securities in GSCC's auction takedown service would provide GSCC and its members that trade these securities with all the benefits described above.

In order to meet the February deadline, it is necessary for GSCC to apply its current auction takedown procedures without any material alteration to the Freddie Mac auctions. Only minor changes to GSCC's rules are necessary. Such changes include the following:

The Department of the Treasury utilizes the Federal Reserve Banks, its fiscal agents, to furnish details of its auction awards to GSCC. GSCC therefore designated both the Treasury Department and the Federal Reserve Banks as locked-in trade sources when it instituted the auction takedown service. GSCC will now add Freddie Mac as a locked-in trade source. The Commission has already given GSCC permission to designate locked-in trade sources on an as-needed basis. It should be noted that Freddie Mac will furnish details of its auction awards directly to GSCC without the involvement of its fiscal agent, the Federal Reserve Bank of New York.

Various definitions will be expanded to include Freddie Mac and its securities in the rules referencing the auction takedown service.

Freddie Mac has indicated that, unlike the Department of the Treasury, it desires that awards made to non-netting members also be handled by GSCC to the extent possible. GSCC thus will make changes to its existing rules, which already allow for secondary market trades executed by non-members to be submitted by members for the net, to specify that it will process auction purchases made by its netting members for their customers as well as for their proprietary accounts. The netting members will remain liable to GSCC as principals with respect to all auction purchase awarded to them whether the purchase is for their own accounts or for customers.

Unlike the Treasury Department, Freddie Mac does not require the clearing banks to effectively guarantee payment in advance for any newly issued securities. thus, there will be no need for the execution of autocharge agreements by the clearing banks.

Freddie Mac retains the right to cancel auctions. GSCC has made it clear in its rules what has always been implicit for an issuer of auction awards that GSCC will have no obligation with respect to any when-issued trades if securities are not ultimately issued by Freddie Mac. GSCC has also added the right to delete or modify trade data with respect to when-issued trades if any event occurs that gives rise to the obligation to substitute securities under guidelines published by The Bond Market Association.

The Department of the Treasury is not a member of GSCC and is therefore not required to make any clearing fund deposits or funds settlement payments to GSCC. Since Freddie Mac is a GSCC netting member and would otherwise be responsible for these deposits and payments, GSCC has exempted Freddie Mac from these requirements but only in connection with its auction deliveries.

The proposed rule change is consistent with the requirements of Section 17A of the Act and the rules and regulations thereunder because it will enhance GSCC's auction takedown service by making it more responsive to the needs of GSCC's members.

(B) Self-Regulatory Organization's Statement on Burden on Competition

GSCC does not believe that the proposed rule change will have an impact or impose a burden on competition.

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

Written comments relating to the proposed rule change have not yet been solicited or received. Members will be notified of the rule change filing and comments will be solicited by an Important Notice. GSCC will notify the Commission of any written comments received by GSCC.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3) of the Act and Rule 19b–4(f)(4) thereunder, because the proposed rule is effecting a change in an existing service that does not adversely affect the safeguarding of securities or funds in the custody or control of the clearing agency and does not significantly affect the respective rights or obligations of the clearing agency or person using the service. At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Securities Exchange Act of 1934.

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. 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 Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of GSCC. All submissions should refer to File No. SR–GSCC–2001–02 and should be submitted by May 29, 2001.

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

Margaret H. McFarland,

Deputy Secretary.

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increased 131 percent over the par value of these transactions in 1999.

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–44234; File No. SR–PCX–00–03]

Self-Regulatory Organizations Notice of Filing of Proposed Rule Change by the Pacific Exchange, Inc. Implementing a One-Year Pilot Program Relating to Its Automatic Executive System

April 30, 2001.

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 February 15, 2000, the Pacific Exchange, Inc. (''PCX'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'' or ''SEC'') the proposed rule change as described in Items I, II and III below, which Items have been

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

[2] 17 CFR 240.19b–4.

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 its rules to allow automatic executions of orders in its Limit Order Book (''Limit Order Book'' or ''Book'') when those orders become marketable. Below is the text of the proposed rule change. Proposed new language is *italicized.*

* * * * *

¶5231 Automatic Execution System

Rule 6.87(a)–(k)—No change.

(l) *Auto-Ex Book Function*

(A) *The Auto-Ex Book function of POETS will permit orders in the Limit Order Book to be executed via the Auto-Ex system when those orders become marketable, subject to the following procedures:*

(i) When one or more orders in the Limit Order Book become marketable, as indicated by a locked or crossed market being displayed on the trading floor, the LMM may direct the OBO to initiate the Auto-Ex Book function, which will cause marketable orders in the Limit Order Book to be automatically executed against the accounts of market makers who are participating on the Auto-Ex system at the time.

(B) The Auto-Ex Book function is subject to a one-year pilot program which is set to expire [insert date one year from date of SEC approval].

