against the regulatory objectives of the Exchange Act. Among other things, those objectives embody the concept that exchanges will deal fairly with the public; that exchanges will be organized in such a fashion as to ensure their continued viability in asserting self-regulatory oversight over their members; and that exchanges may, so far as is consistent with other regulatory objectives of the Act, maintain competitive viability with other exchanges. Applying these criteria, the Commission finds it in the public interest to declare effective the registration of the ISE on the basis of its present rules; and

It appearing to the Commission that the rules of the exchange provide for the expulsion, suspension or disciplining of a member for conduct or proceeding inconsistent with just and equitable principles of trade and declare that the willful violation of any provisions of the Exchange Act, or of any rule or regulation thereunder, shall be considered conduct or proceeding inconsistent with just and equitable principles of trade; and It further appearing that the exchange is so organized as to be able to comply with the provisions of the Exchange Act and the rules and regulations thereunder, and that the rules of the exchange are just and adequate to insure fair dealing and to protect investors; and

Finally, it appearing that the rules of the exchange do not impose any burden on competition that is not necessary or in furtherance of the purposes of the Exchange Act;

It is ordered that the application of the International Securities Exchange LLC for registration as a national securities exchange be, and hereby is, granted.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00–4977 Filed 3–1–00; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42456, File No. 4–429]

Joint Industry Plan; Notice of Filing of Proposed Option Market Linkage Plans by the American Stock Exchange, Chicago Board Options Exchange, Pacific Exchange, and Philadelphia Stock Exchange

February 24, 2000.

I. Introduction

On January 19, 2000, pursuant to Rule 11Aa3–2 under the Securities Exchange Act of 1934 (''Act'') [1] and an order issued by the Securities and Exchange Commission (''SEC'' or ''Commission''),[2] the American Stock Exchange LLC (''Amex''), Chicago Board Options Exchange, Inc. (''CBOE''), Pacific Exchange, Inc. (''PCX''), and Philadelphia Stock Exchange, Inc. (''Phlx'') filed with the Commission proposed plans for the purpose of creating and operating an inter-market option linkage (''plans'').[3] As discussed below, Amex and CBOE filed identical plans (the ''Amex/CBOE plan'') and PCX and Phlx filed separate plans. Although the four exchanges achieved consensus on the majority of issues pertaining to a linkage, disagreement remains on several significant matters. Specifically, the exchanges failed to agree about whether the linkage should require routing of orders based on price/time priority,[4] who should have access to the linkage, and the appropriate remedy owed when one market trades at a price inferior to that displayed on another market (known as a ''trade-through''). Pursuant to Rule 11Aa3–2(c)(1), the Commission is publishing this notice of, and soliciting comments on, the Amex/CBOE plan. The Commission is also publishing this notice of the PCX and Phlx plans, which differ from the Amex/CBOE plan with respect to certain elements which the Commission is considering including in a linkage plan [5] and as to which the Commission therefore also seeks comments.

II. Background

In 1975, Congress directed the Commission to oversee the development of a national market system.[6] At the time, the trading of standardized options was relatively new.[7] As a result, the Commission deferred applying to the options markets many of the national market system initiatives that applied to the equity markets to give options trading an opportunity to develop. Nevertheless, since the establishment of the options exchanges, the Commission has repeatedly called for market integration facilities for the options markets.[8] In 1991, in response

[1] 17 CFR 240.11Aa3–2.

[2] On October 19, 1999, the Commission issued an Order directing the exchanges to file a national market system plan for linking the options markets within 90 days. Securities Exchange Act Release No. 42029 (October 19, 1999), 64 FR 57674 (October 26, 1999) (''October 19, 1999 Order'').

[3] The Commission's October 19, 1999 Order also requested the International Securities Exchange (''ISE'') to participate with the options exchanges in the development of an inter-market linkage plan. The ISE has filed an application with the Commission to register as a national securities exchange. *See* Securities Exchange Act Release No. 41439 (May 24, 1999) 64 FR 29367 (June 1, 1999). The ISE submitted a plan identical to that filed by Amex and CBOE. Because the Commission has not approved the ISE's application for registration as a national securities exchange, however, the ISE may not be a signatory to a linkage plan at this time.

[4] Both PCX and Phlx propose price/time priority as an element of the linkage. Price/time priority generally requires that if an exchange receives an order but it is not the first exchange to display the best price, that exchange must route the order to the exchange that was first at the best price. PCX and Phlx propose a number of textual distinctions from the Amex/CBOE plan to incorporate price/time priority. In the Phlx plan, many of the proposed modifications to the Amex/CBOE plan relate to an expanded role for the facilities manager. Although the term ''facilities manager'' is not defined in the plans, it is presumed by the plans to be an outside vendor who may be selected to build and operate a system linking the options exchanges' existing systems.

