

The Exchange believes it is appropriate for the index options specified in proposed Commentary .10 to be offset by the specified PDRs because the index options and PDRs are based on the same underlying securities, or related to indexes whose underlying securities include all securities underlying another index (i.e., S&P 100® Index and the S&P 500® Index) or indexes that have a high degree of overlap of securities underlying the indexes and that have historically demonstrated a very high correlation in price changes (i.e., the Institutional Index and the S&P 500® Index; the Major Market Index and the Dow Jones Industrial Average). The Exchange will propose additions to or deletions from Commentary .10 by a filing with the Commission pursuant to Rule 19b-4.

#### (1) Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act in general and furthers the objectives of Section 6(b) in particular in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and, in general, to protect investors and the public interest.

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

The Exchange believes that the proposed rule change will impose no 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 solicited or received with respect to the proposed rule change.

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

The Exchange requests that the Commission grant accelerated effectiveness to the proposed rule change pursuant to Section 19(b) of the Act. Amex represents that the proposed rule is similar in effect to the position taken previously by the Federal Reserve in correspondence with Amex, as cited above, in connection with trading of PDRs on the Exchange. Amex further requests that the proposed rule be implemented as a one-year pilot program.

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

Interested persons are invited to submit written data, views and arguments concerning the foregoing,

including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW, Washington, DC. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. Comments also may be submitted electronically at the following E-mail address: rule-comments@sec.gov. File Number SR-AMEX-98-33 should be included on the subject line if E-mail is used to submit a comment letter. Electronically submitted comment letters will be posted on the Commission's Internet web site (<http://www.sec.gov>). All submissions should refer to File Number SR-AMEX-98-33 and should be submitted by November 10, 1999.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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

[Release No. 34-41995; File No. SR-CBOE-99-29]

#### **Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendments No. 1 and No. 2 to Proposed Rule Change by the Chicago Board Options Exchange, Inc. To Allow RAES Orders To Trade Against Orders in the Exchange's Limit Order Book**

October 8, 1999.

#### **I. Introduction**

On June 23, 1999, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange") submitted to the Securities and Exchange Commission

("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4<sup>2</sup> thereunder, a proposed rule change. In its proposal, the CBOE seeks to amend its rules to allow Retail Automatic Execution System ("RAES") orders to trade directly against orders in the Exchange's limit order book. The proposed rule change was published for comment in the **Federal Register** on July 22, 1999.<sup>3</sup> On August 11, 1999, the CBOE filed Amendment No. 1 to the proposed rule change.<sup>4</sup> On September 23, 1999, the CBOE filed Amendment No. 2 to the proposed rule change.<sup>5</sup> The Commission received one comment on the proposal.<sup>6</sup> This order approves the proposal, as amended. In addition, the Commission is publishing this notice to solicit comments on Amendments No. 1 and No. 2 to the proposed rule change and is simultaneously approving Amendments No. 1 and No. 2 on an accelerated basis.

#### **II. Description of the Proposal**

The Exchange is developing a system, the Automated Book Priority system, that will allow an order entered into RAES to trade directly with an order on the Exchange's customer limit order book in those cases where the prevailing market bid or offer is equal to the best bid or offer on the Exchange's book.<sup>7</sup> Currently, when a RAES order is

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

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

<sup>3</sup> See Securities Exchange Act Release No. 41621 (July 14, 1999), 64 FR 39546.

<sup>4</sup> In Amendment No. 1, the CBOE makes technical, non-substantive changes to the proposal. The CBOE resubmitted the text of the Exchange Rules to show the actual text of these rules as of the date the proposed rule change was submitted. See letter from Timothy Thompson, Director, Regulatory Affairs, CBOE, to Michael Walinskas, Associate Director, Division of Market Regulation ("Division"), Commission, dated August 10, 1999 ("Amendment No. 1").

<sup>5</sup> In Amendment No. 2, the CBOE makes additional technical, non-substantive changes to the proposal. The CBOE resubmitted the proposed rule text to reflect amendments to existing rule text from a separate filing (SR-CBOE-99-17) that was approved by the Commission on August 23, 1999. See Securities Exchange Act Release No. 41782, 64 FR 47881 (Sept. 1, 1999). In addition, the CBOE clarifies that portions of rule text approved by SR-CBOE-99-17 will be removed by this proposed rule change. See letter from Timothy Thompson, Director, Regulatory Affairs, CBOE, to Ken Rosen, Attorney, Division, Commission, dated September 22, 1999 ("Amendment No. 2").

<sup>6</sup> In approving the proposal, the Commission has considered the commenter's support of the proposed rule change. See letter from Gerald D. Putnam, Chief Executive Officer, Archipelago, L.L.C., to Jonathan G. Katz, Secretary, Commission, dated August 13, 1999.

<sup>7</sup> In the event that the order in the book is for a smaller number of contracts than the RAES order, the balance of the RAES order will be assigned to participating market-makers at the same price at which the rest of the order was executed.

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

entered into the Exchange's Order Routing System at a time when the prevailing market bid or offer is equal to the best bid or offer on the Exchange's book, the order is routed electronically (i.e., "kicked out") to a Floor Broker's terminal or work station in the crowd subject to the volume parameters of each firm. This allows for manual representation of the order in the crowd and generally prevents orders from trading through the book.<sup>8</sup> The orders are kicked out because CBOE Rule 6.45 provides that bids or offers displayed on the customer limit order book are entitled to priority over other bids or offers at the same price.

