security except at a price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security.

8. Ohio National's recapture of the Credit might arguably be viewed as resulting in the redemption of redeemable securities for a price other than one based on the current net asset value of the Account. Applicants contend, however, that the recapture of the Credit does not violate Section 22(c) and Rule 22c–1. To effect a recapture of a Credit, Ohio National will redeem interests in an owner's Account at a price determined on the basis of the current net asset value of that Account. The amount recaptured will equal the amount of the Credit that Ohio National paid out of its general account assets. Although the owner will be entitled to retain any investment gain attributable to the Credit, the amount of that gain will be determined on the basis of the current net asset value of the Account. Thus, no dilution will occur upon the recapture of the Credit. Applicants also submit that the second harm that Rule 22c–1 was designed to address, namely speculative trading practices calculated to take advantage of backward pricing, will not occur as a result of the recapture of the Credit. However, to avoid any uncertainty as to full compliance with the Act, Applicants request an exemption from the provisions of Section 22(c) and Rule 22c–1 to the extent deemed necessary to permit them to recapture the Credit under the Contracts.

Conclusion

Applicants submit, based on the grounds summarized above, that their exemptive request meets the standards set out in Section 6(c) of the Act, namely, that the exemptions requested are necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act, and that, therefore, the Commission should grant the requested order.

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

Jonathan G. Katz,

Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42807; File No. SR–ISE–00–03]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 by the International Securities Exchange LLC Relating to Block and Facilitation Trades

May 22, 2000.

I. Introduction

On February 25, 2000, the International Securities Exchange LLC (''ISE'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 29b–4 thereunder,[2] a proposed rule change relating to its proposed block order and facilitation mechanisms.

The proposed rule change was published for comment in the **Federal Register** on March 6, 2000.[3] The Commission received three comment letters regarding the proposal.[4] On May 19, 2000, the ISE filed Amendment No. 1 to the proposed rule change.[5] This order approves the proposed rule change. In addition, the Commission is publishing this notice to solicit comments on Amendment No. 1 and is simultaneously approving Amendment No. 1 on an accelerated basis.

II. Description of the Proposal

ISE Rule 716(c) establishes a ''block mechanism'' through which ISE members can obtain liquidity for the execution of block-size orders[6] from market makers and other ISE members with orders at the ISE inside bid or offer (''Crowd Participants''). Similarly, ISE Rule 716(d) establishes a ''facilitation mechanism'' through which members can seek to facilitate block-size public customer orders. Upon the entry of an order into the block or facilitation mechanisms, a broadcast message is sent to the Crowd Participants.

The proposed rule change contains several proposed revisions to existing ISE Rule 716. First, the ISE has proposed commentary to ISE Rules 716(c) and (d) with respect to the block order mechanism and the facilitation mechanism, specifying that participants will be given 30 seconds to respond to a broadcast message from either the block or facilitation mechanism.

Second, the ISE proposes to amend ISE Rule 716(d)(4)(i) to provide that only public customer bids (offers) on the Exchange at the time a facilitation order is executed that are priced higher (lower) than the facilitation price will be executed at the facilitation price, unless there is sufficient size to execute a facilitation order entirely at a better price. Higher bids and lower offers from non-customer orders and quotes will be executed at their stated price. The current rule provides non-customer orders and quotes the benefit of the facilitation or ''block clean-up'' price.

Third, ISE is proposing amendments to ISE Rule 716(d)(4)(ii)[7] to eliminate a Primary Market Maker's (''PMM'') participation right with respect to the allocation of orders entered into the facilitation mechanism by deleting a reference to ISE Rule 713.[8] In other words, under ISE's proposed amendments to ISE Rule 716(d)(4)(ii), if a PMM is among the Crowd Participants with interest at the facilitation price, the PMM will be treated the same as all other Crowd Participants and not given a preferential allocation under ISE Rule 713.

