related Market Index to ensure convergence of the value of those two positions at the time of settlement. The ROS modified opening procedure should allow this convergence by allowing market participants to close out their open Market Index option positions and obtain the exact price (*i.e.,* the opening price) for those series that will be used to calculate the Volatility Index settlement value. The Commission notes that the modified ROS opening procedure was used on May 19, 2004 and that CBOE represented that generally no problems or issues arose regarding its use.[13]

The Commission notes that CBOE has also submitted supplemental surveillance procedures designed to ensure, among other things, that market-makers exercise their discretion to set certain AutoQuote values consistent with their obligation to price options fairly and that identify whether any accounts have engaged in manipulative or violative activity.[14]

IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and rules and regulations thereunder.

[13] Telephone conversation between David Doherty, Attorney, CBOE, and Christopher Solgan, Attorney, Division, Commission, on May 28, 2004. CBOE noted that there were two minor issues that arose regarding the May 19, 2004 opening. First, that while 138 market makers were able to log on to ROS for the modified opening, two market makers were unable to participate in the opening because they failed to log onto ROS in a timely manner. Second, CBOE is investigating whether a broker-dealer violated CBOE Rule 6.2A by failing to cancel a broker-dealer order that was not executed during the opening as explicitly required by the rule. CBOE has represented that these problems did not affect the performance of the modified ROS opening. Further, CBOE has represented that it will work with market makers to ensure their timely participation in ROS.

[14] CBOE has represented, and the Commission expects, that CBOE will work with the Commission's Office of Compliance Inspections and Examinations (''OCIE'') to finalize any surveillance reports used in connection with the modified ROS opening in a manner acceptable to OCIE. The Commission also expects CBOE to assess its surveillance procedures from time to time to determine whether they are adequate to ensure that market makers do not engage in manipulative or improper trading practices. Further, the Commission expects CBOE to consider whether any additional surveillance procedures are necessary to prevent manipulative or other improper practices. In addition, CBOE stated, and the Commission expects, that it will modify the ROS system software to prevent a market-maker who is logged on to ROS from trading against an order on behalf of the market-maker or the market-maker firm that may be resting in the electronic book. CBOE has also represented and the Commission expects that prior to implementation of this system change, CBOE will file a rule change with the Commission to reflect this system change. *See* Notice, *supra* note 5.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[15] that the proposed rule change (SR–CBOE–2004–23) and Amendment Nos. 1 and 2 thereto, are approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[16]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 04–13088 Filed 6–9–04; 8:45 am]

BILLING CODE 8010–01–P

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

[16] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–49793; File No. SR–CHX–2004–02]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Stock Exchange, Incorporated Relating to Automatic Execution of Orders

June 2, 2004.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the ''Act''),[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on February 11, 2004, the Chicago Stock Exchange, Incorporated (''CHX'' or ''Exchange'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I, II and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange proposes to amend Article XX, Rule 37 of the CHX Rules, which governs, among other things, automatic execution of market and marketable limit orders, to eliminate the existing 100-share minimum automatic execution threshold. The text of the proposed rule change is available from the Office of the Secretary of the CHX or at the Commission.

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 regarding 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 Exchange proposes to amend Article XX, Rule 37 and Rule 43 of the CHX Rules, which governs, among other things, automatic execution of market and marketable limit orders, to eliminate the existing 100-share minimum automatic execution threshold.

Background

The vast majority of orders received by a CHX specialist are routed from order-sending firms via the Exchange's MAX'' system, which provides for the electronic routing and automatic execution of orders. CHX rules require that the MAX system automatically execute orders at the national best bid or offer (''NBBO'') if certain conditions are met.[3] In order to manage his position and prudently limit his auto-execution exposure, each CHX specialist designates an ''auto-execution threshold'' for each issue.[4] The auto-execution threshold is the number of shares that the specialist is willing to execute automatically. Under the current rule, the minimum auto-execution threshold is 100 shares.[5]

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

[2] 17 CFR 240.19b–4.

[3] See CHX Article XX, Rule 37(b)(6)(automatic execution of orders in listed securities); CHX Article XX, Rule 37(b)(7)(automatic execution of orders in OTC securities).

[4] Article XX, Rule 37(b)(1).

[5] The CHX believes that it is important to note that under the current version of the CHX rules governing automatic execution, a CHX specialist is required to permit MAX system execution of an unlimited number of orders at the then-prevailing NBBO price, until the consolidated quotation stream reflects a change in the NBBO price. As a consequence, if a large number of orders are routed to the CHX specialist simultaneously, before the consolidated quotation is updated, the CHX specialist would be obligated to fill all of the orders at the NBBO price, despite the fact that the aggregate number of shares vastly exceeded the NBBO size. The CHX represents that this virtually unlimited liability is an unintended, and unwarranted, consequence of automatic execution guarantees like the Exchange's current rule.

