

The sole issue, then, is whether in the instant proposal the crowd members in fact have a reasonable time and opportunity to respond to the broadcast message and compete for the order. As discussed above, the Commission believes that an exposure period of ten seconds on an electronic exchange such as the ISE affords an adequate opportunity for crowd members to respond in such a venue. Therefore, the Commission does not agree with the view of some commenters that an electronic exchange must accommodate manual responses by market makers.

With regard to the comment that floor-based exchanges allow for a "probe phase" before a facilitation cross is bid and offered, which may serve to decrease the possibility of "biased crosses" on those exchanges, the Commission believes that the need for this process on exchange floors may reflect a weakness of incentives on these floors to maintain or respond with quality quotes in the first place.

Accordingly, the Commission believes that it is appropriate for the Exchange to reduce the length of the Facilitation Mechanism's exposure period to 10 seconds. The Commission, however, intends to monitor closely the impact of this reduced exposure period. Therefore, the Commission has requested from the ISE, and the ISE has agreed to provide, statistics reflecting, for each month, the contract and trade volume of transactions executed through the Facilitation Mechanism as compared to total contract and trade volume executed on the Exchange; the extent to which crowd participants traded with orders submitted through the Facilitation Mechanism; and the extent to which EAMs submitting orders through the Facilitation Mechanism traded as principal with such orders.

The Commission also notes its agreement with the comment that an EAM that trades against part or all of a customer's order must satisfy its fiduciary duty to that customer of best execution. The Commission's approval of the proposed rule change in no way relieves a firm from best execution analysis of trades it executes through the ISE's Facilitation Mechanism. For example, if a firm believes it can obtain better terms for its customer by exposing that customer's order to the auction on the floor of another exchange, it may be obligated to do so, depending on the

rule. The Commission further does not believe that this result is significant to market makers, except in the case of orders of unusual size. Moreover, a large institutional customer with an order of unusual size may turn to another venue for facilitation if it is concerned that it will not see price improvement because of this dynamic.

totality of facts and circumstances surrounding the facilitation and the customer's best interests. Moreover, if a firm cancels a customer order after it has been submitted into the Facilitation Mechanism, an investigation into the reason the order was canceled, and whether the customer received a better price elsewhere, may be warranted.

The Commission finds good cause for approving Amendment No. 1 to the proposal prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**.

Amendment No. 1 revised the proposed rule change to provide an exposure period of 10 seconds, affording more time for the ISE crowd to respond to facilitation broadcasts than under the original proposal. Thus, the amendment should alleviate somewhat concerns about shortening the Facilitation Mechanism's exposure time, and does not raise any other regulatory issues. Accordingly, the Commission finds good cause, consistent with Sections 6(b)(5) <sup>73</sup> and 19(b)(2) <sup>74</sup> of the Act to accelerate approval of Amendment No. 1 to the proposed rule change.

## V. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether the amendment 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 ISE. All submissions should refer to File No. SR-ISE-2001-19 and should be submitted by October 16, 2002.

## VI. Conclusion

For the reasons discussed above, the Commission finds that the proposal is consistent with the Act and the rules and regulations thereunder.

<sup>73</sup> 15 U.S.C. 78f(b)(5).

<sup>74</sup> 15 U.S.C. 78s(b)(2).

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (SR-ISE-2001-19), as amended, be and hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>75</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46505; File No. SR-Phlx-2001-104]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the Philadelphia Stock Exchange, Inc. Relating to Clerks on the Exchange's Options Floor

September 17, 2002.

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 December 18, 2001, 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 Phlx. On June 27, 2002, the Phlx submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Phlx proposes to adopt Exchange Rule 1090, Clerks, which would define and set forth permitted and prohibited activities of Clerks on the Exchange's Options Floor.

<sup>75</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> See letter from Richard S. Rudolph, Director and Counsel, Phlx, to Nancy J. Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated June 26, 2002 ("Amendment No. 1"). In Amendment No. 1, the Phlx: (1) Made technical and clarifying changes to the proposed rule text; (2) added proposed Commentaries .01 and .02 to proposed Phlx Rule 1090 to define and set forth additional requirements for Stock Execution Clerks and Specialist Clerks; and (3) provided additional clarifying explanations with respect to the proposed rule change.