* * * * *

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 its 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

At the PCX, limit orders of public customers may be placed in the Exchange's Options Limit Order Book [3] either electronically (via POETS [4]) or manually, by an options floor broker. At this time, only limit orders of ''public customers'' are eligible to be placed in the Limit Order Book.[5] Orders not eligible to be placed in the Limit Order Book must be manually represented by a floor broker at the trading post.

Currently, orders in the Limit Order Book can be executed in two ways. First, they can be executed *electronically* against incoming market or limit orders that a member firm has entered through POETS. For example, if a customer order to buy 20 option contracts at $5 is being represented in the Book, an incoming market order to sell 20 contracts (or limit order to sell 20 contracts at $5) entered electronically will execute against that order in the Book.[6]

Second, orders in the Book can be executed *manually.* To execute an order in the Book manually, a floor member [7] must vocalize a bid or offer for the option contracts being represented in the Book. This requires that the floor member gain the attention of the Order Book Official (''OBO'' [8]) and make an appropriate vocalization, *e.g.,* ''sell 20 XYZ calls to the Book at $5.'' [9] To consummate the trade, the OBO must perform the following actions: (1) call up the appropriate page for that particular option on the class display; (2) highlight the appropriate series (*e.g.,* March 30 calls); (3) enter either the buy key or the sell key; (4) enter either the put key or the call key; (5) type in the number of contracts to be purchased or sold; (6) enter the floor member's acronym (*e.g.,* MO1) and; (7) press the ''enter'' key to execute at the limit price or, alternatively, to improve the limit price, enter the better price (*e.g.,* 4⅞) and press the ''enter'' key.

The current manual process for executing orders in the Book is used when an order in the Book becomes marketable and a trade occurs.[10] For example, assume that the PCX market is 5 bid, 5⅛ asked, with 20 contracts in the Book to buy at 5. Next, assume that the underlying stock ticks down ⅛ of a point, and the new market in the option becomes 4⅞ bid, 5 asked. As long as the order to buy at 5 remains in the Book, the market will be locked at 5 bid, 5 asked.[11] To unlock the market, the order in the Book, which is now marketable, must be traded—but to do so will require a member of the trading crowd to obtain the OBO's attention, vocalize an offer for some or all of the contracts available at 5, and wait for the OBO to type in the information on the trade.

The Exchange believes that the current manual process for executing orders in the Book is inefficient. During times of heavy trading, it can be difficult for the OBO to type in specific trade details when that OBO may be involved in trades in other option series or other option issues. The inefficiencies of the current process have also become exacerbated due to rapid swings in prices that have been occurring recently in the marketplace, particularly in options overlying so-called ''internet stocks.''

Accordingly, the Exchange is proposing to effect a system change that will cause orders in the Book to be executed more efficiently when they become marketable. Specifically,

[3] The rules applicable to the Limit Order Book are set forth in PCX Rules 6.51–6.58.

[4] Pacific Options Exchange Trading System. *See* Securities Exchange Act Release No. 28633 (January 18, 2990), 55 FR 2466 (January 24, 1990).

[5] *See* PCX Rule 6.87.

[6] If there were no orders in the Book to buy at $5, and a bid of $5 was being disseminated by the PCX, then an incoming market order to sell (or a limit order to sell at $5) would be automatically executed by the Auto-Ex feature of POETS, with PCX market makers as the contra side to the trade. *See* note 14, *infra.*

[7] Floor members include market makers and floor brokers. Only members and Exchange employees who have been approved to perform a floor function may consummate transactions on the trading floor. *See* PCX Rule 6.2, Commentary .01.

[8] *See generally* PCX Rules 6.51–6.58 (rules relating to Order Book Officials (''OBOs'')). The Exchange notes that currently, all OBOs are employed by the PCX. However, the Commission recently approved an Exchange proposal to permit LMMs to use their own employees to operate the Book, which would include performing the function of the OBO. *See* Securities Exchange Act Release No. 41595 (July 2, 1999), 64 FR 38064 (July 14, 1999) (order approving SR–PCX–98–02). Therefore, the term ''OBO'' as used in this proposal includes OBOs currently employed by the Exchange and any employees of LMMs who are performing the function of the OBO.

[9] Floor members must trade against orders in the Book ahead of orders then being manually represented in the trading crowd at the same price, because orders in the Book have priority over orders in the trading crowd. *See* PCX Rule 6.75(a)–(b).

[10] A limit order to buy is marketable when the order's limit price is equal to or greater than the current offering price and a limit order to sell is marketable when the order's limit price is equal to or less than the current bid price. At the PCX, when the market on the screen on the trading floor is locked or crossed, the prices in the affected series are displayed in the purple, which alerts the members on the floor that there are buyers and sellers who are ready and willing to trade.

