

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act<sup>26</sup> in general, and furthers the objectives of section 6(b)(5)<sup>27</sup> in particular, in that it is designed 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; and is not designed to permit unfair discrimination between customers, issuers, brokers or dealers. Specifically, the proposed rule change will permit member firms to direct order flow to the specialist of their choice and promotes competition to provide the best market.

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

The Phlx 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*

The Phlx has neither solicited nor received written comments with respect to the proposed rule change.

## 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 Phlx 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 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. Copies of such filing will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-Phlx-2001-98 and should be submitted by December 4, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>28</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

**[Release No. 34-45014; File No. SR-Phlx-2001-98]**

### **Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 by the Philadelphia Stock Exchange, Inc. Relating to Remote Specialists**

November 2, 2001.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934<sup>1</sup> ("Act"), and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 22, 2001, the Philadelphia Stock Exchange, Inc., ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Phlx. The Phlx submitted to the Commission Amendment No. 1 on November 1, 2001. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

<sup>28</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> 17 CFR 240.19b-4.

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

Phlx proposes to establish a remote specialist program. Specifically, the Exchange proposes to adopt new Phlx Rule 461, PACE Remote Specialists. The text of the proposed rule is set forth in full below.

### *Rule 461 PACE Remote Specialist*

PACE terminals and related equipment will be provided to member organizations for trading by remote specialists. The terminals will be linked to the PACT Trading System and will provide the same functionality as is available to on-floor specialists. All orders to remove specialists, including ITS commitments and administrative messages, will be processed the same as orders and ITS Commitments to an on-floor specialist. Floor Broker orders will be routed to remote specialists under the same criteria by which they are routed to on-floor specialists. There will be no remote floor brokerage services. The following shall apply to remote specialists:

(a) All rules and policies of the Board of Governors of the Exchange shall apply except as specifically excluded or amended under this section.

(b) Any specialist unit approved pursuant to Rule 501 may apply to the Equity Allocation, Evaluation and Securities Committee (the "EAES Committee") to trade as a remote specialist, pursuant to this Rule and Rule 511(b).

(c) Unless the EAES Committee specifically authorizes otherwise, participating specialist units shall be prohibited from trading remotely any securities which are currently being traded on-floor by that specialist unit. Individual securities may not be traded by one specialist unit in more than one Phlx remote location under any circumstances.

(d) The number and identity of specialty securities that may be traded remotely by any specialist unit shall be determined by the EAES Committee on a case by case basis.

(e) All non-electronic layoff orders entered on another exchange shall be recorded and submitted to the Exchange pursuant to Exchange procedures.

(f) All rule, by-law and Certificate of Incorporation references pertaining to the trading floor of the Exchange shall be deemed to include any bids, offers, orders and trading done remotely, and all such bids, offers, orders and trades shall be deemed to be Phlx bids, offers, orders and executions on the Exchange.

(g) A written confidentiality policy regarding the location of equipment and

<sup>26</sup> 15 U.S.C. 78f(b).

<sup>27</sup> 15 U.S.C. 78f(b)(5).

access to information, terminals and equipment must be adopted by the firm and filed with and approved by the Exchange prior to the commencement of remote trading. Moreover, this policy must conform to all of the requirements set forth in the rules of the Exchange, including, but not limited to rules dealing with the specialist's book. In accordance therewith, reasonable principles must be applied to limit access by non-specialists to remote specialist facilities and information, and to limit remote specialists' access to and from other proprietary trading venues, including access from outcry or visible communication, intentional or otherwise. Access to the area designated as that of the remote specialist shall be restricted to the specialist, assistant specialist, backup specialist, clerks, designated management of the specialist, and Exchange authorized personnel, consistent with the rules of the Exchange.

(h) Provisions regarding dress code, smoking and the requirement in Rule 108 that birds and offers be made within six feet of the post shall not apply. Rule 204, Hours, and Floor Procedure Advice E-1 shall not apply, provided that the specialist shall be immediately available by dedicated telephone line at all times required by the Floor Procedure Committee.

(i) Exchange correspondence, memoranda, bulletins and other publications shall be sent to remote specialists via electronic mail, if available, and via U.S. mail or overnight delivery, as well as other web-based means, as they become available.

(j) All remote specialists will have dedicated telephone access to the physical trading floor. Any regulatory requirements including trading halts, trading practices, policies, procedures or rules requiring floor official involvement will be coordinated by Exchange personnel with the remote specialist through the dedicated telephone line.

(k) Servicing of PACE terminals and related equipment shall be by Exchange authorized personnel only. Remote specialists may not link any hardware or software to enhance any of the systems or functionality without first requesting in writing and receiving approval to do so from the Exchange.