Below is the text of the proposed rule change. Proposed new language is italicized.

\* \* \* \* \*

Rule 1090. The term "Clerk" means any registered on-floor person employed by or associated with a member, member organization, participant, or participant organization who is not a member and is not eligible to effect transactions on the Options Floor as a Specialist, Registered Options Trader, or Floor Broker. For purposes of this Rule, an Inactive Nominee shall be deemed a Clerk.

(a) Badges. While on the trading floor, Clerks shall display prominently at all times the badge(s) supplied to them by the Exchange.

(b) Conduct on the Trading Floor. Clerks shall be primarily located at a post assigned to their employer or assigned to their employer's clearing firm unless such Clerk is:

(i) entering or leaving the trading floor;

(ii) transmitting, correcting, or checking the status of an order or reporting or correcting an executed trade;

(iii) supervising other Clerks of his member organization if he is identified as a supervisor on the registration form submitted to the Exchange's Membership Services Department.

(c) Registration Requirements. A member or member organization who employs a Clerk that performs any function other than a solely clerical or ministerial function shall, prior to the time such Clerk performs any function as a Clerk, (i) comply with the registration requirement(s) set forth in Exchange Rule 604, where applicable; (ii) disclose in detail to the Exchange, on an annual basis, the specific nature of such additional function(s); and (iii) submit to the Exchange written supervisory procedures relating to such Clerk's activities in accordance with Exchange Rule 748.

(d) Clerks' Use of Vendor Quote Terminals, DOT, and Other Order-Entry Devices. A Clerk may enter an order under the direction of a member by way of a vendor quote terminal, DOT machine, or any other order entry device.

#### Commentary

##### .01 Stock Execution Clerks

(a) Definition. A Stock Execution Clerk is any person other than a Specialist Clerk on the Exchange Floor who functions as an intermediary in a transaction (A) consummated on the Exchange; (B) entered verbally for execution other than on the Exchange;

or (C) entered into a third party system designed to execute transactions other than on the Exchange.

(b) Registration Requirements. Any member or member organization engaged as a Stock Execution Clerk shall register as such with the Exchange's Membership Services Department. A Stock Execution Clerk that performs any function other than a solely clerical or ministerial function shall, prior to performing any function as a Stock Execution Clerk, (i) comply with the registration requirement(s) set forth in Exchange Rule 604, where applicable; (ii) disclose in detail to the Exchange, on an annual basis, the specific nature of such additional function(s); and (iii) in accordance with Exchange Rule 748, submit to the Exchange written supervisory procedures relating to such member or member organization's activities as a Stock Execution Clerk.

(c) Clearing. All transactions by Stock Execution Clerks shall be carried by an NASD member firm. Members and member organizations that function as Stock Execution Clerks shall determine whether their activities as Stock Execution Clerks require them to be registered as NASD members as provided in the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder.

(d) Limitations. No Stock Execution Clerk shall: (i) act as an intermediary in any transaction other than under the direct supervision of a member; (ii) enter into any clearing transaction or participate in any clearing process; (iii) have discretion or independent authority over any account or transaction.

##### .02 Specialist Clerks

(a) Definition. A Specialist Clerk is any on-floor person, not a member of the Exchange, employed by or associated with a member or member organization registered as a specialist.

(b) Registration Requirements. Any member or member organization that employs a Specialist Clerk shall register such Specialist Clerk with the Exchange's Membership Services Department. A Specialist Clerk that performs any function other than a solely clerical or ministerial function shall, prior to performing any function as a Specialist Clerk, (i) comply with the registration requirement(s) set forth in Exchange Rule 604, where applicable; (ii) disclose in detail to the Exchange, on an annual basis, the specific nature of such additional function(s); and (iii) in accordance with Exchange Rule 748, submit to the Exchange written

supervisory procedures relating to such Specialist Clerk's activities.