[11] A similar result would occur if a market maker in the trading crowd offered to sell options at 5, or a floor broker in the crowd representing an order made an offer to sell at 5, while concurrently there was an existing bid in the Book at the same price, *i.e.,* in theory, there would be a locked market. In practice, however, the market maker or floor broker willing to sell at 5 would vocalize an acceptance of the bid in the Book to trade at 5. If the size of the market maker's or floor broker's offer was greater than the size of the order in the Book, the offer at 5 would continue in effect until it was satisfied or withdrawn.

marketable orders in the Book will be executed via the Auto-Ex system when the Lead Market Maker (''LMM'') directs the OBO to operate the Auto-Ex Book Function. For example, if there are 30 contracts in the Book to buy at $5 and the trading crowd's offer to sell changes to a price of $5,[12] rather than locking the market (5 bid, 5 asked), the system will, upon the instruction of the LMM, execute the orders in the Book via the Auto-Ex System.[13] The 30 contracts to buy in the Book at $5 will then be executed against the accounts of market makers who are logged on to Auto-Ex at that time.

The function will also permit orders in the Book at various prices to be executed almost simultaneously. For example, assume that there are multiple orders in the Book, including orders to buy 50 contracts at $5, 50 contracts to buy at 4¾ and 50 contracts to buy at 4½. If the underlying stock price moves significantly, resulting in the PCX offering price of the overlying option price moving from 5¼ down to 4;½, the LMM may direct the OBO to initiate the Auto-Ex Book feature so that all of the buy orders in the Book referred to above will be automatically executed at their limit prices. This result simply speeds up the process for what currently may occur manually, with individual members of the trading crowd selling options against the buy orders in the book at their limit prices. Alternatively, however, the LMM or members of the trading crowd may determine to provide price improvement to the customer orders in the book, and may direct that all of those buy orders in the example (including those with limit prices of $5, 4¾ and 4½) be filled at 4½. In this instance, of course, the Auto-Ex Book feature would not be used.

The Exchange is proposing to implement the use of the Auto-Ex Book function on a one-year pilot program basis. This will allow the Exchange to study the operation of the system and to report back to the Commission at least sixty days prior to seeking permanent approval of the system change.

The Exchange notes that the proposed Auto-Ex Book feature will operate in a manner that is similar to the Exchange's Automated Opening Rotation (''AOR'') system, which automates the execution of orders in the Book at the opening of trading.[14] Specifically, the AOR system permits the OBO to establish a single price opening for executing market and marketable limit orders in the POETS system. It executes any imbalance of orders that existed at the opening at a single price, against the accounts of market makers who are participating on the Auto-Ex System at the time. The Exchange believes that approval of the Auto-Ex Book proposal, like the Commission's approval of the AOR system, will facilitate execution of orders in POETS, eliminate problems and inefficiencies associated with manual trading, eliminate backlogs of unexecuted orders, promote fair participation in trading against orders in the Book by all participants, and in general, improve market efficiency on the PCX.

In conclusion, the Exchange believes that use of the proposed feature will help to assure that customers' orders in the Book are filled more promptly. It will also help to prevent delays in trading and prompt resolution of problems in the crowd, because OBO's will not have to take as much time to respond to requests to execute marketable orders in the Book.

2. Basis

The Exchange believes that this proposal is consistent with Section 6(b) of the Act,[15] in general, and furthers the objectives of Section 6(b)(5)[16] in particular, in that it is designed to facilitate transactions in securities, promote just and equitable principles of trade, and to protect investors and the public interest.

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

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

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

Written comments on the proposed rule change were neither solicited nor 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, 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 proposal 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 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 PCX. All submissions should refer to File No. SR–PCX–00–03 and should be submitted by [May 29, 2001.]

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[17]

Margaret H. McFarland,

Deputy Secretary.

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[12] As noted above, this offer may be generated automatically by Auto-Quote, as a result of a change in the market in the underlying stock, or it may be generated manually by a member of the crowd vocalizing an offer, which is entered into POETS by the Market Quote Terminal Operator and subsequently disseminated.

[13] The Auto-Ex feature of POETS permit eligible market or marketable limit orders sent from member firms to be executed automatically at the displayed bid or offering price. Participating market makers are designated as the contra side to each Auto-Ex order. Participating market makers are assigned by Auto-Ex on a rotating basis, with the first market maker selected at random from the list of signed-on market makers. Auto-Ex preserves book priority in all options. *See* PCX Rule 6.87; *see also* Securities Exchange Act Release No. 41823 (September 1, 1999), 64 FR 49265 (September 10, 1999) (order approving PXC proposal to increase the size of orders that may be automatically executed via Auto-Ex). The Auto-Ex system is also used to execute any imbalance of orders that there may be at the opening via the Automated Opening Rotation System. *See* Note 14, *infra.*

[14] *See* Securities Exchange Act Release No. 43187 (August 21, 2000), 65 FR 54264 (August 29, 2000) (order approving one year extension of pilot program).

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

[16] 15 U.S.C. 78f(b)(5).

[17] 17 CFR 200.30–3(a)(12).