

the municipal securities market by, among other things, helping to ensure that the price charged for an issue in the secondary market reflects all available official information about that issue. The Board will continue to operate the output side of the CDI system to ensure that the information is available to any party who wishes to subscribe to the service. As with all MSIL® system services, this service is available, on equal terms, to any party requesting the service.

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

The Board 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.

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

Written comments were neither solicited nor received.

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

Because the foregoing proposed rule change: (i) Does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; (iii) was provided to the Commission for its review at least five days prior to the filing date; and (iv) does not become operative for thirty days from the date of its filing on August 21, 1996, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(e)(6) thereunder. In particular, the Commission believes the proposed rule change qualifies as a "non-controversial filing" in that the proposed standards do not significantly affect the protection of investors or the public interest and do not impose any significant burden on competition. At any time within sixty 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.

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 submissions, 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 board's principal offices. All submissions should refer to File No. SR-MSRB-96-9 and should be submitted by October 29, 1996.

For the Commission by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-37770; File No. SR-PSE-96-28]

Self-Regulatory Organizations; Pacific Stock Exchange Incorporated; Order Granting Approval to Proposed Rule Change Relating to Its Rule on the Evaluation of Its Equity Specialists

October 1, 1996.

I. Introduction

On August 18, 1996, the Pacific Stock Exchange, Incorporated ("PSE" or "Exchange") submitted to 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 to revise its equity specialist evaluation performance measures on a nine-month pilot basis.

The proposed rule change was published for comment in Securities Exchange Act Release No. 37590 (August 21, 1996), 61 FR 44376 (August 28, 1996). No comments were received on the proposal.

II. Description

The Exchange is proposing to adopt a pilot program amending its rule relating to specialists evaluations for a nine month period from October 1, 1996 to July 1, 1997. Currently, PSE Rule 5.37(a) provides that the Equity Allocation

Committee ("EAC") shall evaluate all registered specialists on a quarterly basis and that each registered specialist shall receive an overall evaluation rating based on the following three measures of performance: (1) Specialist Evaluation Questionnaire Survey ("Questionnaire"); (2) SCOREX Limit Order Acceptance Performance; and (3) National Market System Quote Performance.

The Exchange is proposing to modify PSE Rule 5.37(a) by adding three new measures of performance and eliminating one measure of performance. The new measures are: (1) Executions, (2) Book Display Time; and (3) Post 1-P.M. Parameters. The Exchange is also proposing to: add more questions to the Questionnaire and to expand the Quote Performance measure (formerly the National Market System Quote Performance measure)³ to include a performance measure for bettering the quote. In addition, the Exchange is proposing to eliminate SCOREX Limit Order Acceptance Performance as a measure of specialist performance. The Exchange's new rule for the evaluation of specialists will therefore consist of five separate measures of performance, as specified below:

a. Executions

This category on which 50% of each specialist evaluation is based, consists of four subcategories: (a) Turnaround Time; (b) Holding Orders Without Action; (c) Trading Between the Quote; and (d) Executions in Size Greater Than BBO.

Turnaround Time calculates the average number of seconds for all eligible orders up to 1,099 shares based upon the number of seconds between the receipt of a market or marketable limit order in P/COAST and the execution, partial execution, stopping, or cancellation of the order. An order that is moved from the autoex screen to the manual screen will accumulate time until it is executed, partially executed, stopped, or canceled. This measurement begins after the stock opens for the day on the primary market. Only those orders received by P/COAST after the stock opens will be counted. If there is a trading halt or period when the P/COAST system is experiencing problems, Turnaround Time will not be included for those blocks of time. A specialist will be awarded points based on the average number of seconds between the receipt of eligible market or marketable limit orders and any of the actions specified above being taken

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See *infra* text accompanying note 6.

upon such orders. This category will count for 15% of the overall score. The parameter ranges and corresponding points for Turnaround Time are listed below:

Number of seconds parameter range	Points
1- 8	10
9-10	9
11-12	8
13-14	7
15-16	6
17-18	5
19-20	4
21-22	3
23-24	2
25-26	1
27+	0

Holding Orders Without Action measures the number of market and marketable limit orders up to 10,099 shares that are held without action for greater than 25 seconds. As in the Turnaround Time calculation, the order will accumulate time until it is cancelled, stopped, executed, or partially executed. This measurement begins after the stock opens for the day on the primary market. Only those orders received by P/COAST after the stock opens will be counted. If there is a trading halt or period when the P/COAST system is experiencing problems, those blocks of time will be excluded from the Holding Orders Without Action calculation. The specialist will be awarded points based on the percentage of orders that are held under the established time period.⁴ This category will count for 15% of the overall score. The parameter ranges and corresponding points for Holding Orders Without Action are listed below:

Number of seconds parameter range	Points
1- 3	10
4- 6	9
7- 9	8
10-12	7
13-15	6
16-18	5
19-21	4
22-24	3
25-27	2
28-30	1
31+	0

Trading Between the Quote measures the number of market and marketable limit orders that are executed between the best primary market bid and offer. For this criterion to count toward the overall evaluation score, ten orders or

more must have been executed during the quarter the specialist is being evaluated. If less than ten orders are executed, this criterion will not be counted and the rest of the evaluation criteria will be given more weight.

When a market or marketable limit order is executed, the execution price is compared to the primary bid and offer. The specialist will be awarded points based on the percentage of orders the specialist receives that are executed between the primary bid and offer. If the execution price falls between the primary bid and the primary offer, the trade is counted as one that traded between the quote at the time of execution. Each time a trade is executed, the primary market quote will be noted. If the spread of that quote is two or more trading fractions apart, that trade will count as one eligible for the comparison of the execution price to the quote. If there is a trading halt or period when the P/COAST system is experiencing problems, those blocks of time will not be included in the Trading Between the Quote calculation.

This category will count for 10% of the overall score. The parameter ranges and corresponding points for Trading Between the Quote are listed below:

Percent of orders parameter range	Points
51+	10
46-50	9
41-45	8
36-40	7
31-35	6
26-30	5
21-25	4
16-20	3
11-15	2
5-10	1
0- 4	0

Executions in Size Greater Than BBO measures the number of market and marketable limit orders which exceed the best bid and offer ("BBO") size. When a market or marketable limit order is executed, the order must meet two tests to be counted: first, the original order size must be greater than the BBO size; and second, the execution size must be greater than the BBO size. If the execution size is greater than the bid size (for a sell order) or offer size (for a buy order), the trade is counted as one that was executed in size greater than the BBO. If there is a trading halt or period when the P/COAST system is experiencing problems, those blocks of time will not be included in the Executions in Size Greater Than BBO calculation. For this criterion to count toward the overall evaluation score, ten orders or more must have been executed during the quarter the specialist is being

evaluated. If less than ten orders are executed, this criterion will not be counted and the rest of the evaluation criteria will be given more weight.

The specialist will be awarded points based on the percentage of orders that are executed that exceed the BBO size. This category will count for 10% of the overall score. The parameter ranges and corresponding points for Executions In Size Greater than BBO are listed below:

Percent of orders parameter range	Points
98-100	10
95-97.999	9
92-94.999	8
89-91.999	7
86-88.999	6
83-85.999	5
80-82.999	4
77-79.999	3
74-76.999	2
71-73.999	1
0-70.999	0

b. Specialist Evaluation Questionnaire Survey

The Questionnaire is filled out by equity floor brokers on a quarterly basis. The Questionnaire responses will count for 15% of the overall score. Each question in the Questionnaire has a possible rating of 1 to 10. Each question will be weighted equally and will count for 1.875% of the overall evaluation score.

The Questionnaire currently solicits from floor brokers ratings in the following categories: the quality of markets maintained by the specialists; the specialists's effectiveness in his (her) handling of orders; communication; and the specialist's handling of clerical and administrative matters. The Questionnaire will be expanded to solicit from floor brokers ratings on the specialist's: Handling of manual orders for a size greater than that provided for in the BBO; failure to trade on displayed quotes; representation of the broker's orders in his (her) quotes; and facilitation of crosses.

The new questions proposed to be added to the Questionnaire are the following: Does the specialist handle manual orders from floor brokers for greater than the BBO size?; Does the specialist fail to trade on his (her) displayed quotes?; Does the specialist adequately represent brokers' orders in the quotes?; and Does the specialist allow for easy facilitation of crosses?

c. Book Display Time

This criterion calculates the percentage of the book shares at the best price in the book that are displayed in the specialist's quote, by symbol, and

⁴ I.e., a specialist will receive fewer points the larger the percentage of orders that he (she) holds for greater than 25 seconds.

the duration of time that each percentage is in effect. This criterion rates the P/COAST book displayed 100% of the time. The sizes of all open buy limit orders at the best price for the symbol in the specialist's book will be totaled and compared to the bid size quote. The sizes of all open sell limit orders at the best price for the symbol in the book will be totaled and compared to the offer size quote. This will be done for each symbol traded by the specialist, and only for those orders priced within the primary quote. Limit orders in the book which are priced beyond the primary quote will not be included; they will not be executed until they reach the price in the primary quote, so the specialist should not be required to cover them in his (her) quote sizes.