(c) Conduct on the trading floor. A Specialist Clerk is permitted to communicate verbal market information (i.e., bid, offer, and size) in response to requests for such information, provided that such information is communicated under the direct supervision of his or her member employer. A Specialist Clerk may consummate electronic transactions under the express direction of his or her member employer by matching bids and offers. Such bids and offers and transactions effected under the supervision of a member employer are binding as if made by the member employer.

\* \* \* \* \*

## 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 Exchange 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 Exchange 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

The Phlx proposes to define and set forth permitted and prohibited activities of Clerks on the Exchange's Options Floor.

#### a. Definition

Proposed Phlx Rule 1090 would define a Clerk as any registered on-floor person employed by or associated with a member, member organization, participant, or participant organization who is not a member and is not eligible to effect transactions on the Options Floor as a Specialist, Registered Options Trader, or Floor Broker. The purpose of this definition is to identify a category of all persons that are not members of the Exchange and who are not eligible to effect transactions, but are located on the Exchange's Options Floor.<sup>4</sup> Under proposed Phlx Rule 1090, Clerks would not be eligible to effect transactions on

<sup>4</sup> The Exchange notes that only Exchange members may bid for and offer securities in the open market on the Exchange Floor. See Exchange Rule 104.

the Exchange Options Floor, except in the specific circumstances set forth in proposed Commentary .02 (c) to proposed Phlx Rule 1090 relating to the matching of electronic bids and offers by a Specialist Clerk under the express direction of his or her employer.

Finally, the Exchange proposes that in order for the proposed rule to apply to all categories of registered persons located on the Exchange's Options Floor that are generally not eligible to effect transactions, Inactive Nominees would be deemed to be Clerks for purposes of the proposed rule.<sup>5</sup>

#### b. Badges

The Exchange proposes to require that Clerks, while on the trading floor, display prominently at all times the badge(s) supplied to them by the Exchange. The purpose of this provision is to ensure that Exchange members are made aware of the identity of all Clerks on the Options Floor, and that Exchange members seeking to effect transactions with other members are able to ascertain the status of those other members with whom they may enter into on-floor transactions.<sup>6</sup>

With respect to Inactive Nominees, the Phlx notes that the Exchange's Membership Services Department currently issues nonmember badges to Inactive Nominees, who are ineligible to effect transactions on the Options Floor. The Exchange's Membership Services Department also issues member badges to activated persons who are eligible to effect transactions on the Options Floor. All badges are issued on a daily basis. The Phlx believes that a further purpose of the badge requirement is to facilitate the Exchange's Market Surveillance Department in ascertaining the function of on-floor persons, and to surveil for violations of Exchange rules accordingly.<sup>7</sup>

<sup>5</sup> See Exchange Rule 21, which provides that the term "Inactive Nominee" shall mean a natural person associated with and designated by a member organization whom has applied for and been approved by the Admissions Committee for such status and is registered as such with the Office of the Secretary. An Inactive Nominee shall have no rights or privileges of membership unless and until the Inactive Nominee becomes a member of the Exchange pursuant to the By-Laws and Rules of the Exchange. An Inactive Nominee merely stands ready to assume legal title to a membership upon notice by the member organization to the Office of the Secretary to be transferred intra-firm on an expedited basis.

<sup>6</sup> Regulation 3 under Exchange Rule 60 requires persons on the Exchange's Options Floor to wear identification badges chest high in full view, and the badges must accurately reflect the respective person's associations and dual affiliations.

<sup>7</sup> The Exchange represents that it currently does not provide badges to Clerks based on the type of Clerk (*i.e.*, Specialist Clerks, Stock Execution Clerk). The Exchange does, however, provide different

#### c. Conduct on the Trading Floor

The Exchange proposes that a Specialist Clerk<sup>8</sup> would be permitted to consummate electronic transactions under the express direction of his or her member employer by matching electronic bids and offers. The purpose of this provision is to enable Clerks employed by specialists on the Options Floor to assist in matching electronic bids and offers once electronic orders become due for execution. According to the Exchange, such activity, generally administrative in nature, does not involve actual bidding or offering of securities, and could only be carried out by a Specialist Clerk under the direct supervision of his or her employer member. In no circumstance would any Clerk be allowed to consummate a face-to-face transaction with an Exchange member.<sup>9</sup> In order to ensure that transactions effected by Specialist Clerks matching electronic bids and offers are binding on members, the Exchange proposes to require that bids and offers and transactions effected by Specialist Clerks under the supervision of a member are binding as if made by the member employer.