[5] Rule 11Aa3–2 specifically provides that the Commission may approve a proposed national market system plan ''with such changes or subject to such conditions as the Commission may deem necessary or appropriate.''

[6] Pub. L. No. 94–29 Stat. 97 (1975).

[7] The trading of standardized options on securities exchanges began in 1973, with the organization of CBOE as a national securities exchange. *See* Securities Exchange Act Release No. 9985 (February 1, 1973) 1 S.E.C. Doc.11 (February 13, 1973). Subsequently, the Commission approved options pilot programs at Amex, Phlx, PCX, and the Midwest Stock Exchange (''MSE''). The New York Stock Exchange (''NYSE'') began trading options in 1985. *See* Securities Exchange Act Release No. 11144 (December 19, 1974) 40 FR 3258 (January 20, 1975); Securities Exchange Act Release No. 11423 (May 15, 1975) 6 S.E.C. Doc. 894 (May 28, 1975); Securities Exchange Act Release No. 12283 (March 30, 1976) 41 FR 14454 (April 5, 1976); Securities Exchange Act Release No. 13045 (December 8, 1976) 41 FR 54783 (December 15, 1976); and Securities Exchange Act Release No. 21759 (February 14, 1985) 50 FR 7250 (February 21, 1985). The MSE's options program was merged into the CBOE's program in 1979. The NYSE sold its options business to CBOE in 1997. Currently, Amex, CBOE, PCX, and Phlx are the only national securities exchanges that trade standardized options.

[8] *See* Report of the Special Study of the Options Markets to the Securities and Exchange Commission, 96th Cong., 1st Sess. (Comm. Print No. 96–IFC3, December 22, 1978) (examining the major issues of market structure in standardized options markets, including multiple trading); Securities Exchange Act Release No. 16701 (March 26, 1980) 45 FR 21426 (April 1, 1980) (deferring expansion of multiple trading to afford the options exchanges an opportunity to consider the development of market integration facilities); Securities Exchange Act Release No. 22026 (May 8, 1985) 50 FR 20310 (May 15, 1985) (urging options market participants to consider the development of market integration facilities); Directorate of Economic and Policy Analysis, ''The Effects of Multiple Trading on the Market for OTC Options'' (November 1986); Office of the Chief Economist, ''Potential Competition and Actual Competition in the Options Market'' (November 1986); Securities Exchange Act Release No. 26871 (May 26, 1989) 54 FR 24058 (June 5, 1989) (requesting comment on three measures, including an inter-market linkage). In 1989, the Commission adopted Rule 19c-5, which generally prohibits any exchange from adopting rules limiting its ability to list any stock option class because that option class is listed on another exchange. *See* Securities Exchange Act Release No. 26870 (May 26, 1989) 54 FR 23963 (June 5, 1989). In proposing Rule 19c-5, the Commission acknowledged that market integration facilities were unlikely to be built voluntarily if they were a prerequisite to

to these calls, four of the five options exchanges submitted a proposal for the development of a linkage.[9] The plan was never adopted, in part, because a consensus among the exchanges could not be achieved regarding the feasibility of implementing a single linkage plan.

In February of 1999, Chairman Levitt wrote to the options exchanges expressing the need to develop system linkages and data processing facilities between the options markets.[10] On October 1, 1999, the Chairman again wrote to the options exchanges requesting their cooperation and consensus on an inter-market linkage plan.[11] On October 19, 1999, with no substantial progress having been made by the options markets to develop a linkage, the Commission ordered the markets to submit a linkage plan within 90 days.[12] The Commission required that, at a minimum, any plan submitted under the October 19, 1999 Order must include uniform trade-through rules and an expanded definition of public customer to include agency orders presented by competing exchanges.[13] On January 19, 2000, Amex and CBOE submitted the Amex/CBOE plan and PCX and Phlx filed separate plans. The plans diverge on several fundamental issues, the details of which are discussed below.

III. Description of the Plans

The three different plans submitted by the respective exchanges reflect numerous areas of agreement between the exchanges.[14] A brief summary of each section of the plans, highlighting their distinctions, is provided below. The full text of the separate plans submitted by the options exchanges is available on the Commission's website at *www.sec.gov,* at the principal offices of the options exchanges, and at the Commission.