The specialist will be awarded points on the basis of the percentage of the book that the specialist displays. This category will count for 15% of the overall score. The parameter ranges and corresponding points for Book Display Time are listed below:

Percent of book parameter range	Points
80 +	10
75 - 79	9
70 - 74	8
65 - 69	7
60 - 64	6
55 - 59	5
50 - 54	4
45 - 49	3
40 - 44	2
35 - 39	1
0 - 34	0

d. Post-1 P.M. Parameters

This criterion measures the specialist's quote performance in the post-1 p.m. (Pacific Time) auction market ("Extended Trading Session").⁵ The Post-1 P.M. Parameters criterion has the following features:

1. Specialists' activity is recorded in post-1 p.m. files, where there is one record for each quote and trade per post and symbol as they occur during the Extended Trading Session.

2. Specialists are not subject to the post-1 p.m. quote-spread parameters until after 1:10 p.m. This allows the specialists time to do any primary market runoff business that is necessary.

3. The specialist's quote prices in effect ten minutes past the beginning of the Extended Trading Session must be within the defined number of trading fractions of the primary closing quote.

A. If the primary exchange is the NYSE, and the primary bid price at closing on that day for the stock is under \$1.00, the trading fraction is $\frac{1}{16}$; if the price is at or over \$1.00, it is $\frac{1}{8}$.

B. If the primary exchange is the Amex, and the primary bid price at closing on that day for the stock is under \$10.00, the trading fraction is $\frac{1}{16}$; if the price is at or over \$10.00, it is $\frac{1}{8}$.

4. The specialist's quote sizes in effect ten minutes past the beginning of the Extended Trading Session must be 500 shares or more if the primary bid price is less than \$50.00, or 200 shares if the primary bid price is \$50.00 or more.

5. The specialist's quote-spread parameters must apply to a minimum of 25% of the stocks traded at the post to receive full credit on the evaluation (i.e., 10 points).

6. If the specialist executes any trades after ten minutes of the Extended Trading Session and they are priced within the allowable trading fraction of the primary closing quote price, the quantity of the trade is deducted from the required quote size.

7. If the specialist changes his (her) quote at any time on the same day for that symbol while the required quote size is not zero, his (her) quote price must be within the allowable trading fraction from the primary closing bid price and his (her) quote size must be at least the remaining quote size required (as adjusted for trades, as explained in item 6). If either the price or size on either side of the quote for that symbol does not comply, the symbol is not counted as adhering to the parameters for that day.

8. If, at the end of the Extended Trading Session, the required quote size is still not zero (after adjusted for trades) for bid and/or ask, but the specialist has complied with the quote price and size guidelines on both and ask, the symbol is counted as one that adhered to the parameters.

This category will count for 10% of the overall score. The parameter ranges and corresponding points for Post-1 P.M. Parameters are listed below:

Percent of book parameter range	Points
25 +	10
22 - 24.999	9
19 - 21.999	8
16 - 18.999	7
13 - 15.999	6
10 - 12.999	5
7 - 9.999	4
4 - 6.999	3
0 - 3.999	0

e. Quote Performance

This category, on which 10% of each specialist evaluation is based, consists

of two subcategories: (a) Equal or Better Quote Performance; and (b) Better Quote Performance.

Equal or Better Quote Performance calculates for each issue traded, the percentage of time in which specialist's bid or offer is equal to or better than the primary market quote with a 500-share market size or the primary market size, whichever is less, with a 200-share market minimum. This category will count for 5% of the overall score. The parameter ranges and corresponding points for Equal or Better Quote Performance are listed below:

Percent of time parameter range	Points
40 +	10
36 - 39	9
32 - 35	8
28 - 31	7
24 - 27	6
20 - 23	5
16 - 19	4
12 - 15	3
8 - 11	2
4 - 7	1
0 - 3	0

Better Quote Performance calculates for each issue traded, the percentage of time in which a specialist's bid or offer, is better than the primary quote with a 500-share market size or the primary market size, whichever is less, with a 200-share minimum. This category will count for 5% of the overall score. The parameter ranges and corresponding points for Better Quote Performance are listed below:

Percent of time parameter range	Points
34 +	10
3 - 3.999	9
2 - 2.999	8
1 - 1.999	7
0 - 0.999	0

The Exchange noted that the pilot program only modifies the performance criteria of PSE Rule 5.37(a); consequently, during the pilot the EAC will evaluate the performance of specialists in accordance with the standards and procedures found in PSE Rule 5.37. The Exchange represented that during the nine month pilot, it will re-program its computer program so that the following three criteria are based upon the national best bid and offer ("NBBO") instead of the primary market bid and offer: Trading Between the Quote, Book Display Time, and Quote Performance.⁶ The Exchange also represented that during the pilot it will establish an overall passing score for the

⁵ The PSE's Extended Trading Session is an auction market trading session that runs from 1:00-1:50 p.m. (Pacific Time).

⁶ See Securities Exchange Act Release No. 37590 (August 21, 1996), 61 FR 44376 (August 28, 1996).

performance evaluation as well as individual passing scores for each criterion. The Exchange further stated that it will file a proposed rule change with the Commission pursuant to Rule 19b-4 of the Act that will include these changes by May 1, 1997.⁷

III. Discussion

The Commission believes that specialists play a crucial role in providing stability, liquidity, and continuity to the trading of stocks. Among the obligations imposed upon specialists by the Exchange, and by the Act and the rules promulgated thereunder, is the maintenance of fair and order markets in their designated securities.⁸ To ensure that specialists fulfill these obligations, it is important that the Exchange conduct effective oversight of their performance. The PSE's specialist evaluation program is critical to this oversight.

The PSE's proposed pilot program adds three new objective measures to the Exchange's specialist evaluation program and eliminates one of its objective performance measures. The first new objective measure, Executions, consists of four submeasures: Turnaround Time, Holding Orders Without Action, Trading Between the Quote, and Executions in Size Greater Than BBO. Turnaround Time and Holding Orders Without Action (30% of the overall program weight) apply to the timeliness of executions of orders received by specialists; Trading Between the Quote (10%) applies to the execution prices of orders directed to specialists; and Executions in Size Greater Than BBO, applies to the depth of the markets provided by specialists.

The Commission notes that these submeasures are almost identical to the objective measures currently used in the Boston Stock Exchange, Inc.'s ("BSE") specialist performance evaluation program ("SPEP").⁹ The Commission believes that the adoption of the Execution measure will greatly enhance the Exchange's specialist evaluation program in that its component submeasures should generate sufficiently detailed information to enable the Exchange to make accurate assessments of specialist performance in

the areas of timeliness of executions, price performance, and market depth.

The second proposed measure of specialist performance, Book Display Time, calculates for each security the percentage of shares in the specialist's book at the best price in the book that are displayed in the specialist's quote, and the duration of time that each percentage is in effect. The Commission also believes that the adoption of this measure is appropriate, in that it may encourage PSE specialists to display a greater percentage of the best priced limit orders in a security in their quotes, thereby increasing PSE market depth and the possibility of execution for such limit orders.¹⁰

The third proposed measure of specialist performance, Post 1-P.M. Parameters, calculates each specialist's quote performance during the Exchange's Extended Trading Session. Given that the PSE is one of either two or three national securities exchanges conducting an auction market trading session between 1:00 and 1:30 p.m. (PT),¹¹ and the only such exchange doing so between 1:30 and 1:50 p.m. (PT), the quality of PSE specialists' quote performance is of particular importance during this time. The Exchange's current evaluation program does not include a performance measure specifically tailored to the Extended Trading Session. Accordingly, Commission believes that the adoption of this measure is appropriate as it will provide such a performance measure as well as a possible incentive to PSE specialists to maintain or improve their quote performance during this time.

The Commission finds that the Exchange's proposal to expand its former National Market System Quote Performance measure (referred to as Quote Performance for the nine-month pilot) to include a performance measure for bettering the quote is, with one qualification discussed below,¹² responsive to the previous request by the Division of Market Regulation for the inclusion of such a measure in the PSE's evaluation program.¹³

Furthermore, the exchange is proposing to eliminate SCOREX Limit Order Acceptance Performance, which calculates the percentage of limit orders accepted by specialists, as a measure of specialist performance. In light of the adoption of the three new performance measures into the Exchange's evaluation program, one of which will measure limit order handling in particular (Book Display Time), the Commission believes that the elimination of this proposal from the PSE's evaluation program is appropriate.