The Exchange also proposes to require that Clerks be primarily located at a post assigned to their employer or assigned to their employer's clearing firm unless a Clerk is entering or leaving the trading floor; transmitting, correcting, or checking the status of an order or reporting or correcting an executed trade; and/or supervising other Clerks of his member organization if he or she is identified as a supervisor on the registration form submitted to the Exchange's Membership Services Department. The Exchange believes that

badges for Clerks and for members permitted to trade on the Phlx floor. The "member" badge includes a red square symbol that identifies such member as eligible to enter into transactions on the Exchange floor. Clerk badges do not include such a symbol. Inactive Nominees on the options trading floor are required to wear and display badges identifying them as nonmembers. See Amendment No. 1, note 3, *supra*.

<sup>8</sup> A Specialist Clerk is any on-floor person, not a member of the Exchange, employed by or associated with a member or member organization registered as a specialist. See proposed Phlx Rule 1090, Commentary .02(a).

<sup>9</sup> Exchange Option Floor Procedure Advice ("OFFPA") F-23 provides that Clerks, other than Specialist Clerks, are prohibited from maintaining a sustained presence in the trading crowd. In addition, Clerks are prohibited from requesting market quotations from a Specialist or ROT, except that a Specialist Clerk, under the supervision of a Specialist, may request the crowd's market in order to update disseminated markets or ascertain parity/priority splits in relation to the execution of an order. A sustained presence is defined as a period of time beyond such time that, under the prevailing circumstances, is needed by the Clerk to complete the allowable business function which brought the Clerk to that crowd in the first place.

this provision should facilitate the Exchange's Market Surveillance Department in ascertaining the function of Clerks on the Options Floor and ensure that Clerks are not in a position on the Options Floor to enter into transactions in securities with Exchange members without appropriate member employer supervision.

With respect to appropriate member employer supervision, the Exchange proposes to allow a Clerk to enter an order under the direction of a member via a vendor quote terminal, Designated Order Turnaround ("DOT") System machine, or any other order entry device. Such a Clerk would not have discretion over orders entered, nor be permitted to bid and/or offer through the use of an order entry device without the express direction of a member.<sup>10</sup>

#### d. Stock Execution Clerks

The proposed rule change would define a Stock Execution Clerk would be defined as any person, other than a Specialist Clerk on the Exchange Floor, who functions as an intermediary in a transaction (i) consummated on the Exchange; (ii) entered verbally for execution other than on the Exchange; or (iii) entered into a third party system designed to execute transactions other than on the Exchange.

According to the Exchange, a Stock Execution Clerk provides a service to Exchange members on the Options Floor by accepting orders for the purchase and sale of securities underlying options transactions. Once such orders are accepted, the Stock Execution Clerk forwards such orders to the appropriate marketplace for execution. The transactions executed are typically hedging transactions in underlying stocks for Exchange specialists and ROTs. The Exchange believes that the proposed rule would assist the Exchange in regulating the business activities of its members and member organizations that function as Stock Execution Clerks.

The Exchange proposes to require any member or member organization engaged as a Stock Execution Clerk to register as such with the Exchange's Membership Services Department. A Stock Execution Clerk that performs any function other than a solely clerical or ministerial function shall, prior to

<sup>10</sup> For example, a Registered Options Trader ("ROT") that instructs a Clerk to enter an order via an electronic order entry device would be required to specify whether the order is a buy or sell order; the number of contracts; whether it is a day good till canceled order; whether it is a market or limit order; and the account number. A member employer instructing his or her employee Clerk would be required to provide the same express direction.

performing any function as a Stock Execution Clerk, comply with the registration requirement(s) set forth in Exchange Rule 604, where applicable, disclose in detail to the Exchange, on an annual basis, the specific nature of such additional function(s), and submit to the Exchange written supervisory procedures relating to such activities as a Stock Execution Clerk in accordance with Exchange Rule 748. The Exchange believes that this provision would serve to assist the Exchange in regulating Stock Execution Clerks, and would subject Exchange members and member organizations to possible disciplinary action for failure to supervise their employee Stock Execution Clerks.