(l) The Exchange's examination program will include the remote specialist operations. Every firm must submit specific supervisory procedures, in accordance with the Exchange's Examinations procedures, relating to the remote specialist operations and appropriate identification of all individuals who will have access to the

remote specialist operation, including all supervisory personnel.

(m) Any arbitration or disciplinary action arising out of trading activity pursuant to this section would be subject to Rules 950 and 960 respectively regardless of the remote location of the trade or dispute.

(n) "Remote Authorization" Requirement. Each remote PACE terminal assigned and registered by the Exchange will require a non-transferable Remote Authorization, and will be subject to the following:

(1) Each approved specialist unit may be authorized to trade such number of issues remotely as the EAES Committee may determine on a case by case basis.

(2) Each remote specialist must have at least one registered Exchange membership.

(A) A specialist unit may be authorized to obtain additional Remote Authorizations for qualified registered clerks to access PACE in support of the specialist unit.

(B) All specialists and registered clerk Remote Authorization holders must be approved by the EAES Committee after they have completed the following:

(i) File a Remote Authorization application with the Exchange.

(ii) Completion of the required floor training program. On-site floor training would be waived for current floor specialists and registered clerks who transfer to remote specialist operations. The on-site floor training period could also be waived by the EAES Committee in exceptional circumstances, if other arrangements are made with and approved by the Exchange. In such exceptional circumstances, a waiver will be permitted if the Committee is assured that the person requesting the waiver has made other arrangements that ensure the person meets all of the requirements listed below. However, the on-site floor training period will not be waived for easily remedied reasons such as geographical location or inconvenience, and will include, among other things,

- Questioned trade procedures
- Communication procedures with Floor Brokers, PACE Desk, Surveillance, Systems Support, and ITS coordination with the floor
- The remote/competing specialist program and Unlisted Trading Privilege ("UTP") applications and procedures
- Allocations and procedures
- Book or symbol change procedures
- Trading Halt procedures
- Floor official rulings
- Minor Rule Plan Violations policies and application
- Books and Records/reports available

—Explanation of the specialist performance evaluation categories and procedures

—Certain other rules and policies deemed appropriate by the Exchange (e.g., Limit Order Display Rule, auto-executions, Price Improvement, etc.)

—ITS Quick Reference Card

(iii) Successful completion of any applicable state requirements.

(iv) Submission of fingerprint records to the Phlx.

(3) Each remote specialist firm will be evaluated under the Exchange's specialist evaluation program.

## II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, Phlx included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in item IV below. Phlx 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 purpose of the proposed rule change is to establish rules to permit competing Phlx specialist units<sup>3</sup> to conduct specialist trading activities off the Phlx trading floor using the PACE terminal/trading system, including the Exchange's Order Entry Window feature of the Exchange's equity trading system.<sup>4</sup>

Specialists currently access the PACE system only from the Exchange's physical trading floor, and all market making occurs on that floor.<sup>5</sup> Under the remote program being proposed, specialists will have the ability to access the PACE system from approved remote locations using PACE terminals. Like floor specialists, remote specialists will

<sup>3</sup> Currently, only one specialist unit is selected as the specialist in any given security. Phlx is filing, contemporaneously with this filing, proposed Rule 460, Procedures for Competing Specialists, which establishes rules for trading by more than one specialist unit in any given security. See SR-Phlx-2001-97.

<sup>4</sup> PACE is the Exchange's automatic order routing, delivery, execution and reporting system for equity securities which is governed by Rule 229, Philadelphia Stock Exchange Automated Communication and Execution System. See also proposed Rule 229A in SR-Phlx-2001-97.

<sup>5</sup> Eligible order entry firms may route orders into the PACE System as well.

receive orders, commitments over the Intermarket Trading System ("ITS"), and administrative messages through the PACE system. The Exchange will provide Phlx competing specialist firms the option to operate remotely under existing Exchange systems and rules, while retaining the ability to permit specialists to trade on the physical trading floor. All bids, offers, orders and executions, occurring within PACE or otherwise, whether conducted on the floor or electronically from remote locations, will be considered to be bids, offers, orders and executions occurring on the Exchange. All rule, by-law and Certificate of Incorporation references to the trading floor of the Exchange shall be deemed to include bids, offers, orders and executions done remotely, which shall also be deemed to be on the Exchange.<sup>6</sup>

To authorize the remote specialist program, the Exchange proposes to adopt Phlx Rule 461. The introductory part of Phlx Rule 461 generally provides that the Exchange will provide terminals linked to the PACE system for specialist trading in remote locations with the same functions that are available to on floor specialists. The remainder of proposed Phlx Rule 461 describes how remote specialists will operate, discusses the information barrier and other requirements that remote specialists must follow, and sets forth the way the Exchange will select and surveil remote specialists as well as other minimum criteria that remote specialists must satisfy.