A. Definitions

Section 2 of each of the plans defines specific terms for purposes of the plans.[15] With minor exceptions, the definitions proposed in each of the plans are generally consistent. For example, the plans define three types of ''linkage orders'': (1) ''Principal acting as agent (''P/A'') order,'' defined as an order for the principal account of a ''market maker'' authorized to represent customer orders reflecting the terms of a related unexecuted customer order for which the market maker is acting as agent; (2) ''principal order,'' defined as an order for the principal account of an ''eligible market maker'' that is not a P/A order; and (3) ''satisfaction order,'' defined as an order for the principal account of an exchange member who initiated a trade-through that is sent through the ''linkage'' to satisfy the trade-through liability.

As discussed below, the plans differ on the extent to which market makers should get access to the linkage with respect to proprietary business. The definition of ''eligible market maker'' is important because it delineates which market makers are eligible to participate in the linkage for their proprietary accounts. An ''eligible market maker'' is defined in the plans of Amex, CBOE, and PCX with respect to an ''eligible options class,'' as a ''market maker'' that: (i) Is assigned to, and is providing two-sided quotations in, the eligible option class; (ii) is participating in its market's automatic execution system in such eligible option class; and (iii) is not prohibited from sending ''principal orders'' in such eligible option class through the linkage pursuant to the plan. These prohibitions are discussed below. Phlx would delete item (iii) of the definition to indicate its support for broader access to the linkage.

The term, ''firm customer quote size,'' is defined in each of the plans. Under the plans submitted by Amex, CBOE, and Phlx, the exchange that receives a linkage order that is for a customer (*i.e.,* non-broker-dealer) account must guarantee automatic execution for at least ten contracts and up to the number of contracts guaranteed automatic execution for orders entered directly on the exchange. PCX's plan would require that a market be firm for at least 20 contracts for linkage orders for customer accounts up to the same maximum as the others. All of the plans define ''firm principal quote size'' as the number of contracts for principal orders that a receiving exchange will guarantee to execute. This number is 10 contracts under all of the plans.

B. New Parties to the Plan

Section 4 of each of the plans contains an identical, self-effecting provision for the admission of new participants, in which eligible exchanges[16] may become a party to the plan by: (1) Executing a copy of the plan, as then in effect; (2) effecting an amendment to the plan reflecting the addition of the new participant's name; and (3) paying the applicable fee, as discussed below.

C. Administration of the Plan

Each of the plans provides, in Section 5, for an Operating Committee, to be composed of one representative of each participating exchange, responsible for: (1) Overseeing the development and implementation of the linkage; (2) monitoring the exchanges' use of the linkage; and (3) advising the participant exchanges regarding the operation of the linkage. The plans also uniformly provide for the creation of a Member Advisory Committee, to be composed of between one and three members from each participating exchange, to advise the Operating Committee on linkage matters. Each participating exchange would have one vote on all matters considered by the Operating Committee and the Member Advisory Committee, respectively. Votes, except as otherwise specified in the plan, would be decided by a majority of a quorum of the Operating Committee.

The plans uniformly propose that amendments to the plan, other than with respect to the addition of new participants, as discussed above, may be effected only with the unanimous approval of the participating exchanges, and the approval of the Operating Committee and the Commission. The plans also provide a mechanism for dispute resolution, as discussed below.

D. Linkage Overview

Section 6 of each of the plans sets forth the responsibilities of each participating exchange for providing a linkage supervisory function to oversee

multiple trading. *See* Securities Exchange Act Release No. 24613 (June 18, 1987) 52 FR 23849 (June 25, 1987). In 1990, then Chairman Breeden requested that the options exchanges develop an inter-market linkage plan. *See* Letter from Chairman Breeden to the Registered Options Exchanges dated January 9, 1990.

[9] *See* Securities Exchange Act Release No. 30187 (January 14, 1992) 57 FR 2612 (January 22, 1992) (soliciting comments on an inter-market linkage plan submitted by four out of five options exchanges).

[10] *See* Letters from Arthur Levitt, Chairman, SEC, to Richard F. Syron, Chairman and Chief Executive Officer, Amex; William J. Brodsky, Chairman and Chief Executive Officer, CBOE, Robert M. Greber, Chairman and Chief Executive Officer, PCX; and Meyer S. Frucher, Chairman and Chief Executive Officer, Phlx; dated February 10, 1999.

