

MEMO# 12542

August 29, 2000

SEC PROPOSES TRADE-THROUGH DISCLOSURE RULE AND AMENDMENTS TO FIRM QUOTE RULE FOR OPTIONS MARKETS

[12542] August 29, 2000 TO: EQUITY MARKETS ADVISORY COMMITTEE No. 47-00 RE: SEC PROPOSES TRADE-THROUGH DISCLOSURE RULE AND AMENDMENTS TO FIRM QUOTE RULE FOR OPTIONS MARKETS The Securities and Exchange Commission has proposed a new rule under the Securities Exchange Act, Rule 11Ac1-7, and amendments to an existing rule, Securities Exchange Act Rule 11Ac1-1, to provide investors with increased information regarding the quality of executions in the options markets and to require market makers to be firm for their quotes.¹ Trade-Through Disclosure Rule Proposed Rule 11Ac1-7 would require a broker-dealer to disclose to a customer when the customer's order to buy or sell a listed option was executed at a price inferior to the best quote published at the time of execution of the customer's order (the "Trade-Through Disclosure Rule"). The disclosure would be required to be made on the customer's confirmation delivered pursuant to Securities Exchange Act Rule 10b-10. The disclosure would not be required, however, if the transaction was effected on an options exchange that participates in an intermarket linkage plan that has explicit provisions reasonably designed to limit trade-throughs.² The proposed rule does not explicitly prohibit trade-throughs, as the Release states that the SEC recognizes that there may be times when a customer would rather receive an immediate execution rather than pursue an opportunity for price improvement. The rule is intended, however, to provide incentives for markets to develop means to access one another to avoid trade-throughs. Amendments to the Quote Rule The Release states that the Trade-Through Disclosure Rule would not be meaningful if the market publishing a better quote is not firm for a specified number of contracts at that ¹ Securities Exchange Act Release No. 43085 (July 28, 2000), 65 FR 47918 (August 4, 2000) ("Release"), a copy of which is attached. ² See Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000) and Memorandum to Equity Markets Advisory Committee No 46-00, dated August 29, 2000. ³ The SEC therefore, in conjunction with the proposed rule, is proposing amendments to Securities Exchange Act Rule 11Ac1-1, the "Quote Rule," that would require options exchanges and options market makers to publish firm quotes.³ Currently, by its terms, the Quote Rule does not apply to options. Comments on these proposals are due to the SEC no later than September 18, 2000. If you have any questions regarding the proposals, please contact the undersigned by phone at (202) 371-5408, by fax at (202) 326-5839, or by email at aburstein@ici.org. Ari Burstein Assistant Counsel Attachment Attachment (in .pdf format) ³ The Release explains that the Quote Rule

currently requires that the best bid, best offer, and size for each market quoting any security covered by the Quote Rule be collected and publicly disseminated. These quotations must be firm and a market maker, specialist, or other responsible broker or dealer generally is obligated to execute an order at a price at least as favorable as its published bid or offer up to the size of its published bid or offer. This is the broker- dealer's "firm quote obligation."

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