Under this proposal, the "Primary Specialist" may not operate remotely. Any specialist unit approved to trade as a specialist pursuant to existing Rules 506(a) and 511(b), whether such appointment occurred prior to or after the commencement of the competing specialist program, would be the Primary Specialist in that security.

<sup>6</sup> Consequently, Remote Specialists would be subject to the jurisdiction of the Floor Procedure Committee in the same manner they would if their operations were conducted on the physical trading floor. Remote Specialists would be eligible to serve on Board of Governors and in committee positions reserved for persons associated with member organizations primarily engaged in business on the Exchange's Equity Floor (*i.e.*, in the case of the Board as "On-Floor Equity Governors") even though the member organization is not actually on the physical trading floor. Similarly, persons associated with Remote Specialist units may not be eligible to serve as Off-Floor Governors, even though the member organization conducts no business on the Exchange's physical trading floor. A person associated with a Remote Specialist unit would be eligible to serve as On-Floor Vice Chairman of the Board of Governors. See Article IV, Section 4-1 of the Exchange's By-Laws. See also Article IV, Section 17 of the Exchange's By-Laws regarding the powers of the Board to interpret the By-Laws.

Other specialist units would be permitted to apply under new Phlx Rule 460 to trade as competing specialists in the security. The Exchange is proposing in this filing to permit only competing specialists to trade remotely. Specialist units will not be permitted to trade remotely as alternate specialists under Phlx Rules 201A and 202A.

*Application of Phlx Rules to Remote Specialists.* The Exchange will apply all of its membership, net capital, equity, examination, specialist performance evaluation, competing specialist, allocation, and trading rules and policies to remote specialists in the same way that the Exchange applies those rules and policies to on-floor specialists, to the extent that such rules are not inconsistent with Phlx Rule 461. For example, the Exchange will require remote specialists—like other specialists—to make two-sided markets in specialty securities, execute customer orders they have accepted, and act as odd-lot dealers.

*Remote Specialist Access to PACE system.* Remote specialist terminals will be linked to the PACE trading systems using dedicated lines. These terminals will provide the same functionality that is available to on-floor specialists. Like on-floor specialists, remote specialists will have access to the Intermarket Trading System. Remote specialists will be routed orders, ITS commitments, and administrative messages through the PACE terminal. Remote specialists may also receive orders by telephone. Remote specialists will be subject to the same limit order display requirements that apply to other Phlx specialists. Floor broker orders will also be routed to remote specialists under the same criteria by which they are routed to on-floor specialists.<sup>7</sup> Servicing of PACE terminals will be by Exchange authorized personnel only.

*Remote Specialist Communication with the Exchange.* Phlx Rule 461(e) provides that Exchange correspondence, memoranda, bulletins and other publications shall be sent to remote specialists via electronic mail, if available, and via U.S. mail or overnight delivery, as well as other web-based means, as they become available. The Exchange believes that there are only limited situations in which a specialist would consult with a floor official—trading halts, issues involving ITS, and executions at an inferior price. The Exchange will keep a record of any situation that requires a floor official ruling involving remote specialists. The

<sup>7</sup> Member will not be able to use the PACE remote specialist program to conduct remote floor brokerage services in non-specialty securities.

Exchange will monitor communications between remote specialists and Exchange personnel to ensure that such communications are done in a timely manner, particularly if the communication involves a regulatory issue. Exchange personnel will coordinate floor official involvement with remote specialists. The Exchange's disclaimer of liability also applies.<sup>8</sup>

*Surveillance and Examinations.* Before the Exchange begins remote specialist trading, it will develop and put into place specific information barrier policies and surveillance policies that are consistent with the Exchange's existing rules and acceptable to the Commission's Office of Compliance Inspection Examinations. The Exchange's examination program will include the examination of books and records of all non-DEA member firms with remote specialist operations. Every firm will be required to submit supervisory procedures relating to remote specialist operations and to identify all individuals who will have access to remote specialist operations, including all supervisory personnel. The Exchange will conduct surveillance of limit order display practices by remote specialists to ensure that those practices are consistent with all applicable requirements including the Commission's limit order display rule. Before the Phlx allows remote specialist trading to begin at an off-site facility, the Exchange must fully investigate that facility, and ensure that trading at the facility will be subject to information barrier and surveillance policies that address the particular circumstances of the facility.

