, then that person shall be deemed to own that security.<sup>15</sup> Separately, the Exchange has requested exemptive relief from the "tick test" of Section 10(a) of the Act.<sup>16</sup> Thus, pursuant to Rule 237(g), UTS Morning Session orders and commitments are not subject to the short sale restrictions of Rule 455. Specifically, because a long position creates an irrevocable contract,

a purchase during the UTS Morning Session may be followed by sales during the regular trading session in that security, without such sales deemed short sales.

Lastly, the Exchange proposes to amend Rule 101 to adopt Commentary .03 reflecting the UTS Morning Session and providing reference to Rule 237. The Exchange also proposes minor changes to Rule 101 for clarity and correction. Specifically, A.M. and P.M. would appear in capital letters consistently throughout the rule, and there would be a heading for each commentary. In addition, reference to two specific index options, the Value Line Index Options and National Over-the-Counter Index Options, would be replaced with the language "broad-based (market) index options," which shall freely trade until 4:15 P.M. (ET) each business day. Thus, each Exchange market index option would not have to be listed in this rule; Rule 1101A currently provides such a list of market index options, all of which trade until 4:15 P.M. (ET). The Exchange believes that these changes to Rule 101 should both correct and clarify its provisions.

## 2. Statutory Basis

For the reasons stated above, the Phlx believes that the proposal to operate a Morning Session utilizing the UTS is consistent with the Act, and particularly with Sections 6, 11 and 11A. Specifically, the proposal is consistent with Section 6(b)(5), in that it is designed to promote just and equitable principles of trade, prevent fraudulent and manipulative acts and practices, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, as well as to protect investors and the public interest, by providing an automated order entry and execution system for securities traded during the Morning Session.

The Exchange anticipates that significant institutional volume could be attracted to the Phlx, which should, in turn, add liquidity to both the Morning Session as well as to the Phlx's regular trading session. The Exchange believes that the UTS provides an important new pricing mechanism for exchange trades—the VWAP. Further, the Exchange believes that the Morning Session should provide a unique opportunity to electronically submit block-sized orders for automatic matching before the regular opening at

<sup>14</sup> See Securities Exchange Act Release No. 35030 (Nov. 30, 1994) (File No. SR-CHX-93-19) (Order approving Chicago Match and, at note 70, reference to the New York Stock Exchange's SuperDOT).

<sup>15</sup> The Exchange also understands that amendments to these provisions propose that if the ownership of a security is claimed by virtue of having entered into a contract to purchase it, the contract must involve a fixed, currently ascertainable amount of the security at a fixed, currently ascertainable price. Separately, the Exchange requested that an exemption for the Morning Session be incorporated into these amendments. See letter from Gerald D. O'Connell, First Vice President, Phlx, to Larry E. Bergmann, Assistant Director, Division of Market Regulation, SEC, dated November 9, 1995.

<sup>16</sup> *Id.*

9:30 A.M. (ET). Thus, the UTS should perfect the mechanism of a free and open market and a national market system. The proposal at hand employs specific procedures and safeguards designed to protect investors and the public interest, prevent fraudulent and manipulative acts and practices and promote just and equitable principles of trade. These procedures include specific execution priority parameters, order entry specifications and Exchange surveillance procedures (separately submitted) designed to monitor UTS transactions. The Exchange also believes that because the UTS Morning Session is limited to a once-per-day session and adequately provides for transparency, despite the requested limited exemptive relief, the proposal is consistent with the Act.

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

The Exchange does not believe that the proposed rule change will impose any inappropriate burden on competition.

**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 publication of this notice in the Federal Register or within such other 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 the 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. 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. 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 Section, 450 Fifth Street, N.W., Washington, D.C. 20549. 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-Phlx-96-14 and should be submitted by October 2, 1996.

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

Margaret H. McFarland,

*Deputy Secretary.*

[FR Doc. 96-23122 Filed 9-10-96; 8:45 am]

BILLING CODE 8010-01-M

**SMALL BUSINESS ADMINISTRATION**

**National Advisory Council Public Meeting**

The U.S. Small Business Administration, National Advisory Council, located in the geographical area of Washington, DC will hold a public meeting at 8:00 a.m. on Thursday and Friday, September 12-13, 1996, in the East Room of the Mayflower Hotel, located at 1127 Connecticut Avenue, NW., Washington, DC, to discuss such matters as may be presented by members, staff of the U.S. Small Business Administration, or others present.

For further information, write or call Ms. Toy Tolson, U.S. Small Business Administration, 409 3rd St. SW., Washington, DC 20416, (202) 205-7648.

Dated: September 4, 1996.

Michael P. Novelli,

*Director, Office of Advisory Council.*

[FR Doc. 96-23176 Filed 9-10-96; 8:45 am]

BILLING CODE 8025-01-P

**Maine District Advisory Council Meeting**

The U.S. Small Business Administration, Maine District Advisory Council, located in the geographical area of Augusta, will hold a public meeting at 9:00 a.m. on Monday September 23, 1996, in the Business Information Center of Maine, located at The Bates Mill Complex, 35 Canal Street, Lewiston, Maine, to discuss such matters as may be presented by members, staff of the U.S. Small Business Administration, or others present.

For further information, write or call Mr. Roy Perry, District Director, U.S. Small Business Administration, 40 Western Avenue, Augusta, Maine 04330, (207) 622-8242.

Dated: September 4, 1996.

Michael P. Novelli,

*Director, Office of Advisory Council.*

[FR Doc. 96-23177 Filed 9-10-96; 8:45 am]

BILLING CODE 8025-01-P

**DEPARTMENT OF STATE**

**[Public Notice No. 2440]**

**Advisory Committee on Private International Law; Meeting of Study Group on Electronic Commerce**

The Study Group on Electronic Commerce will hold its next meeting from 3:00-8:00 p.m. on Wednesday, September 18 in Dallas, Texas. The purpose of the meeting will be to review legal issues and possible standards or guidelines concerning the establishment of electronic registries to facilitate the recording of interests in moveable commercial property involved in international transactions.

The need for this review arises from the work on draft multilateral treaties involving international commercial finance at two international organizations, the United Nations commission on International Trade Law (UNCITRAL) and the International Institute for the Unification of Private Law (UNIDROIT). The United States is actively participating in both projects. Preliminary decisions may now need to be taken in both organizations whether to base their respective treaties on registry systems, which will involve issues similar to those dealt with under the Uniform Commercial Code, as well as registry systems involving vessels, certain commodities, etc. In addition, both organizations will need to consider whether such registries would be computer-based, and in what manner systems and standards in different countries can be harmonized for purposes of transactions covered by each respective treaty. The establishment of one or more internationally-based registry systems will also need to be considered, which could serve to establish or monitor standards, provide coordination and linkage with nationally-based systems, or provide direct registry services.

In addition, documents are available on the two multilateral commercial law treaty projects from the office designated below; the UNCITRAL project involves international rules for assignment of accounts receivable; the