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May 15, 1978

Mr. Andrew M. Klein
Director
Division of Market Regulation
Securities and Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Dear Mr. Klein:

In accordance with recent conversations with you and Ms. McGrath, this letter contains our suggestions for improving Rule 19b-4, Form 19b-4A and related procedures. Although we are counsel to the Chicago Board Options Exchange and The Options Clearing Corporation, and most of our recent experience with the subject has been on behalf of those organizations, the views expressed herein are not necessarily those of our clients.

The basic difficulties that we have perceived are that (1) the filing and publication requirements of Rule 19b-4 and the specific items of Form 19b-4A have imposed undue burdens on SROs and the Commission, (2) communications between SROs and the Commission have often been impaired rather than facilitated by overly formalistic procedures, and (3) for these and other reasons there have been inordinate delays in the processing of many rule proposals. Below we make a number of specific suggestions to improve communications and otherwise overcome the foregoing difficulties. But first we will comment in more general terms as to the source of the difficulties.

Somehow the concept of "cooperative regulation" has been weakened in the course of implementing the 1975 Amendments. We recognize that the new law enlarged the Commission's role and formalized the process of review in connection with SROs' rule change proposals, but this was done "not to diminish the role of self-regulation but to strengthen the total regulatory fabric." (S. Rep. No. 75, 94th Cong., 1st Sess. (1975) at 23). Congress understood that "one of the advantages of self-regulation is the flexibility and informality of its decision-making procedures" and expressly indicated its concern for preserving such flexibility. (Id. at 29). The 1975 Amendments did not change the basic concept that SROs have statutory authority and responsibility for regulation of their markets and their members, subject to Commission oversight.

In keeping with the statutory scheme we believe the Commission, and particularly the staff, should, to the greatest extent possible, work with each SRO as a partner in a joint regulatory enterprise. Procedurally, the process of reviewing SRO proposals should be as flexible and down-to-earth as possible, instead of being as formalistic as it has become. Substantively, in furtherance of Congress's intention to encourage SROs "to continue their healthy experimentation and innovation with regard to decision-making processes" (Ibid.), SROs should have reasonable leeway in formulating their own trading systems and regulatory programs, even if not taking precisely the same path or going precisely as far as the Commission might have done if it were the SRO.*

As to the specifics of the review procedure, we have the following suggestions:

1. We believe there should be greater distinctions in procedures under Section 19(b), throughout the reviewing process, as between very broad or novel proposals (such as the creation of a new market, a new product, a new facility, or a new category of members) and more limited or routine ones; or as between those that raise significant economic or competitive issues and those that are essentially administrative or operational in nature. Distinctions of this kind, which would usually be evident on the face of the filing, could be the basis for distinctions as to the length of the public comment period, the time within which the staff should ordinarily inform the SRO of any questions or concerns (see paragraph 4 below), and similar matters.

2. In any case, Form 19b-4A should be substantially revised to provide more meaningful information with less burden on all concerned. For example, instead of containing a large number of specific items that tend to invite "boiler plate" responses, the from should follow

* The following statement of the Special Study of Securities Markets (Part 4 at 723) would seem just as valid after the 1975 Amendments as before: "Although governmental oversight of self-regulation is essential, the workability of self-regulation depends also on restraint in the Commission's exercise of its reserve power…. [T]he roles of the Commission and the self-regulatory agencies are essentially complementary, and self-regulatory agencies must enjoy such autonomy as will enable them to act as responsible, dynamic partners in a cooperative enterprise." This view would seem especially relevant to legislative (rule-making) aspects of cooperative regulation.

the statute in requiring merely a "concise general statement of the basis and purpose" of a proposed rule change.* In the case of more complicated or controversial proposals, the form, or perhaps Rule 19b-4 itself, should encourage SROs to file supplemental information (for the use of the staff and available for public inspection on request but not included in the published notice of filing) and should emphasize that better prepared and more informative filings are likely to be processed faster than poorly prepared ones. Such supplemental information could, where appropriate, be responsive to the following kinds of questions:

> If and to the extent the proposal is regulatory in nature, state concisely how it is expected to enhance (or in any event why it will not impair) investor protection, and explain whether and how "equal regulation" may be favorably or adversely affected.
>
> If and to the extent the proposal is operational in nature (affecting how particular market functions are carried out), explain concisely how the proposal is expected to affect the efficiency or economy of handling those functions.
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> To the extent the proposal may be expected to affect competition among markets or among market participants, explain exactly how any type of competition may be enhanced or impaired.
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> If it is known or expected that there will be significant opposition to the proposal on the part of members or others, indicate what is known of the grounds of such opposition.