[11] *See* Letters from Chairman Levitt, to Salvatore Sodano, Chairman and Chief Executive Officer, Amex; William J. Brodsky, Chairman and Chief Executive Officer, CBOE; Philip D. DeFeo, Chairman and Chief Executive Officer, PCX; and Meyer S. Frucher, Chairman and Chief Executive Officer, Phlx; dated October 1, 1999.

[12] *See* note 2, *supra.*

[13] *Id.*

[14] As previously noted, Amex and CBOE filed identical plans and ISE has stated its intent to execute the Amex/CBOE plan as a signatory should the Commission grant the ISE's application for registration as a national securities exchange. *See* notes 3 and 4 and accompanying text, *supra.*

[15] Section 1 of the each plan contains a non-substantive preamble.

[16] The plans define an ''eligible exchange'' as a national securities exchange registered with the Commission pursuant to Section 6(a) of the Act, 15 U.S.C. 78f(a), that is a participant in the Options Clearing Corporation (''OCC'') and a party to the Options Price Reporting Authority (''OPRA'') Plan.

the linkage and resolve inter-market trade problems. Administrative messages, either in free form or fixed format, could be sent through the linkage under all of the proposals. The Operating Committee would be authorized to determine how the linkage should be built and operated, including whether to select a facilities manager. The Operating Committee's decisions with respect to the selection of a facilities manager would require an affirmative vote of at least two-thirds of the members of the entire Operating Committee.

With respect to the implementation of the linkage, the Amex/CBOE plan and the Phlx plan would grant the Operating Committee the authority to phase in the implementation of the linkage. The PCX, however, specifically proposes a multiple phase implementation, as discussed further below. Under the PCX plan, the participating exchanges would conduct a study to assess the impact of the linkage during Phase I and, based on that study, develop an amendment to the plan for a second phase.

E. Linkage Operations

In Section 7 of the plans, the exchanges set forth the specific mechanics of the linkage. With respect to eligible option classes, each participating exchange would be required to furnish to OPRA the current bid-ask quotation emanating from its market. These quotations would be considered ''firm'' to the extent provided in the plans.[17]

1. Amex/CBOE Linkage Plan

The Amex/CBOE linkage plan proposes that the linkage be used for either customer orders, where the market maker chooses not to ''step-up'' to match a better price displayed on an away market, or principal orders.

(a) P/A Orders Eligible for Automatic Execution

The Amex/CBOE linkage plan would permit the transmission of a P/A order for execution in the automatic execution system of a participating exchange at the best price (''NBBO'')[18] if the size of the P/A order is no larger than the firm customer quote size. The exchange receiving the P/A order through the linkage must execute it in its automatic execution system, if available, if its disseminated quotation is equal to or better than the limit price attached to the linkage order by the sending exchange (''reference price'')[19] when the order arrives at the receiving exchange. The receiving exchange must immediately report the trade to OPRA. Except in limited circumstances, the proposal would not permit customer orders larger than the firm customer quote size to be broken up into multiple orders. Members would be prohibited from sending P/A orders eligible for automatic execution at a price inferior to the NBBO.

(b) P/A Orders not Eligible for Automatic Execution

With respect to P/A orders not eligible for automatic execution in the receiving market because the size of the order is larger than the firm customer quote size, the Amex/CBOE linkage plan provides two alternatives. First, a P/A order representing the entire customer order may be sent through the linkage. If the receiving exchange's disseminated quotation is equal to or better than the reference price of the incoming linkage order, the receiving exchange must execute that order for at least the firm customer quote size. Within 15 seconds of receipt of the order, the receiving exchange must inform the sending exchange of the amount of the order that was executed and the amount, if any, that was canceled. In the alternative, the sending exchange may send an initial P/A order for the firm customer quote size. If the receiving exchange executes that order and continues to disseminate the same quote at the NBBO 15 seconds after reporting the execution of the initial P/A order, the sending exchange may send a second P/A order. If it chooses to send the second order, that order must be for the lesser of 100 contracts or the entire remainder of the customer order the sending exchange is representing. Under either alternative, if the receiving exchange does not execute the entire P/A order, it must move its quote to a price inferior to the reference price of the P/A order.