Finally, ISE is proposing to amend ISE Rule 716(d)(2) and (3)[9] to clarify that a Crowd Participant may enter into the facilitation mechanism an indication at a better price than the facilitation price, but only if such better price is inferior to the ISE best bid or offer. If a Crowd Participant wishes to enter an indication at a price equal to or better than the ISE best bid or offer, the Crowd Participant may do so only by changing its quote or entering an order, so that

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Securities Exchange Act Release No. 42473 (February 29, 2000), 65 FR 11818.

[4] *See* letters to Jonathan G. Katz, Secretary, SEC, from Holly H. Smith, Sutherland, Asbill & Brennan LLP, dated March 24, 2000 (''SA&B Letter''); Peter J. Chepucavage, Fulbright 7 Jaworski L.L.P., dated March 28, 2000 (''Phlx Letter''); and Charles J. Henry, President and Chief Operating Officer, Chicago Board Options Exchange, dated March 31, 2000 ''CBOE Letter'').

[5] *See* letter from Katherine Simmons, Vice President and Associate General Counsel, ISE, to Deborah Flynn, Senior Special Counsel, Division of Market Regulation, SEC, dated May 19, 2000 (''Amendment No. 1''). In Amendment No. 1, ISE proposes to delete a reference to ISE Rule 713 to eliminate a Primary Market Maker's participation right with respect to facilitation orders. ISE also proposes to clarify that members may enter indications at prices that improve the facilitation price if such improved price is inferior to the ISE best bid or offer.

[6] For purposes of ISE rules only, block-size orders are orders for fifty contracts or more. *See* ISE Rule 716(a).

[7] *See* Amendment No. 1, *supra* note 5.

[8] ISE Rule 713 sets forth the PMM's allocation algorithm. *See* Securities Exchange Act Release No. 42808.

[9] *See* Amendment No. 1, *supra* note 5.

such interest will be disseminated to the public.

III. Summary of Comments

The Commission received three comment letters on the proposal. [10] These commenters opposed ISE's proposed rule change, as originally proposed.[11] Commenters argued that the proposed 30 second response time would make it easier for ISE members to execute as principal their own customers' orders for 50 contracts or more without meaningful opportunity for price improvement by competitors, which they argued would undermine the intended purpose of having customers' orders reasonably exposed to other trading interest before being executed by the facilitating ISE member.[12] Moreover, this proposed 30 second response time, commenters emphasized, is not enough time for market participants to have a reasonable opportunity to improve the facilitation price, especially because Crowd Participants who wish to improve the price are required by the rules to do so 10 seconds prior to the expiration of the 30 second time period, effectively reducing the response time to 20 seconds.[13]

In response to commenters' objections to the proposed 30 second ''exposure period,'' ISE states that 30 seconds is sufficient time for Crowd Participants in the ISE market to respond to an order, noting that the Commission has approved exposure times of as few as 15 seconds for certain equity exchanges.[14] ISE notes that floor-based exchanges have no specific limitation on how long a proposed facilitation order must be exposed to the crowd before it is executed. Moreover, ISE states that commenters have no basis to assert that 20, 30 or 60 seconds is the appropriate exposure time, given the lack of precedent for an electronic options market.[15] ISE asserts that, based upon consultation with its members and using the knowledge and understanding of electronic trading it has developed, its proposal is reasonably designed to protect both customers and liquidity providers in its electronic marketplace and is consistent with the requirements of the Act.[16]

Commenters also objected to the proposed amendment requiring non-customer bids (offers) priced higher (lower) than the facilitation price to be executed at their stated price, rather than a single ''clean-up'' price.[17] The commenters argued that the ISE's proposal would act as a disincentive to ISE Competitive Market Makers (''CMMs'') and other Electronic Access Members (''EAMs'') to display their true trading interest and offer price improvement, because a CMM who wants to trade, but cannot facilitate the entire order at an improved price, will likely elect not to offer any price improvement to avoid the ''penalizing impact'' of the rule.[18]

In response, ISE argues that this proposed amendment benefits customers because where a non-customer (*i.e.,* broker-dealer or market maker) indicates that it is willing to trade at a price that is better than the facilitation or ''clean-up'' price, the customer order being facilitated would get the benefit of the better price, even if the entire order cannot be executed at the better price.[19] The ISE believes that the effect of the proposed change will be to increase opportunities for price improvement for customer orders.[20]

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether the proposed amendment is consistent with the Act. Persons making written submission 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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the ISE. All submissions should refer to File No. SR–ISE–00–03 and should be submitted by June 20, 2000.

V. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.[21] In particular, the Commission finds that proposal is consistent with Section 6(b)(5) of the Act.[22]

Under Section 6(b)(5) of the Act,[23] a registered national securities exchange must have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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, and, in general, to protect investors and the public interest.

Specifically, the Commission finds that ISE's proposed commentary to ISE Rule 716 establishing the ''exposure time'' for a facilitation order at 30 seconds is consistent with Section 6(b)(5) of the Act.[24] Currently, there is no time period specified in the ISE's rules for how long facilitation orders must be exposed to the trading crowd. Instead, the amount of time to respond is set by the Exchange. The Commission believes that setting out in the ISE's rules the response period will provide certainty to the other market participants and ensure that this time period will not be changed without a corresponding change in the ISE rules. On floor-based exchanges, there are no rules that govern how long an order, including a proposed facilitation order, must be exposed to the crowd before it is executed. In addition, in the Commission's view, 30 seconds is a reasonable time frame for Crowd Participants in ISE's market to assess market conditions and their own trading interest and to enter a response to a facilitation order. Accordingly, the Commission is approving the ISE's proposed commentary to ISE Rule 716.

[10] *See* note 4, *supra.*

[11] The Commission notes that commenters expressed views on a number of issues related to the ISE block and facilitation mechanisms that were outside the scope of the current ISE proposal, several of which were addressed in the Commission's approval of ISE as a national securities exchange. *See* Securities Exchange Act Release No. 42455 (February 24, 2000, 65 FR 11388. Consequently, this order addresses only comments regarding those issues presented by the current proposal.

[12] *See* SA&B Letter; Phlx Letter; CBOE Letter.

[13] *See* SA&B Letter; Phlx Letter.

[14] *See* letter to Jonathan G. Katz, Secretary, SEC, from Katherine Simmons, Vice President and Associate General Counsel, ISE, dated May 19, 2000 (''ISE Response Letter'').

[15] *Id.*

[16] *Id.*

[17] *See* SA&B Letter; Phlx Letter.

[18] *Id.*

[19] *See* ISE Response Letter.

[20] *Id.*

[21] In approving this rule, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[22] 15 U.S.C. 78f(b)(5).

[23] *Id.*

[24] *Id.*

The Commission also agrees with the ISE that public customer bids (offers) on the Exchange at the time a facilitation order is executed that are priced higher (lower) than the facilitation price should be executed at the facilitation price. The Commission believes that this proposal will both protect public customer limit orders on the ISE's book and provide public customers with the benefit of price improvement through the facilitation mechanism. The Commission also believes that allowing the execution of higher bids and lower offers from non-customer orders and quotes by executing them at their stated price is reasonable. Accordingly, the Commission finds that the proposed amendment to ISE Rule 716(d)(4)(i) is consistent with Section 6(b)(5) of the Act [25] in that it promotes just and equitable principles of trade and facilitates transactions in securities by allowing the partial execution of a facilitation order at an improved price for the number of non-customer contracts available, while protecting public customer orders on the book by giving them the benefit of a better execution price.

The Commission also finds that the proposed amendments to ISE Rule 716(d)(4)(ii) are consistent with Section 6(b)(5) of the Act.[26] Under current ISE rules, a PMM is guaranteed certain participation rights in a facilitation order after public customer orders are executed and the facilitating EAM receives an allocation of 40 percent of the order. Amendment No. 1 eliminates the PMM's participation guarantee. Thus, any indication or quote by a PMM will be treated the same as other Crowd Participants' interest. The Commission believes that this proposed amendment is consistent with the public interest, and that it promotes just and equitable principles of trade by ensuring that market makers will be able to compete in a fair and equitable manner, based on the competitiveness of their quotes, for that portion of an order remaining after public customer interest and the EAM's facilitation guarantee.