3. The first available notice of a proposed rule change generally appears in the SEC News Digest, but this is often so abbreviated as to fail to give adequate notice of the nature and purpose of the proposal. The Federal Register notice is of course more complete but (a) it does not appear promptly, (b) it does not readily come to the attention of the relatively small number of persons who might want to comment, and (c) it puts a heavy burden on the Commission to prepare each filing and pay for what may be a great deal of printing, in order to reach a wide audience of mostly non-interested persons. One or more of the following ideas might be helpful in making the notice process both more effective and less burdensome:

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* The Form itself (as distinguished from provisions for supplemental information as discussed in the next sentence) might contain just three items:

Item 1	Text of change
Item 2	Concise general statement of basis and purpose
Item 3	Status of change, including (a) whether final action taken by SRO; (b) further action required by SRO (describe); (c) whether comments solicited or received (summarize); (d) whether requested to be effective upon filing under Section 19(b) (3) (state grounds).

(i) Moderately expand the notice in the SEC News Digest; this can be done without delaying the review process by requiring the SRO to include in its Form 19b-4A filing a draft notice to be used for this purpose, containing a very brief summary of the proposed rule change and a very brief statement of its basis and purpose.

(ii) Require SROs to provide a copy of any rule change filing on request of any interested party (similar to the requirement that registrants provide copies of 10-K reports), possibly at some modest charge per page, and make a uniform statement as to such availability of copies (as well as the right to inspect or copy official files) in each News Digest containing one or more notices of rule change filings.

(iii) Do away entirely with Federal Register notices, as being neither legally nor practically necessary.

(iv) If, contrary to (iii), the Commission concludes that Federal Register notice is necessary, modify present practices as follows: (A) Where a proposed rule change runs more than approximately ____ words (or pages), require the SRO to include a fair summary of not more than _____ words (or page) as part of item 1 of the 19b-4A filing (see note * on page 3 above) for publication in the Federal Register in lieu of the full text. (B) Include in the News Digest the Federal Register citation, as soon as known, for each previously announced rule change filing. (C) Count all time periods from the time of publication of notice in the News Digest rather than in the Federal Register.

4. Within a fixed number of days after a filing has been made (perhaps 15 days for filings expected to be processed within the standard 35 day statutory time period, and 30 days for filings where the review period has been extended), the staff should be expected to inform the SRO as to any questions or concerns that it has and to request further information that it needs in order to process the proposal expeditiously. Where necessary, the staff's concerns should be discussed informally with the SRO as soon as possible. This sort of informal dialogue should in most instances enable the SRO to give a satisfactory explanation or modify its proposal to meet the staff's concerns. If the Division of Market Regulation determines that a proposal should be referred to another division, the comments of the other division should also be conveyed to the SRO and discussed with it on a similar informal basis.

5. If the staff believes, after informal exploration with the SRO, that it must make an adverse recommendation to the Commission, it should so inform the SRO and make available a copy (or draft) of its memorandum to the Commission, so that the SRO can respond to specific points made therein, or perhaps withdraw the proposal and avoid further burdens on everyone's time and resources. In situations where there is a real difference in views between the SRO and the staff, we believe that the SRO's argumentation should ordinarily be seen directly by the Commission rather than merely being summarized in a staff memorandum. But in any case, where a staff summary of the SRO's arguments is all that the Commission sees, we believe a copy of the summary should be given to the SRO.

6. In appropriate cases, there ought to be means for the Commission itself to address questions orally to the SRO or for the SRO to make oral comments that might be useful to the Commission. One suggestion would be to reserve two or three seats at the Commission table, or at least in the front row of the meeting room, for officers and/or counsel of the SRO when a rule proposal is taken up at a public meeting of the Commission. The SRO representatives would then be able to hear the discussion at the table better than often is true today, and would be able to answer occasional questions that the Commissioners might want to put to them. Further, within the Commission's control and discretion, SRO representatives might occasionally be allowed a few minutes to express themselves on specific points in light of the discussion at the Commission table and prior to a vote.

7. Various of the foregoing suggestions might have to be modified in respect of rule proposals involving controversial issues between the SRO and some category of its members or between the SRO and one or more competing markets. However, with due regard to the Administrative Procedure Act, the Home Box Office case and other procedural safeguards, we believe that it should still be possible to improve communications between the staff and the SRO (and/or other interested parties) in the general directions suggested above even if specifics must be changed at some places.

Obviously, the foregoing list does not exhaust the possibilities of changes that might simplify and expedite the review procedure. However, we believe strongly that some changes of the kinds outlined above are essential if the procedure is to function better than it has in the past.

If you have any questions or if we can be of help in working out any of the above, please call me, Burt Rissman or Mike Meyer.

Sincerely yours,

Milton H. Cohen

cc: Chairman Harold M. Williams
Commissioner John R. Evans
Commissioner Philip A. Loomis, Jr.
Commissioner Irving M. Pollack
Commissioner Roberta S. Karmel
Ms. Kathryn B. McGrath
Mr. Sheldon Rappaport
Mr. Harvey L. Pitt
Mr. Ralph C. Ferrara