

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-42161; File No. SR-PHLX-99-39]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Amending Phlx Rule 1014(g) Regarding Specialist Enhanced Participation

November 19, 1999.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on October 4, 1999, the Philadelphia Stock Exchange, Inc. ("Phlx") or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. On November 4, 1999, the Exchange submitted Amendment No. 1 to the proposed rule change.³ 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 proposes to amend Phlx Rule 1014, "Obligations and Restrictions Applicable to Specialists and Registered Options Traders," and its corollary Option Floor Procedure Advice B-6 to revise the enhanced participation available to Exchange specialists. Under the proposal, if three or more controlled accounts⁴ are on parity with an Exchange specialist, the specialist will receive 30% of the contracts of the initiating order.

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 Phlx 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 Phlx 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

a. Background

On August 26, 1994, the Commission approved the Exchange's proposal to adopt and enhanced participation for Exchange specialists in equity options.⁵ The enhancement, or "enhanced parity split," provided Exchange specialists with a greater participation in parity trades than the specialists would otherwise be entitled to receive. Initially, the enhanced parity split was approved as a one year pilot expiring August 26, 1995. On November 30, 1994, the Commission approved the Exchange's proposal to make the enhanced parity split available to index option specialist.⁶ The enhanced parity split was later revised with respect to situations where less than three controlled accounts are on parity with a specialist.⁷ The enhanced parity split was renewed unaltered and on a continuing pilot basis on three subsequent occasions.⁸ Thereafter, the enhanced parity split was extended until December 31, 1998, and revised or that it would apply to: (1) All index options; (2) 50% of each specialist's equity options; and (3) all new options allocated to a specialist during the year. In addition, specialists were permitted to revised the list of eligible equity options on a quarterly basis, instead of annually.⁹ Finally, in July 1999, the enhanced parity was permanently approved.¹⁰

⁵ See Securities Exchange Act Release No. 34606 (August 26, 1994), 59 FR 45741 (September 2, 1994).

⁶ See Securities Exchange Act Release No. 35028 (November 30, 1994), 59 FR 63151 (December 7, 1994).

⁷ See Securities Exchange Act Release No. 35429 (March 1, 1995), 60 FR 12802 (March 8, 1995).

⁸ See Securities Exchange Act Release Nos. 36122 (August 18, 1995), 60 FR 44530 (August 28, 1995); 37254 (August 5, 1996), 61 FR 42080 (August 13, 1996); and 38924 (August 11, 1997), 62 FR 44160 (August 19, 1997).

⁹ See Securities Exchange Act Release No. 39401 (December 4, 1997), 62 FR 65300 (December 11, 1997).

¹⁰ See Securities Exchange Act Release No. 41588 (July 1, 1999), 64 FR 37185 (July 9, 1999). The Exchange also received approval to give specialists and enhanced parity split when they develop and trade a new product. The enhanced parity split works as follows: when the specialist is on parity with three or more controlled accounts, the specialist receives 40% of the contracts and the controlled accounts receive the remaining 60%.

Currently, the enhanced parity split applies to orders for more than five contracts. Specifically, when an equity or index option specialist is on parity with one controlled account, the specialist receives 60% of the initiating order and the controlled account receives 40%. When the specialist is on parity with two controlled accounts, the specialist receives 40% of the initiating order and each controlled account receives 30%. When the specialist is on parity with three or more controlled accounts, the specialist is counted as two crowd participants when dividing up the contracts. In any of these situations, if a customer is on parity, the customer will not be disadvantaged by receiving a lesser allotment than any other crowd participant, including the specialist.

b. Proposal

The Exchange proposes to revise the manner in which the enhanced parity split operates. Specifically, in those cases where the specialist is on parity with three or more controlled accounts, the specialist will receive 30% of the contracts instead of being counted as two crowd participants. However, if a customer is on parity, the customer will not be disadvantaged by receiving a lesser allotment than any other crowd participant including the specialist. Pursuant to the current text of the rule, the Exchange will continue to limit the enhanced parity split to 50% for each of the specialist unit's equity issues.

The Exchange believes that fixing the percentage of an order that a specialist receives under the enhanced parity split should provide more certainty because a fixed percentage is ascertained more easily than a percentage that varies depending on the number of controlled accounts on parity. In addition, in larger crowds, a specialist may not receive a significant enhanced participation using the current two-for-one split because the potentially large number of controlled accounts on parity would significantly dilute the specialist's share of the order. For example, if there are seventy controlled accounts on parity, and there is an initiating order for seventy contracts, the specialist will only receive two contracts and the rest of the crowd will divide the remaining sixty-eight. However, with the proposed 30% enhanced parity split, the specialist will receive twenty-one contracts and the

When the specialists is on parity with less than three controlled accounts in the crowd, the specialist receives 60% of the contracts and the controlled accounts receive 40%. In either these situations, if a customer is on parity, the customer may not receive a lesser allotment than any other crowd participant including the specialist.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, the Exchange made technical changes to the proposal. See letter from Nandita Yagnik, Phlx, to Richard Strasser, Assistant Director, Division of Market Regulation, Commission, dated November 3, 1999 ("Amendment No. 1").