(c) Handling of Principal Orders

For principal orders, the Amex/CBOE proposal would allow eligible market makers, as defined above, to send orders on behalf of their principal trading accounts as principal orders at the NBBO. If the principal order is not larger than the ''firm principal quote size,'' the receiving exchange must execute the order in its automatic execution system, if available, if its disseminated quotation is equal to or better than the reference price when the order arrives at the receiving exchange. If the principal order is larger than the firm principal quote size, the receiving exchange must execute the order in its automatic execution system for at least the firm principal quote size and within 15 seconds of receipt of such order, inform the sending exchange of the amount of the order that was executed and the amount, if any, that was canceled. If the receiving exchange does not execute the entire principal order, it must move its quote to a price inferior to the reference price of the principal order. The sending exchange is not permitted to send a second principal order in the same eligible option class for at least 15 seconds after it sent the first principal order unless the receiving exchange changes its price and the price is at the NBBO. After the 15 second period, and until there is a change in the receiving exchange's disseminated quote, the exchange that initially sent the principal order for automatic execution may send only principal orders for greater than the firm principal quote size. The restriction on sending principal orders for automatic execution would expire one minute after the automatic execution of the first principal order.

(d) Obligations for Failure to Respond to Linkage Orders

A member that sends a P/A order or principal order through the linkage and who does not receive a reply within 30 seconds may reject any response received thereafter purporting to report a total or partial execution of that order. The member that sent the original order must inform the receiving exchange that it is rejecting the response within 15 seconds of receiving it. Upon receiving the rejection, the receiving exchange must report a cancellation to OPRA.

2. PCX Linkage Plan

The PCX proposal would incorporate a price/time priority feature into a phased implementation schedule for customer orders for 20 contracts or less.[20] Specifically, the PCX proposes

[17] The plans also uniformly propose procedures for the minimum information to be included in a linkage order, order validation, routing, responses, and partial executions.

[18] The plans uniformly define the term ''NBBO'' as the national best bid and offer in a series of an eligible option class calculated by a participating exchange.

[19] Except with respect to a ''satisfaction order,'' defined above, the reference price is equal to the quotation disseminated by the receiving exchange at the time the linkage order is transmitted. With respect to a ''satisfaction order,'' the reference price is the price to which the member in the sending exchange is entitled pursuant to the linkage plan.

[20] On November 10, 1999, Chairman Levitt requested the options exchanges and ISE to submit within thirty days a detailed statement of their views on whether incorporating price/time priority into an inter-market linkage plan would be beneficial to investors and the options markets. *See* Letters from Chairman Levitt, to Salvatore Sodano, Chairman and Chief Executive Officer, Amex; William J. Brodsky, Chairman and Chief Executive Officer, CBOE; Philip D. DeFeo, Chairman and

that during Phase I, customer orders for 20 contracts or less may be automatically executed by the exchange initially receiving the order only if that market is disseminating a quotation with price and time priority or, if the market is at the NBBO (although not first in time) and provides price improvement for that order.[21] If the exchange initially receiving the order is not at the NBBO when it receives the order, that exchange must automatically generate a P/A order and send it for execution to the away market that is disseminating a quotation with price and time priority, so long as the away market provides a firm customer quote size of at least 20 contracts in that particular eligible option class.

The PCX plan virtually mirrors the Amex/CBOE proposal with respect to the handling, during Phase I, of P/A orders not eligible for automatic execution in the receiving market (*i.e.,* orders for more than 20 contracts), principal orders, and other matters, such as restrictions on breaking up customer orders that are larger than the firm customer quote size. The PCX plan, however, differs from the other plans with respect to locked and crossed markets. The Amex/CBOE and Phlx plans propose language stating that the dissemination of locked and crossed markets must be avoided and that the participating exchanges will file with the Commission for approval uniform rules for unlocking and uncrossing markets. The PCX, conversely, would permit principal orders to be sent through the linkage for the purpose of unlocking or uncrossing markets.[22]

3. Phlx Linkage Plan

The Phlx proposal incorporates strict price/time priority, requiring each exchange to build a front-end system to route, as P/A orders, either directly through the linkage or to the facilities manager, all customer orders eligible for automatic execution where the exchange initially receiving the order was not the first to disseminate the best price. The Phlx proposal parallels the Amex/CBOE and PCX proposals with respect to other aspects of handling linkage orders for customer accounts, including the obligations on the exchange that receives a linkage order.

The Phlx plan tracks the Amex/CBOE and PCX plans with respect to the handling of principal orders, except that the Phlx proposal incorporates strict price/time priority and prohibits an eligible market maker from sending through the linkage principal orders not only at a price inferior to the NBBO, but also at a price equal to or inferior to the market quote disseminated on the eligible market maker's exchange.