To implement the Automated Book Priority system, the CBOE proposes to amend paragraphs (b) and (c) of CBOE Rule 6.8, "*RAES Operations in Equity Options*," to provide for RAES orders to trade directly against orders entered in the Exchange's customer limit order book. The Exchange also proposes to delete Interpretation .04 of CBOE Rule 6.8 which concerns how orders that have been kicked out pursuant to the current paragraph (c) should be handled.

The CBOE believes that the Automated Book Priority system will both prevent the RAES order from becoming subject to market risk and preserve the priority of the booked order. Thus, the proposed rule change will benefit customers using the RAES system as well as those whose orders are in the Exchange's book because both categories of orders will be executed more quickly than they would have been executed otherwise.

The Exchange anticipates that the Automated Book Priority system will be ready to be implemented by October 31, 1999.<sup>9</sup> The Exchange will provide its membership with prior notice by means of a Regulatory Circular informing them of the date the system and the rule change will be implemented.

### III. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the

Act.<sup>10</sup> In particular, the Commission finds the proposal is consistent with Section 6(b)(5)<sup>11</sup> of the Act. Section 6(b)(5) requires, among other things, that the rules of an exchange be designed to promote just and equitable principles of trade and to protect investors and the public interest.

The Commission believes that the proposed rule change will benefit investors by allowing RAES orders to trade against orders in the Exchange's limit order book. Currently, when a RAES order is entered at a time when the prevailing market bid or offer is equal to the best bid or offer of the Exchange's limit order book, the order is kicked out into the crowd for manual execution. Although this generally prevents RAES orders from trading through the book, when a RAES order is kicked out to the crowd, it may become subject to market risk, which can be significant in a fast moving market. Moreover, the kick out feature is not employed for IBM, DJX, and OEX options, where RAES orders can trade through the book. The Commission finds that the implementation of this new system will provide for more efficient execution of both RAES and booked orders. Investors should benefit from more efficient executions, while the priority of booked orders is maintained.

Linking the Exchange's limit order book to the RAES system is important to ensure proper quality of execution of RAES orders and booked limit orders. Implementation is particularly important for limit orders on IBM, DJX, and OEX options, where booked orders may receive delayed or no execution. The Commission expects that the Exchange will take all reasonable steps necessary to implement the proposal by October 31, 1999.

The Commission finds good cause for approving Amendments No. 1 and No. 2 prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. In Amendment No. 1, the CBOE merely clarified the text of the Exchange Rules to show the actual text of these rules as of the date the proposed rule change was submitted. In Amendment No. 2, the CBOE resubmitted the text of the Exchange Rules to show the text of these rules as amended by filing (SR-CBOE-99-17) that was approved by the Commission on August 23, 1999.<sup>12</sup> In addition, the CBOE explains that portions of the rule

text approved by SR-CBOE-99-17 will be removed by this proposed rule change. Therefore, the amendments did not substantively alter the proposal.

### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>13</sup> that the proposed rule change (SR-CBOE-99-29), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

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

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42004; File No. SR-CHX-99-16]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 and Order Granting Accelerated Approval of Proposed Rules Change and Amendment Nos. 1 and 2 by the Chicago Stock Exchange Relating to the Implementation of an Extended Hours Trading Session

October 13, 1999.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 14, 1999, the Chicago Stock Exchange, Incorporated ("CHX" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the CHX. On October 7, 1999, the CHX submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> On October 8, 1999, the CHX filed Amendment No. 2 to the proposed rule change.<sup>4</sup> The

<sup>13</sup> 15 U.S.C. 78s(b)(2).

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> Letter to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), Commission, from Paul B. O'Kelly, Executive Vice President, Market Regulation and Legal, CHX, dated October 5, 1999 ("Amendment No. 1"). In Amendment No. 1, the CHX proposes to amend the initial filing to request that the Commission approve its proposed extended hours trading session on a pilot basis through March 1, 2000.

<sup>4</sup> Letter to Katherine A. England, Assistant Director, Division, Commission, from Paul B. O'Kelly, Executive Vice President, Market Regulation and Legal, CHX, dated October 7, 1999 ("Amendment No. 2"). In Amendment No. 2, the CHX proposes that, although effective upon

<sup>8</sup> Currently, RAES orders in options on IBM, the Dow Jones Industrial Average (DJX), and the Standard & Poor's 100 Stock Index (OEX) may be executed on RAES even where the prevailing market bid or offer equals the best bid or offer on the Exchange's book. Upon the implementation of the Automated Book Priority system, RAES orders in these option classes, like all other option classes, will trade against orders in the book in these circumstances.

<sup>9</sup> Telephone call between Timothy Thompson, Director, Regulatory Affairs, CBOE, and Joseph P. Corcoran, Attorney, Division, Commission, on August 25, 1999.

<sup>10</sup> In addition, pursuant to Section 3(f) of the Act, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>11</sup> 15 U.S.C. 78f(b)(5).

<sup>12</sup> See *supra* note 5.