The Exchange is also proposing to add four new questions to its Questionnaire and to reduce the weight of the Questionnaire from 45% to 15% of the overall evaluation program. The Commission believes that the new questions should solicit additional relevant information as to the market making performance of PSE specialists. Moreover, the Commission finds that the reduction in the weight of the Questionnaire is appropriate in that it will accommodate the inclusion of the proposed new objective criteria into the PSE's evaluation program, while still maintaining the combination of a subjective floor broker survey and objective performance criteria that, as the Commission previously stated, should provide an exchange with an effective and fair means of evaluating specialist performance.¹⁴

Despite the improvements to the existing specialist performance evaluation program being adopted herein, the Commission is concerned with the Exchange's use of the primary market quote, instead of the NBBO, in the proposed Trading Between the Quote, Book Display Time, and Quote Performance measures.¹⁵ The Commission believes that the use of the NBBO in this context is necessary to gauge the performance of PSE specialists in comparison with their competitors in the national market system. The Exchange's proposed use of the primary market quote in these three measures does not allow for such comparisons to be made in instances where the primary market quote is not equal to the NBBO.¹⁶

⁷ *Id.*

⁸ Rule 11b-1, 17 CFR 240.11b-1; PSE Rules 5.29(f).

⁹ See *infra* notes 15-16 and accompanying text. For a detailed description of the BSE's SPEP, see Securities Exchange Act Release Nos. 31890 (February 19, 1993), 58 FR 11647 (February 26, 1993) (order approving incorporation of objective criteria into BSE SPEP); 37581 (August 19, 1996), 61 FR 43797 (August 26, 1996) (order approving revision of program weights applicable to objective criteria).

¹⁰ However, the Exchange's use of the primary market quote instead of the NBBO in calculating this measure may reduce the possibility of these beneficial effects occurring during the pilot program. See *infra* notes 15-16 and accompanying text.

¹¹ The Philadelphia Stock Exchange, Inc. conducts a post-4 p.m. (ET) auction market trading session between 4:00-4:15 p.m. (ET), while the Chicago Stock Exchange, Incorporated conducts such a session between 4:00-4:30 p.m. (ET).

¹² See *infra* notes 15-16 and accompanying text.

¹³ Telephone Conversation between Jeff Norris, Special Projects and Financial Administration Manager, PSE, and Sharon Lawson, Senior Special Counsel, SEC, dated July 20, 1995.

¹⁴ See, e.g. Securities Exchange Act Release No. 28843 (February 1, 1991), 56 FR 5040 (February 7, 1991) (order permanently approving PSE specialist evaluation program); SEC, Division of Market Regulation, The October 1987 Market Break Report ("Market Break Report") (February 1988), at xvii.

¹⁵ See *supra* notes 8, 9, and 11.

¹⁶ The following illustrates the difficulties arising out of the PSE's use of the primary market quote instead of the NBBO in these three measures: PSE specialists will receive credit in Trading Between the Quote when the primary market bid (offer) is lower (higher) than the NBBO and the specialist

Although the Commission is concerned about approving a specialist evaluation program containing objective measures that are more appropriately based on the NBBO,¹⁷ the Commission believes that approval of the proposal on a pilot basis is appropriate. The Exchange has represented that during the operation of the pilot it will reprogram its computer systems so that these three measures are calculated using the NBBO instead of the primary market quote and will submit a rule change pursuant to Rule 19b-4 by May 1, 1997 to effect this change.¹⁸

Moreover, the Exchange has represented that the reprogramming of these measures may take up to six months. As the Exchange's revision of its objective performance measures already has been subject to significant delays,¹⁹ and the Commission feels that the proposed specialist evaluation program is a substantial improvement over the existing program even with the use of the primary market quote in these measures, the Commission believes that it is appropriate to approve the proposal on a pilot basis. This will allow the PSE to commence using the new measures immediately for the last quarter of 1996.

The Commission has previously stated that true relative performance standards are the preferable means to evaluate comparative performance of specialists on a national securities exchange.²⁰ Moreover, the Commission

effects a trade at the NBBO; PSE specialists will receive credit in Book Display Time for displaying its limit orders priced at the primary market bid (offer) is lower (higher) than the NBBO; and, PSE specialists may receive credit in either component of the Quote Performance measure when the specialist's quote is equal to or better than the primary market quote but either inferior or equal to the NBBO.

¹⁷ The use of the primary market quote rather than the NBBO may be appropriate in limited circumstances. For example, the primary market closing price may be useful as a benchmark to specialist performance in a post-4 p.m. action market trading session, and is therefore appropriate for use in the proposed Post—1 p.m. Parameters measure.