⁴ Pursuant to Phlx Rule 1014(g)(i), a controlled account includes any account controlled by or under the common control with a member broker-dealer.

rest of the crowd will divide the other forty-nine equally. Thus, the 30% enhanced parity split should help to ensure that specialists in larger crowds receive participations that encourage them to make deep and liquid markets.¹¹ In addition, the proposal should allow the Exchange to recruit and retain well-capitalized specialists who attract order flow to the Exchange.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6 of the Act,¹² in general, and with Section 6(b)(5),¹³ in particular, in that it is designed to promote just and equitable principles of trade; prevent fraudulent and manipulative acts and practices; foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities; remove impediments to and perfect the mechanism of a free and open market and a national market system; and protect investors and the public interest. The Exchange further believes that the proposal balances the competing interests of specialists and market makers while helping specialists protect the public interest by making tight and liquid markets in assigned issues.

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

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

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.

¹¹ In those instances where three of four controlled accounts are on parity, the Exchange recognizes that the proposed 30% enhanced parity split will provide specialists with a lesser number of contracts than under the current two-for-one enhanced parity split. For example, if there is an initiating order of fifty contracts, and three controlled accounts are on parity, the specialist will currently receive twenty contracts and the controlled accounts will each receive ten contracts. In contrast, under the proposed 30% enhanced parity split the specialist will only receive fifteen contracts. However, the Exchange believes that the proposed 30% enhanced parity split will provide a more equitable treatment to all specialists such that specialists of both large and small crowds shall receive a significant enhanced participation when there are five or more controlled accounts on parity. See Amendment No. 1, *supra* note 3.

¹² 15 U.S.C. 78f.

¹³ 15 U.S.C. 78f(b)(5).

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

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

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-PHLX-99-39 and should be submitted by December 21, 1999.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁴

Margaret H. McFarland,

Deputy Secretary.

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DEPARTMENT OF TRANSPORTATION

Office of the Secretary

Aviation Proceedings, Agreements Filed During the Week Ending November 19, 1999

The following Agreements were filed with the Department of Transportation under the provisions of 49 U.S.C. Sections 412 and 414. Answers may be filed within 21 days of date of filing.

Docket Number: OST-99-6508.

Date Filed: November 16, 1999.

Parties: Members of the International Air Transport Association.

Subject:

Mail Votes 037 and 038

PTC12 NMS-ME 0092 dated 20

September 1999

Mid Atlantic-Middle East Resolutions r1-r10

PTC12 NMS-ME 0093 dated 20

September 1999

South Atlantic-Middle East

Resolutions r11-r22

PTC12 NMS-ME 0097 and 0098 dated 5 November 1999

Adoption of Mail Votes 037 and 038

Minutes—PTC12 NMS-ME 0095

dated 1 October 1999

Tables—PTC12 NMS-ME Fares 0052

and 0053 dated 12 November 1999

Intended effective date: 1 April 2000

Docket Number: OST-99-6511.

Date Filed: November 16, 1999.

Parties: Members of the International Air Transport Association.

Subject:

PTC23 ME-TC3 0077 dated 8 October 1999

Middle East-TC3 except South East

Asia Resolutions r1-r43

PTC23 ME-TC3 0081 dated 2

November 1999 Technical

Correction

PTC23 ME-TC3 0078 dated 14

October 1999 (Mail Vote 041)

Middle East-South East Asia

Resolutions r44-r58

PTC23 ME-TC3 0082 dated 9

November 1999 (Adoption Mail

Vote 041)

Minutes—PTC23 ME-TC3 0080 dated 29 October 1999

Tables—PTC23 ME-TC3 Fares 0038

dated 15 October 1999 and PTC23

ME-TC3 Fares 0040 dated 12

November 1999

Intended effective date: 1 April 2000

Docket Number: OST-99-6512.

Date Filed: November 16, 1999.

Parties: Members of the International Air Transport Association.

Subject:

PTC1 0126 dated 16 November 1999

Mail Vote 050 Resolution 010s

TC1 Special Passenger Amending

¹⁴ 17 CFR 200.30-3(a)(12).