The Exchange proposes to require that Stock Execution Clerks clear transactions through an NASD member firm, and determine whether their activities as Stock Execution Clerks require them to be registered as NASD members.<sup>11</sup> The purpose of this provision is to ensure that the activities of Stock Execution Clerks are conducted consistently with the Act and the rules and regulations thereunder. According to the Exchange, the ability of the Exchange's Market Surveillance Department to surveil the activities of Stock Execution Clerks on an exchange floor other than its own is limited. The Exchange believes that this is the primary reason for the Commission's rule requiring NASD membership (and compliance with NASD rules, subject to NASD disciplinary jurisdiction), except in limited circumstances.

Finally, the Exchange proposes to provide that no Stock Execution Clerk may act as an intermediary in any transaction other than under the direct supervision of a member; enter into any clearing transaction or participate in any clearing process; nor have discretion or independent authority over any account or transaction. The purpose of this provision is to ensure that Stock Execution Clerks would not perform

<sup>11</sup> Section 15(b)(8) of the Act requires every broker-dealer registered with the Commission to become a member of the NASD unless the broker-dealer effects transactions in securities solely on a national securities exchange of which it is a member. 15 U.S.C. 78o(b)(8). Section 15(b)(9) of the Act provides the Commission with authority to exempt any class of broker-dealers from the requirement to become a member of the NASD. 15 U.S.C. 78o(b)(9). Rule 15b9-1 under the Act exempts members of a national securities exchange from becoming a member of the NASD if the entity (i) carries no customer accounts; and (ii) earns no more than \$1,000 annual gross income from securities transactions carried out otherwise than on an exchange of which it is a member. The gross income limitation does not apply to income derived from transactions (A) for the dealer's own account with or through another registered broker or dealer; or (B) through the Intermarket Trading System. 17 CFR 240.15b9-1.

duties customarily performed by a Registered Representative (necessitating NASD Series 7 qualification)<sup>12</sup> and to ensure that Stock Execution Clerks comply with applicable federal securities laws.<sup>13</sup>

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act,<sup>14</sup> in general, and furthers the objectives of section 6(b)(5) of the Act,<sup>15</sup> in particular, in that it is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to protect the investors and the public interest, and to promote just and equitable principles of trade by regulating the conduct of Clerks on the Exchange's Options Floor.

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

The Phlx 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 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 Exchange consents, the Commission will:

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

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

<sup>12</sup> Exchange Rule 604(a) provides that no member organization shall permit any natural persons to conduct a public business or duties customarily performed by a registered representative unless such person is registered and qualified as a Registered Representative. Exchange Rule 604(a)(ii) provides that a person is deemed to be a qualified Registered Representative if he or she maintains an effective Series 7 "Full Registration/General Securities Representative" registration or an equivalent predecessor of this examination/registration.

<sup>13</sup> Telephone conversation between Richard S. Rudolph, Director and Counsel, Phlx, and Frank N. Genco, Attorney, Division, Commission.

<sup>14</sup> 15 U.S.C. 78f(b).

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

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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, as amended, 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 principal offices of the Exchange. All submissions should refer to File No. SR-Phlx-2001-104 and should be submitted by October 16, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

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

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46513; File No. SR-SCCP-2002-03]

### **Self-Regulatory Organizations; Stock Clearing Corporation of Philadelphia; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Fees for Remote Competing Specialists**

September 18, 2002.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on August 6, 2002, the Stock Clearing Corporation of Philadelphia ("SCCP") 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 primarily by SCCP. The Commission is publishing this notice to solicit comments on the

<sup>16</sup> 17 CFR 200.30-3(a)(12).

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