For example, if the national best bid (''NBB'') was 50 x 1000 shares, the CHX specialist would be obligated to execute an unlimited number of customer sell orders at 50, as long as each order was 1000 shares or less in size, until the consolidated quotation information indicated a change in the NBB. Continuing this hypothetical example, assume

Continued

If an order exceeds the specialist's auto-execution threshold, the order is automatically directed into the specialist's book for manual execution.[6] Orders that are executed manually must be executed in accordance with CHX Article XX, Rule 37(a), commonly referred to as the ''BEST Rule,'' which currently requires that manually executed orders be executed by the CHX specialist as principal at the NBBO or, if the CHX specialist elects to act as agent for the order, at the best available price in the marketplace.[7]

A number of the Exchange's specialist firms have developed and are implementing a remote pricing functionality (''RFP'') that permits their specialists to better respond to orders that are dropped for manual handling. This RFP functionality provides the MAX system with automated execution instructions for orders that otherwise would require the manual intervention of a CHX specialist.[8] Of course, a specialist firm may also continue to act as agent for an order or manually execute orders using more manual processes.

Proposal

The Exchange's current rule requires a minimum auto-execution threshold of 100 shares, thus ensuring that all 100-share orders are executed automatically by the MAX system. The CHX believes, however, that in many cases a CHX specialist might prefer to act as agent for the order or manually execute the order, rather than having the order (or a large number of 100-share orders) executed against him automatically at the NBBO. Accordingly, the Exchange proposes to eliminate the requirement of a 100-share minimum auto-execution threshold, so that a CHX specialist may use his or her discretion in determining how best to handle these 100-share orders.

This change is principally intended to permit CHX specialists to utilize their RFP functionalities to price 100-share orders.[9] Although the elimination of the 100-share minimum automatic execution threshold would also permit specialists to switch to manual execution mode on the CHX floor without using an RFP functionality, the Exchange does not anticipate that this would occur very often, if at all; in today's fast-paced trading environment, a specialist would not be able to manually manage his order flow for any sustained period of time.

Significantly, the Exchange represents that orders will continue to be subject to surveillance by the CHX Department of Market Regulation and members will remain subject to CHX rules relating to order execution requirements.

The CHX would further note that in today's market environment, where specialists are required to make public their quality-of-execution statistics and broker-dealers are bound as fiduciaries to make order-routing decisions in accordance with best execution practices, there exist sufficient market-based incentives for specialists to continue to provide execution prices and liquidity akin to the best available in the national market.[10] The CHX believes that these incentives render a rule-based requirement largely obsolete, and amply support the rule change that the Exchange now proposes.

The Exchange also is seeking to delete CHX Article XX, Rule 37, Interpretation and Policy .04, which currently governs the procedures by which specialists are to obtain permission to switch from automatic execution mode to manual execution mode. Because deletion of the 100-share minimum automatic execution threshold would effectively permit CHX specialists to switch to manual execution mode, it is no longer necessary to include procedures for seeking floor official approval.

2. Statutory Basis

The proposed rule is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.[11] In particular, the proposed rule is consistent with Section 6(b)(5) of the Act in that it is designed to promote just and equitable principles of trade, to remove impediments to and to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.[12]

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

The Exchange 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 self-regulatory organization consents, the Commission will:

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

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

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's Internet comment form *(http://www.sec.gov/rules/sro.shtml);* or
- Send an e-mail to *rule-comments@sec.gov*. Please include File Number SR–CHX–2004–02 on the subject line.

that 200 sell orders, each for 100 shares, were routed to the CHX before a change in the NBB to 49 one second later. Notwithstanding the one-second pendency of the 50 NBB, the CHX specialist would be obligated to buy 20,000 shares at 50, when such liquidity at that price was not truly present anywhere in the national market system. In today's decimal environment, such extraordinary results, which could not have been anticipated when the Exchange's automatic execution provisions were enacted, occur often.

[6] An exception to this general rule occurs if the order-sending firm has elected to receive partial automatic executions, in which case a portion of the order will automatically execute, up to the size of the auto-execution threshold, and the balance of the order will be placed in the specialist's book for manual execution. *See* CHX Article XX, Rules 37(b)(6),(7).

[7] The CHX has filed a proposal to modify the BEST Rule's requirement that specialists, when acting as principal, manually-execute orders at the NBBO. *See* SR-CHX–2004–03.

[8] The REP systems are proprietary to the specialist firms and are not facilities of the Exchange.

[9] CHX specialists believe that use of their RFP technology for 100-share orders will, among other things, better enable them to address situations in which a co-specialist simultaneously receives a large number of 100-share orders.

[10] Specialists would of course remain free to increase their auto execution thresholds to larger sizes if they believe that business/marketing considerations so demand; in fact, a number of specialists have indicated that they would reduce their auto execution threshold below 100 shares only in very limited instances, or for the sole purpose of routing 100-share orders to their RFP functionalities.