The Commission finds good cause for approving this proposed amendment prior to the thirtieth day after date of publication of the notice of filing in the **Federal Register**. The proposed change to paragraph (d)(4)(ii) of ISE Rule 716 makes available to Crowd Participants a greater percentage of facilitation orders. [27] Specifically, this change ensures that, if a PMM is among the Crowd Participants with interest at the facilitation price, the PMM will be treated equally with all other Crowd Participants, rather than being ''guaranteed'' special participation rights. Because this amendment reduces the guarantees to PMMs, the Commission believes it will increase the opportunity for other participants in ISE to complete for order flow and finds that granting accelerated approval to the proposed amendments to ISE Rule 716(d)(4)(ii) in Amendment No. 1 consistent with Section 18(b)(2) Act. [28]

Finally, the Commission believes that ISE's proposed amendment to ISE Rules 716(d)(2) and (3) to clarity that members may enter indications into the facilitation mechanism at prices that improve the facilitation price, if such improved price is inferior to the ISE best bid or offer, is consistent with the Act. ISE's rules currently state that indications from Crowd Participants must be priced *at* the price of the order to be facilitated and must not exceed the size of the order to be facilitated. To facilitate the order at a price superior to the facilitation price, ISE's current rules require Crowd Participants to enter orders change their quotes, as applicable. The proposed amendment allows a Crowd Participant to enter an indication to facilitate an order at a price better than the facilitation price, but inferior to the ISE best bid or offer. Without this change, it would have been possible for a Crowd Participant to improve the facilitation price, but not be at the ISE best bid or offer. In this situation, only the PMM [29] would know about the improved price, creating the potential for PMM to benefit at the expense of the customer order being facilitated. For these reasons, the Commission finds that ISE's proposed amendment is consistent with Section 6(b)(5) of the Act [30]

The Commission also finds good cause for approving the proposed amendments of ISE Rules 716(d)(2) and (3) prior to the thirtieth day after the date of publication of notice of filing in the **Federal Register**. These proposed changes eliminate a potential avenue for abuse and ensure that a public customer order would receive the benefit of any price offered that is better than the facilitation price. Accordingly, the Commission believes that these proposed amendments do not significantly alter the original proposal, which was subject to a full notice and comment period and addresses the issued raised by commenters. Therefore, the Commission finds that granting accelerated approval to the proposed changes to ISE Rules 716(d)(2) and (3) in Amendment No. 1 is consistent with Section 19(a)(2) of Act. [31]

VI. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, [32] that the proposed rule change (SR–ISE–00–03), including Amendment No. 1, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[33]

Margaret H. McFarland,

Deputy Secretary.

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[25] *Id.*

[26] *Id.*

[27] *See* Amendment No. 1, *supra* note 5.

[28] 15 U.S.C. 78f(b)(2).

[29] Under ISE's rules, only the PMM has access to all orders on the ISE book; not just the top of the book.

[30] 15 U.S.C. 78f(b)(5).

[31] 15 U.S.C. 78f(b)(2).

[32] *Id.*

[33] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42808; File No. SR–ISE–00–01]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 by the International Securities Exchange LLC Relating to Market Maker Allocations

May 22, 2000.

I. Introduction

On February 25, 2000, the International Securities Exchange LLC (''ISE'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission''), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] a proposed rule change relating to its proposed market maker allocation algorithm.

The proposed rule change was published for comment in the **Federal Register** on March 6, 2000.[3] The Commission received three comment letters regarding the proposal.[4] On May 19, 2000, the ISE filed Amendment No.

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Securities Exchange Act Release No. 42473 (February 29, 2000), 65 FR 11818.

[4] *See* letters to Jonathan G. Katz, Secretary, SEC, from Holly H. Smith, Sutherland, Asbill & Brennan LLP, dated March 24, 2000 (''SA&B Letter''); Peter J. Chepucavage, Fulbright & Jaworski L.L.P., dated March 28, 2000 (''Phlx Letter''); and Charles J. Henry, President and Chief Operating Officer, Chicago Board Options Exchange, dated March 31, 2000 (''CBOE Letter'').