6(b)(5)[3] that an exchange have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

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

The proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purpose of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange has not solicited,and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from members or other interested parties.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549–0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR–ISE–00–05, and should be submitted by June 26, 2000.

IV. Commissions's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission has reviewed carefully the ISE's proposed rule change and finds, for the reasons set forth below, the proposal is consistent with the requirements of Section 6 of the Act[4] and the rules and regulations thereunder applicable to a national securities exchange.[5] Specifically, the Commission finds the proposal is consistent with Section 6(b)(5) of the Act.[6]

Section 6(b)(5) of the Act[7] requires an exchange to promulgate rules designed to prevent fraudulent and manipulative acts and practice, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and national market system, and, in general, to protect investors and the public interest. The Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,[8] because the proposal is designed to enhance liquidity on the Exchange during its start-up phase.

The Commission finds that the proposal is narrowly-tailored, and provides reasonable standards and guidelines to be applied in granting exemptions pursuant to this authority. In particular, the Commission notes that the Exchange's decisions to grant exemptions would be made on a case-by-case basis, and any exemption granted would be limited to a term of no longer than one month. In addition, the guidelines require that a market maker's exemption from the Volume Limitations would end as soon as the Group to which the market maker is assigned is opened for trading, even if only one options class in that Group has been listed at that time. Similarly, the exemption granted to a market maker holding more than one ISE membership would be reduced when one or more of its assigned Groups are opened for trading.

The Commission also believes that the proposal may encourage market makers to begin trading on the Exchange as soon as they are authorized and able to do so, which in turn, may benefit investors by providing liquidity to the market. The Commission notes that the proposed standards require market makers receiving an exemption to perform market making functions in the classes in which they trade, which should also enhance the liquidity of the market. Because of these potential improvements to the market, the Exchange's authority to grant exemptions on a case-by-case basis tailored to the individual situation of each market maker applying for an exemption, and the limited duration of the grant of exemptive authority, the Commission finds that the proposal is both reasonable and consistent with the Act.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. Having found that the proposal is both reasonable and consistent with the Act, and that it should result in enhancements to the marketplace during the Exchange's start-up phase, the Commission believes it would be counterproductive to delay the implementation of the proposal. Specifically, the Commission notes that the ISE intends to commence trading on May 26, 2000, in a limited number of options classes. The proposal will permit ISE PMMs and CMMs that are ready to begin trading, but have been assigned to Groups that are not yet open for trading, to participate in ISE's market, thereby increasing liquidity in the market. The Commission finds, therefore, that granting accelerated approval of the proposed rule change is consistent with Section 6(b)(5) of the Act.[9]

It is Therefore Ordered, pursuant to Section 19(b)(2) of the Act,[10] that the proposed rule change (SR–ISE–00–05) is hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[11]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00–13958 Filed 6–2–00; 8:45 am]

BILLING CODE 8010–01–M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42825; File No. SR–ISE–00–04]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Amendment No. 1 by the International Securities Exchange LLC Relating to the Exposure of Orders on the Exchange

May 25, 2000.

I. Introduction

On February 25, 2000, the International Securities Exchange LLC (''ISE'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission''), pursuant to

[3] 15 U.S.C. 78f(b)(5).

[4] 15 U.S.C. 78f.

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

[6] 15 U.S.C. 78f(b)(5).

[7] *Id.*

[8] *Id.*

[9] 15 U.S.C. 78f(b)(5).

[10] 15 U.S.C. 78s(b)(2).

[11] 17 CFR 200.30–3(a)(12).

Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] a proposed rule change relating to the exposure of orders on the Exchange.

The proposed rule change was published for comment in the **Federal Register** on March 6, 2000.[3] The Commission received three comment letters regarding the proposal.[4] On March 30, 2000, the ISE amended the proposed rule change.[5] This order approves the proposed rule change, as amended.

II. Description of the Proposal

The ISE proposes to amend ISE Rule 717 to reduce from two minutes to 30 seconds the amount of time that Electronic Access Members (''EAMs'') are required to expose agency orders on the Exchange before executing them as principal or executing them against a solicited order. According to the ISE, its order exposure requirements are intended to assure that agency orders have an opportunity to interact on the Exchange before they are executed. The Exchange proposes to reduce the exposure time because it believes that the objective of the exposure rule can be satisfied by a 30 second exposure period.