*Selection of Remote Specialists.* Specialist units will apply to the EAES Committee for approval to operate as a remote specialist unit. The EAES Committee will determine the number and identity of securities any particular specialist unit may trade remotely, on a case-by-case basis.<sup>9</sup> As a condition of such approval, each clerk and individual specialist in the unit must receive a "Remote Authorization" as provided in Phlx Rule 461(n). The

<sup>8</sup> Section 12-11 of the Exchange's By-Laws provides that the Exchange shall not be liable for any damages sustained by a member or member organization growing out of the use or enjoyment by such member or member organization of the facilities afforded by the Exchange to members for the conduct of their business.

<sup>9</sup> The EAES Committee will approve remote specialist units pursuant to this Rule 461 and Rule 511(b). Rule 511(b) will continue to govern the allocation of securities to specialist units, whether the Primary Specialist or a competing specialist. Those criteria will also apply to any determination by the EAES Committee to permit a Competing Specialist to trade remotely under Rule 461.

Exchange will authorize and approve Remote Authorizations based on certain qualifications. Each remote PACE terminal will then be individually identified and associated with a particular Remote Authorization holder such that all activity on any particular PACE terminal will be specifically identified and associated, by the use of the Remote Authorization, with an authorized and qualified specialist or registered clerk. The Exchange is proposing to issue Remote Authorizations primarily as a surveillance tool to monitor its remote specialists' operations. Remote Authorization is not transferable and is independent of Exchange membership requirements. Although PACE remote clerks will be required to obtain a Remote Authorization, there is nothing in the Remote Authorization which will grant them any more rights or privileges than a current on-floor clerk possesses. Rule 104, for example, would continue to restrict members in their dealings with non-members, including clerks. Additionally, Rule 748 would require the remote location of a specialist unit to be under the supervision and control of a member and of an appropriately qualified supervisor. The Remote Authorization requirement is designed to permit the Exchange to better surveil the activities of specialists and clerks that utilize the PACE system remotely.<sup>10</sup> Remote Authorization holders will be subject to an on-floor training program as a condition of Remote Authorization, subject to waiver under certain circumstances, pursuant to the terms of Phlx Rule 461(n)(2)(B)(ii).

**Implementation.** For an initial period, the Exchange intends to limit its remote program to specialist member organizations that maintain concurrent equity floor operations. The EAES Committee will determine the identity and the total number of individual securities that will be included in the remote program. In the future, the Exchange may determine to accept applications from specialist units that do not have concurrent equity floor operations.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act<sup>11</sup> in general, and furthers the objectives of section 6(b)(5)<sup>12</sup> in particular, in that it is

designed 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; and is not designed to permit unfair discrimination between customers, issuers, brokers or dealers. Specifically, the Exchange believes that the proposed rule change will promote efficiency by potentially reducing the costs associated with transactions on the Exchange, and will promote liquidity and competition on the Exchange by enabling specialists to make markets either on or off of the Phlx's physical trading floor. In particular, by allowing Phlx specialists to conduct their activities off of the Exchange's physical trading floor, while retaining the availability of on-floor market making, the Exchange believes that the proposal will permit Phlx specialists to choose the most efficient and cost-effective way to conduct business. At the same time, remote specialists will have full access to the information and functions available on the PACE terminal/trading system, and the PACE trading system will maintain and display limit orders represented by remote specialists consistent with the practice applicable to other Phlx specialists. Accordingly, the Exchange believes that the proposal uses technology in a manner that should promote competition in the securities markets, consistent with the congressional mandate set forth in section 11A of the Act.<sup>13</sup>

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

The Phlx 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*

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**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 Phlx 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 person 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. Copies of such filing will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-Phlx-2001-98 and should be submitted by December 4, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

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

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**BILLING CODE 8010-01-M**

## **SMALL BUSINESS ADMINISTRATION**

### **[Declaration of Disaster #3364]**

### **State of New York; (Amendment #2)**

In accordance with a notice received from the Federal Emergency Management Agency, dated November 1, 2001, the above numbered declaration is hereby amended to extend the deadline for filing applications for physical damages as a result of this disaster to January 10, 2002.

All other information remains the same, i.e., the deadline for filing

<sup>10</sup> See letter from Carla Behnfeldt, Director, Legal Department New Product Development Group, Phlx to John Riedel, Attorney Adviser, Division of Market Regulation, Commission, dated November 1, 2001 ("Amendment No. 1").

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

<sup>13</sup> 15 U.S.C. 78k(a).

<sup>14</sup> 17CFR 200.30-3(a)(12).