4. ISE Alternative Proposal

In its transmittal letter, the ISE proposes an alternative plan for handling P/A orders. Under the terms of its proposal, member firms would be permitted to route orders to the exchange of their choice. If an exchange is quoting at the NBBO when it receives an order (regardless of whether it was the first market to quote at that price), that exchange would be permitted to execute the order and would owe no obligation to away markets. If, however, the exchange to which the order is initially routed by the member firm is not quoting at the NBBO when it receives the order, a market maker on that exchange may step up to match the best price and execute the order. If an away market that was quoting at the NBBO complains, however, the market that matched the NBBO would be required to provide ''specified protection'' [23] to those customer limit orders on the book of the complaining away market. If the exchange that receives the order from the member firm decides not to step up, it must route the order through the linkage based on price-time priority. The alternative proposal suggested by the ISE is here because it is not included in the plans submitted by the exchanges. Although the ISE's alternative proposal was not addressed specifically by any other exchanges, both Amex and CBOE's transmittal letters stated a commitment to further study the issue of customer limit order protection.

F. Implementation Obligations

1. Access to the Linkage

Section 8 of each of the plans sets forth, among other things, requirements relating to access to the linkage and order protection. With respect to P/A access, all of the plans agree that the linkage should not be used as an order delivery system in which all or a substantial portion of customer orders are routed through the linkage.

There are several significant differences between the plans with respect to appropriate limitations on principal access to the linkage. The Amex/CBOE plan proposes an ''80/20 Test,'' which would be applied each calendar quarter and would limit principal access in the subsequent calendar quarter based on customer order volume executed on the principal's exchange.[24] Under this test, a market maker that effected 20 percent or more of its market maker volume by sending principal orders through the linkage in a calendar quarter would be prohibited from sending principal orders through the linkage for the next calendar quarter (*i.e.*, would not be an ''eligible market maker'' for that period). The PCX proposes to prohibit the transmission of principal orders, except to unlock or uncross markets or to satisfy trade-through liability. Under the Phlx plan, eligible market makers would be permitted to send principal orders through the linkage without limitation, so long as the market maker meets the Phlx's proposed definition of ''eligible market maker.'' [25]

2. Order Protection

The exchanges all propose to prohibit trade-throughs (with certain exceptions discussed below), absent reasonable justification and during normal market conditions. The plans propose uniform exceptions to trade-through liability, including, among other things, systems malfunction, failure of the receiving market to respond to a P/A or principal order within 30 seconds, failure of the market traded through to complain within the specified time period, complex trades (to be defined by the Operating Committee), trading rotations, and non-firm quotations on the market that was traded through.

The plans propose identical language with respect to the responsibilities and rights of the participating exchanges following trade-through complaints and the proposed provisions relating to notice and mitigation of damages.

Chief Executive Officer, PCX; and Meyer S. Frucher, Chairman and Chief Executive Officer, Phlx; dated November 10, 1999. The options exchanges and the ISE set forth their positions on this issue in their response letters, dated December 10, 1999. *See* Letters to Chairman Levitt, from Salvatore F. Sodano, Chairman and Chief Executive Officer, Amex; William J. Brodsky, Chairman and Chief Executive Officer, CBOE; Philip D. DeFeo, Chairman and Chief Executive Officer, PCX; and Meyer S. Frucher, Chairman and Chief Executive Officer, Phlx; dated December 10, 1999.

[21] If the exchange receiving the order is at the NBBO but does not have time priority and is not willing to provide price improvement, it must send a P/A order to the away market that is at the NBBO with time priority.

[22] In fact, as discussed below, the PCX proposes to permit principal access to the linkage only to send orders to unlock or uncross markets or to satisfy trade-through liability.

[23] ISE did not define the term ''specified protection'' in its transmittal letter. The Commission seeks public comment on how, if at all, that term should be defined. *See* Section IV.

[24] Incoming P/A orders, but not outgoing P/A orders would be included in this calculation.

[25] As noted above, Phlx defines an ''eligible market maker'' as a ''market maker'' that is assigned to, and is providing two-sided quotations in, the eligible option class and is participating in its market's automatic execution system in such eligible option class.

With one exception, the exchanges agree on the appropriate satisfaction of trade-throughs, either by satisfying the complaining market, adjusting the price, or canceling the trade. If customer orders constituted either or both sides of the transaction involved in the trade-through, each customer order would receive the price of the trade that caused the trade-through, or the satisfaction price, if the trade-through was satisfied, or the adjusted price, if there was an adjustment, whichever price is most beneficial to the customer order. The member initiating the trade-through is responsible for any differences.