¹⁸ See Securities Exchange Act Release No. 37590, *supra* note 6.

¹⁹ See Letter from Sharon Lawson, Senior Special Counsel, SEC, to David P. Semak, Vice President—Regulation, PSE, dated January 9, 1995 (requesting PSE to submit revised specialist evaluation program by October 31, 1995); Letter from David P. Semak, Vice President—Regulation, PSE, to Sharon Lawson, Senior Special Counsel, Commission, dated April 6, 1995 (requesting extension to April 30, 1996); Letter from David P. Semak, Vice President—Regulation, PSE, to Sharon Lawson, Senior Special Counsel, Commission, dated August 11, 1995 (requesting extension to July 31, 1996).

²⁰ By relative performance standards the Commission means standards that automatically subject specialists that fall below a predetermined threshold of performance to a special performance review by the appropriate exchange authority. See Securities Exchange Act Release No. 28843, *supra*

has also stated that an effective evaluation program should subject specialists who meet minimum performance levels on the overall program, but need help or guidance in improving their performance in a particular area, to review. While PSE's specialist evaluation program subjects those specialists falling into the bottom 10% of all specialists on his or her trading floor to review by the EAC, it does not set a minimum performance level on the overall program. In addition, the Exchange has not established minimum performance standards for individual performance measures. However, the Commission notes that the PSE has represented that it will establish an overall passing score for the evaluation program as well as individual passing scores for each performance measure during the course of the pilot.

Accordingly, the Commission believes that it is appropriate to approve this rule filing on a nine-month pilot basis, expiring July 1, 1997. This nine-month period will enable the Exchange to determine the appropriateness of the newly adopted objective measures, their respective weights and the acceptable levels of performance; reprogram its systems so that Trading Between the Quote, Book Display Time and Quote Performance are calculated using the NBBO instead of the primary market quote; develop an overall passing score for the performance evaluation as well as individual pausing scores for each criterion; as well as to review the effectiveness of the overall PSE Rule 5.37 equity evaluation program.

The Commission therefore requests that the PSE submit by May 15, 1997 a proposed rule change pursuant to Rule 19b-4 to revise the pilot to utilize the NBBO to calculate the Trading Between the Quote, Book Display Time, and Quote Performance measures; a passing score for the overall performance evaluation as well as each criterion, and a request to extend the pilot beyond July 1, 1997. The Commission also requests that the PSE submit a report to the Commission, by May 15, 1997, describing its experience with the pilot. At a minimum, this report should contain data, for the last review period of 1996 and the first review period of 1997, on (1) the number of registered specialists who scored in the bottom 10% of all registered specialists on his or her trading floor in the overall program; (2) the number of specialists who, as a result of scoring in the bottom 10% in any one quarterly evaluation,

note 14; Market Break Report at xvii and 4-28 to 4-29.

appeared before the EAC, and the type of restrictions that were imposed on such specialists (*i.e.*, restriction on new allocations or acting as an alternate specialist), or any further action that was taken against such specialists; (3) the number of specialists who, as a result of scoring in the bottom 10% in any two out of four consecutive quarterly evaluations, appeared before the EAC, whether any restrictions were imposed on such specialists, and whether formal proceedings were initiated against such specialists; and (4) the number of specialists for whom formal proceedings were initiated, the results of such proceedings, including a list of any stocks reallocated from a particular unit.

For the reasons discussed above, the Commission finds that the PSE's proposal to modify its Rule 5.37 specialist evaluation program performance measures is consistent with the requirements of section 6(b) and 11 of the Act²¹ and the rules and regulations thereunder applicable to a national securities exchange. Specifically, the Commission finds that the proposed rule change is consistent with the Section 6(b)(5) requirement that the rules of an exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

Further, the Commission finds that the proposal is consistent with Section 11(b) of the Act²² and Rule 11b-1 thereunder which allow securities exchanges to promulgate rules relating to specialists in order to maintain fair and orderly markets and to remove impediments to and perfect the mechanism of a national market system.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,²³ that the proposed rule change (SR-PSE-96-28) is approved on a pilot basis, through July 1, 1997.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁴

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²¹ 15 U.S.C. 78f (b) and 78k.

²² 15 U.S.C. 78k (b).

²³ 15 U.S.C. 78s(b)(2).

²⁴ 17 CFR 200.30-3(a)(12).