III. Summary of Comments

The Commission received three comment letters on the proposal.[6] These commenters opposed ISE's proposal to reduce the order exposure time from two minutes to 30 seconds.[7] Commenters argued that the proposed reduction in response time would make it easier for ISE members to execute as principal orders for less than 50 contracts without meaningful opportunity for price improvement by competitors.[8] The commenters contend that this would undermine the intended purpose of having customers' orders reasonably exposed to other trading interest before being executed by the facilitating ISE member.[9] Two commenters agreed that two minutes is an appropriate time frame for this purpose, but that a 30 second exposure time would make it unlikely that interested market participants would have sufficient time to gauge their risk exposure in other markets and related positions, and reveal on the ISE their true ''best'' price.[10]

Commenters stated that this proposal encourages internalization because it allows an EAM to execute orders as principal if it utilizes the facilitation mechanism of ISE Rule 716(d) or has been bidding or offering on the ISE for 30 seconds. Commenters noted that an EAM could easily internalize orders by, upon receiving a customer order, holding that order until the EAM has posted a bid or offer at this intended crossing price for 30 seconds, then executing the order as principal, effectively subverting the intent of the exposure period.[11]

In response to commenters' objections to the proposed reduction in the exposure period from two minutes to 30 seconds, the ISE states that it believes 30 seconds is a sufficient time for participants in the ISE market to respond to an order, noting that the Commission has approved exposure times of as few as 15 seconds for certain equity exchanges.[12] With regard to the sufficiency of the proposed 30 second exposure time, the ISE contends that a 30 second order exposure time is especially appropriate in light of the fact that floor-based exchanges have no limitation on how long a crowd must interact with a proposed crossing of orders, nor do floor-based exchanges have safeguards preventing a firm from negotiating with the crowd to execute against any and all of its customer orders, regardless of size.[13] ISE states that, because it is an electronic marketplace, it must define some order exposure time period.[14]

In response to the commenters' claim that members can subvert the 30 second requirement, ISE argues that the only exception to the 30 second exposure rule is the situation in which an EAM had disseminated proprietary trading interest on the ISE for at least 30 seconds prior to the customer order. In this case, according to ISE, the firm has disseminated trading interest, available to all customer orders, at the stated price, thus putting itself at risk to the public. Accordingly, ISE believes that execution of the EAM's own customer orders would not deprive the public of the opportunity to trade at the same prices.[15] Moreover, ISE notes that a broker would not be permitted, under its rules, to simply delay entering an order into the system in order to circumvent the exposure rule.[16]

In response to the commenters' internalization claims, ISE notes that that there is little opportunity for an EAM to be assured of executing against its own customer orders. Once customer orders are entered into the system, those limit orders that do not improve upon the ISE best bid or offer are placed into the ISE's electronic limit order book last in time priority behind any existing customer orders at the same price. Thus, the ISE argues, a given EAM would have no way of knowing whether the resulting increase in the best bid or offer (assuming the order matched the ISE best bid or offer) was due to its' customer's order, as opposed to other customer orders or interest from non-customers.[17] In addition, the ISE maintains that its proposed amendment to ISE Rule 717(d) addresses the only real opportunity for internalization in its system: The narrow case where an EAM has a limit order that improves upon the ISE best bid or offer or a market order that it is willing to execute at an improved price. The ISE argues that the proposed 30 second delay required by its amendment will remove the informational advantage that makes internalization profitable and will provide other market participants an opportunity to compete for such orders.[18]

Discussion

After careful review, the Commission find that the proposed rule change is consistent with the requirements of the Act and the rules and regulations

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

[2] 17 CFR 240.19b–4.

[3] Securities Exchange Act Release No. 42475 (February 29, 2000), 65 FR 11818.

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

[5] *See* letter from Katherine Simmons, Vice President and Associate General Counsel, ISE, to Deborah Flynn, Senior Special Counsel, Division of Market Regulation, SEC, dated March 28, 2000 (''Amendment No. 1''). In Amendment No. 1, the ISE made minor technical changes to ISE Rule 717, replacing section headings ''(a)'' and ''(b)'' with ''(d)'' and ''(e),'' respectively. Because Amendment No. 1 did not change the substance of the proposal, there was no need to publish it in the **Federal Register**.

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

[7] The Commission notes that commenters also raised issues related to ISE's system that were outside of the scope of the current ISE proposal, several of which were addressed in the Commission's order approving ISE's registration as a national securities exchange. *See* Securities Exchange Act Release No. 42455 (February 24, 2000), 65 FR 11388 (March 2, 2000). Consequently, this order addresses only comments regarding those issues presented by the current proposal.

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

[9] *Id.*

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

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

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

[13] *See* ISE Response Letter.