The plans uniformly propose rules regarding the price at which the bid or offer that was traded through must be satisfied, yet differ on the appropriate size of the satisfaction. The satisfaction price would equal the price of the bid or offer, unless the transaction that constituted the trade-through was a block trade,[26] in which case satisfaction would be the price of the transaction that caused the trade-through. With respect to the appropriate size of satisfaction, in the absence of disseminated size, the Amex/CBOE and PCX plans would limit the satisfaction of a trade-through to the verifiable number of customer contracts in the market of each exchange that was traded through that were included in the disseminated bid or offer of that exchange subject to certain limitations. In particular, if the number of contracts to be satisfied in one or more exchanges exceeds the size of the transaction that caused the trade-through, satisfaction will be limited to the size of the transaction that caused the trade-through. Moreover, if the transaction that caused the trade through was for a size larger than the firm customer quote size with respect to any of the exchanges traded through, the total number of contracts to be satisfied to all exchanges will not exceed the size of the transaction that caused the trade through and will be allocated *pro rata* based on the verifiable number of customer contracts traded through on each exchange. In the absence of disseminated size, the Phlx proposal would require that if the transaction was for a size larger than the firm customer quote size, the total number of contracts to be satisfied would not exceed the size of the transaction that caused the trade-through on each exchange that was traded through.

G. Trade Comparison; Error Resolution

The plans submitted to the Commission propose uniform procedures for trade comparison and error resolution, set forth in Section 9 of the plans.

H. Trading Halts and Suspensions, Non-Firm Quotations, and Hours of Operation

In Section 10 of the plans, the exchanges uniformly propose procedures for trading halts and suspensions and non-firm quotations. Specifically, each exchange reserves the right to halt or suspend trading or declare market conditions to be non-firm in its market. In addition, where a particular market is closed, has halted or suspended trading, has not yet opened for trading, or has disseminated notice to the other linkage plan participants that its quotations are not firm in a particular options class, linkage orders may be neither sent to that exchange nor accepted by it through the linkage. In a scenario in which the exchange sending the linkage order halts or suspends trading, or declares its quotations to be non-firm subsequent to the transmission of a linkage order, the linkage order must be accepted and handled by the receiving exchange pursuant to the provisions of the linkage plan, unless the receiving exchange also halts or suspends trading, or declares its quotations to be non-firm.

I. Financial Matters

The plans all propose, in Section 11, to divide the development and operating costs of the linkage equally among the participant exchanges, while each exchange proposes to be solely responsible for the costs of any modifications to its systems needed to accommodate the linkage. The exchanges propose that the Operating Committee will, at least once a year, establish a participation fee to be charged to any eligible exchange that seeks to become a party to the linkage plan. The participation fee, which is proposed to reflect a new participant's pro-rata share of the costs of developing, maintaining, and enhancing the linkage, will be distributed equally to the then-current participating exchanges.

J. Withdrawal From the Plan

Section 12 of the plans provides that any participating exchange may withdraw from the plan with at least 30 days prior written notice.

K. Implementation of the Plan

The participating exchanges stated that the plan would be implemented upon the Commission's approval of a plan and related rules and the participants' completion of the development of the systems necessary to effectuate the linkage approved by the Commission. The exchanges propose that the linkage will be operable at any time that two or more participating exchanges are open for trading between 9 a.m. and 5 p.m. Eastern time.

L. Development and Implementation Phases

The exchanges expect that there will be a development phase subsequent to Commission approval of a plan. During that time, the Operating Committee will determine the manner in which to build and operate the linkage and whether to select a facilities manager. If the Operating Committee determines to select a facilities manager, it will issue a request for proposals describing the required functionality of the linkage, including a specification that the linkage be developed to accommodate the routing of P/A orders on a price-time basis, should the Commission determine that price/time priority should be a component of the linkage. PCX has proposed a phased implementation schedule, as described above. None of the other plans provide for a phased implementation schedule.

M. Impact on Competition

The plans filed by the exchanges provide for the creation of an inter-market linkage between the options markets. In its October 19, 1999 Order, the Commission found that establishing a linkage among the options markets would benefit investors by increasing competition among markets (and market participants) to provide best execution of customer orders. Given the recent increases in the listing of options classes that are traded on more than one options exchange, the need for an inter-market linkage has become increasingly acute. Without a linkage, the possibility of inter-market trade-throughs, discussed above, becomes increasingly common, to the detriment of investors and other market participants. A linkage between the options exchanges should reduce the frequency of inter-market trade-throughs, and provide a mechanism for satisfying the markets that are traded through when a trade-through occurs.