[11] 15 U.S.C. 78f(b).

[12] 15 U.S.C. 78f(b)(5).

Paper Comments

• Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609.

All submissions should refer to File Number SR–CHX–2004–02. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (*http://www.sec.gov/rules/sro.shtml*). 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 Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal offices of the Amex. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–CHX–2004–02 and should be submitted on or before July 1, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[13]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 04–13086 Filed 6–9–04; 8:45 am]

BILLING CODE 8010–01–U

[13] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–49810; File No. SR–PCX–2003–35]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment Nos. 3 and 4 to the Proposed Rule Change by the Pacific Exchange, Inc. Relating to Corporate Governance of Listed Issuers

June 4, 2004.

I. Introduction

On July 14, 2003, the Pacific Exchange, Inc. (''PCX'' or ''Exchange''), through its wholly owned subsidiary, PCX Equities, Inc. (''PCXE''), filed with the Securities and Exchange Commission (''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 to amend its Corporate Governance and Disclosure Policies. On October 14, 2003, the Exchange filed Amendment No. 1 to the proposal.[3] On October 31, 2003, the proposed rule change, as modified by Amendment No. 1, was published for comment in the **Federal Register**.[4] On November 18, 2003, the Exchange filed Amendment No. 2 to the proposal.[5] On December 1, 2003, the Commission partially approved the proposal as modified by Amendment No. 1, granted accelerated approval to Amendment No. 2, and solicited comments from interested persons on Amendment No. 2.[6] Specifically, the Commission approved the portions of the proposed rule change that implemented the requirements of Rule 10A–3 under the Act relating to audit committees of listed issuers.[7] The Commission received no comments on the proposal and Amendment No. 2.

On May 4, 2004, the Exchange filed Amendment No. 3 to the proposed rule change.[8] In Amendment No. 3, PCX proposed additional enhancements to the proposal and revisions to a number of its provisions that were not approved in the Partial Approval Order.[9] The substantive changes to the proposal made by Amendment No. 3 are summarized in Section II below. On June 3, 2004, the Exchange filed Amendment No. 4 to the proposed rule change, making additional, minor clarifications.[10] On June 4, 2004, the Exchange filed Amendment No. 5 to the proposed rule change.[11] This Order approves the proposed rule change in its entirety, as amended; grants accelerated approval to Amendment Nos. 3 and 4; and solicits comments from interested persons on Amendment Nos. 3 and 4.

II. Description of the Proposal

In addition to the provisions of the proposed rule change implementing the requirements of Rule 10A–3 under the Act, which were approved in the Partial Approval Order, PCX proposes further amendments to its rules, set forth in PCXE Rule 5.3, relating to the governance of issuers that list securities on the Exchange. The proposed rule change further includes related changes to PCXE Rule 5.4, regarding suspension of securities from trading privileges, and PCXE Rule 5.5, regarding maintenance requirements and delisting procedures.[12] The new corporate governance standards would apply to all listed companies, including Tier I and Tier II companies,[13] with certain exceptions for registered management investment companies, preferred and debt listings, passive business organizations (such as royalty trusts),

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

[2] 17 CFR 240.19b–4.

[3] *See* letter from Steven B. Matlin, Senior Counsel, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated October 8, 2003 (''Amendment No. 1'').

[4] *See* Securities Exchange Act Release No. 48700 (October 24, 2003), 68 FR 62146 (October 31, 2003) (''Notice'').

[5] *See* letter from Steven B. Matlin, Senior Counsel, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated November 17, 2003 (''Amendment No. 2'').

[6] Securities Exchange Act Release No. 48861 (December 1, 2003), 68 FR 68440 (December 8, 2003) (''Partial Approval Order'').

[7] 17 CFR 240.10A–3.

[8] *See* letter from Steven B. Matlin, Senior Counsel, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated May 3, 2004 (''Amendment No. 3'').

[9] The proposed revisions include some modifications to the text as approved in the Partial Approval Order.

[10] *See* letter from Steven B. Matlin, Senior Counsel, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated June 2, 2004 (''Amendment No. 4''). The revisions made in Amendment No. 4 are discussed *infra*, at notes 17 and 29.

[11] *See* letter from Steven B. Matlin, Senior Counsel, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated June 4, 2004 (''Amendment No. 5''). Amendment No. 5 was a technical amendment and is not subject to notice and comment.

[12] The changes to PCXE Rule 5.5, which were approved in the Partial Approval Order, referenced PCXE Rule 5.3 in its entirety and Rule 5.3(k)(5) in particular. Approval of the remaining proposed changes to PCXE Rule 5.3 that are the subject of this Order will thus affect the application of Rule 5.5.

[13] *See* Amendment No. 3, which eliminated the distinction between Tier I and Tier II companies with respect to the enhanced corporate governance standards that are the subject of this Order.