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] *Id.*

[18] *Id.*

thereunder applicable to a national securities exchange.[19] In particular, the Commission finds the proposal is consistent with Section 6(b)(5) of the Act.[20]

Under Section 6(b)(5) of the Act,[21] a registered national securities exchange must have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission finds that ISE's proposed amendments to ISE Rule 717(d) and (e) reducing the exposure time (*i.e.*, the amount of time EAMs are required to expose agency orders on the Exchange before executing them as principal or against a solicited order) from two minutes to 30 seconds are consistent with Section 6(b)(5) of the Act.[22] The Commission recognizes that, on floor-based exchanges, there are no rules that govern the extent to which a given trading crowd has an opportunity to interact with a proposed crossing of orders. Because the ISE operates a unique electronic options market, it must define an order exposure time period. The Commission finds that a 30 second exposure period is a reasonable time frame for participants in ISE's market to assess market conditions and their own trading interest, and to allow a reasonable opportunity for price improvement from interested participants. The Commission finds that a 30 second exposure period strikes a reasonable balance between maintaining liquidity and efficiency in the ISE market and preventing impediments to a free and open market, while providing the appropriate safeguards for investors and the public.

In determining that a 30-second exposure period is reasonable, the Commission has considered carefully the commenters' concern that market makers might be able to subvert the 30 second exposure period by posting bids or offers for a very short period of time, and arranging to receive agency orders simultaneously when they are executable against the market maker as principal, or against other agency orders held by the market maker.[23] In such a scenario, EAMs allegedly would pre-screen order flow, and hold orders until they can be internalized, denying the order any exposure in the market and the opportunity for price improvement. The Commission is not persuaded by this argument. The ISE allows for only one exception to the 30 second exposure period, in the scenario where an EAM has previously disseminated proprietary trading interest on the ISE for at least 30 seconds prior to receipt of a customer order. Under this limited exception, a firm will have placed itself ''at risk'' to the public by having disseminated trading interest available to all customer orders at a stated price. ISE Rule 717(d) states that a member must have been bidding or offering on the Exchange for *at least* 30 seconds prior to receiving an agency order that is executable against such bid or offer. The Commission finds that an EAM's execution of its own customer order under this particular scenario would not deprive the public of the opportunity to trade at the same price.

The Commission also has considered carefully the commenters' concerns about the potential for internalization of order flow where there is a 30 second exposure period, and finds that the proposal provides sufficient safeguards against such activity. The ISE's system is designed to ensure that, once customer orders are entered into the system, any limit orders that do not improve upon the ISE best bid or offer automatically are placed into the ISE's electronic limit order book last in time priority behind any existing customer orders at the same price. Therefore, an EAM has no guarantee that it will be able to trade against its agency orders. Because ISE's system automatically provides reasonable safeguards to prevent EAMs from executing against their own customer orders, the Commission finds that a 30 second exposure period does not pose an unreasonable risk of increasing the internalization of order flow. For these reasons, the Commission finds that ISE's proposal is consistent with Section 6(b)(5) of the Act.[24]

V. Conclusion

It Is Therefore Ordered, pursuant to Section 19(b)(2) of the Act,[25] that the proposed rule change (SR–ISE–00–04), as amended, is approved.

Margaret H. McFarland.

Deputy Secretary.

For the Commission, by the Division of Market Regulation, pursuant to delegated authorty.[26]

[FR Doc. 00–13959 Filed 6–2–00; 8:45 am]

BILLING CODE 8010–01–M

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

[20] 15 U.S.C. 78f(b)(5).

[21] *Id.*

[22] *Id.*

[23] *See* SA&B Letter at 8.

[24] 15 U.S.C. 78f(b)(5).

[25] 15 U.S.C. 78s(b)(2).

[26] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–42847; File No. SR–NASD–00–30]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. to Include UTP Exchanges in the Nasdaq National Market Execution Service

May 26, 2000.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on May 25, 2000, the National Association of Securities Dealers, Inc. (''NASD'' or ''Association''), through its wholly owned subsidiary, the Nasdaq Stock Market, Inc. (''Nasdaq''), filed a proposed rule change with the Securities and Exchange Commission (''SEC'' or ''Commission''). The proposed rule change is described in Items I, II, and III below, which Items have been prepared by Nasdaq. The Commission is publishing this notice to solicit comments on the proposed rule changes from interested persons.

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

Nasdaq is proposing to provide for the inclusion of national securities exchanges trading Nasdaq-listed securities pursuant to grants of unlisted trading privileges (''UTP'') in the automatic-execution functionality of the Nasdaq National Market Execution System (''NNMS''). Below is the text of the proposed rule change. Proposed deletions are in brackets and proposed addition are in italics.

4720. SelectNet Serve

(a)–(b) No Change

(c) Prohibition Regarding the Entry of Certain Preferenced Orders to Nasdaq National Market Execution System Market Makers

(i) No member [may] *shall* direct a SelectNet preferenced order to a Nasdaq

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

[2] 17 CFR 240.19b–4.