N. Terms and Conditions of Access

As described above, Section 4 of each of the plans contains an identical, self-effecting provision for the admission of

[26] The plans uniformly define a ''block trade'' as a trade that: (i) Is of block size, defined as 500 or more contracts and a premium value of at least $150,000; (ii) is effected at a price outside of the NBBO; and (iii) involves either a cross (where a member of the exchange represents all or a portion of both sides of the trade) or any other transaction that is not the result of an execution at the current bid or offer on the exchange.

new participants, in which any national securities exchange may become a party to the plan by agreeing, in an amendment to the plan, to comply with the provisions of the plan, and paying the applicable fee.

O. Method of Determination of Imposition, and Amount of Fees and Charges

The plans do not provide for the imposition of any fees or charges associated with the use of the linkage. Section 11 of each of the plans uniformly proposes the allocation among the exchanges of costs associated with the development, implementation, and maintenance of the linkage. As described above, the exchanges propose that the Operating Committee will, at least once a year, establish a participation fee to be charged to any eligible exchange that seeks to become a party to the linkage plan. The participation fee, which is proposed to reflect a new participant's *pro-rata* share of the costs of developing, maintaining, and enhancing the linkage, will be distributed equally to the then-current participating exchanges.

P. Method and Frequency of Processor Evaluation

Under Section 6 of the plans, the Operating Committee may determine to select a facilities manager. The selection of a facilities manager would require the affirmative vote of at least two-thirds of the members of the entire Operating Committee. A decision to remove, or not to renew the contract of, a facilities manager would likewise require the affirmative vote of at least two-thirds of the members of the entire Operating Committee.

Q. Dispute Resolution

Section 5 of each of the plans provides for a mechanism for the resolution of disputes arising under the plan.[27] The proposals provide for a procedure by which a participating exchange may request an interpretive opinion of a rule made by another participant on the application of the plan. The dispute must pertain to a situation involving a minimum loss of $5,000, which must have been established pursuant to the plan, including the mitigation provisions of the plan. All routine internal exchange surveillance reviews relating to the disputed ruling must have been completed prior to the request. Periodic reports on the functioning of, and experience under, the dispute resolution process will be submitted to the Operating Committee for its information and review.

R. Written Understandings or Agreements Relating to Interpretation of, or Participation in, the Plan

Not applicable.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed plans are consistent with the Act. In particular, the Commission seeks comment on the following issues:

1. What are the benefits and detriments of requiring that orders be routed to competing exchanges based on strict price/time priority? Should the plan include price/time priority?

2. Would a linkage that allows a market maker to step up to match the NBBO, but permits an away market to receive an execution if it was displaying a customer limit order at the price of the execution on the exchange that stepped up, provide desirable protection to customer limit orders?

3. How would a linkage system as described in the above question work in practice? Should satisfaction of a ''trade at'' be automatic or on a complaint basis? If by complaint, how long should the market whose limit order was ''traded at'' have to complain?

4. In ISE's alternative proposal, the term ''specified protection'' is not defined. What would be an appropriate level of satisfaction for a ''trade-at''?

5. What other requirements might be imposed on a linkage that could protect customer limit orders on away markets?

6. Because quote size is not disseminated, the plan establishes a firm quote size for customer orders and principal orders and establishes different size criteria for satisfying trade-throughs. What is the appropriate size for these purposes?

7. Should the linkage plan require the options markets to disseminate quotes with size? If so, what time frame is reasonable to implement this proposal? How should the requirement that quote size be disseminated be balanced against concerns about constraints on options systems capacity?

8. Who should have access to the linkage?

9. In what way, if any, should access to the linkage be restricted for orders involving principal accounts?

10. What is an appropriate level of discretion for the proposed Operating Committee? In particular, should it have discretion to define plan terms such as ''complex trade'' as an exception to trade-through liability?

11. In what way, if any, will a linkage plan between the options markets impact competition?

12. Is it useful to require a unanimous vote in order to amend the plan? Would a super-majority (or a simple majority vote) to amend the plan be more or less appropriate than a requirement of unanimity? Under what circumstances, including those included in the plan, should a super-majority be required? Would a simple majority be more appropriate in any of those instances?

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, and 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 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 also will be available at the principal offices of the participating exchanges. All submissions should refer to File No. 4–429 and should be submitted by April 3, 2000.

Dated: April 3, 2000.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

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[27] The proposed dispute resolution process is essentially the same process adopted by the Intermarket Trading System Operating Committee and approved by the Commission. See Securities Exchange Act Release No. 29194 (May 15, 1991) 56 FR 23318 (May 21, 1991).