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Stuart

U.S. House of Representatives
Subcommittee on Oversight and Investigations
of the
Committee on Energy and Commerce
Washington, DC 20515

August 11, 1986

Honorable John S. R. Shad
Chairman
Securities and Exchange Commission
450 Fifth Street, N. W.
Washington, D. C. 20549

Dear Chairman Shad:

Pursuant to Rules X and XI of the Rules of the U.S. House of Representatives, the Subcommittee on Oversight and Investigations is conducting an inquiry into the Commission's action on Friday, August 8, 1986, approving staff issuance of a no-action letter to Security Pacific National Bank and certain affiliates for the operation of an automated facility for the trading of put and call options on U.S. Government securities, without registration of the system as a securities exchange pursuant to Sections 3(a)(1), 5 and 6 of the Securities Exchange Act of 1934.

The Subcommittee understands that the Commission believes that such registration would be inappropriate because it would stifle innovation. The Subcommittee also understands that the Division of Market Regulation has granted no-action positions to operators of seven automated systems, conditioned on their providing the Commission with updated operational data and information regarding material changes in their systems. Compliance with reporting requirements has been erratic but the Commission has allowed the systems to operate in violation of these requirements rather than revoking the no-action letters.

The Subcommittee further understands that the Commission is of the view that, while the staff prepares for Commission consideration a release proposing for comment a rule to regulate automated trading systems, that the existing no-action letters should remain in effect and the staff was admonished that there should be no delay in granting other no-action letters on similar facts. The Subcommittee understands that in order to create a so-called level playing field, the Commission encouraged regulated exchanges to file no-action requests for similar unregulated electronic trading systems, notwithstanding the procedural requirements of Section 19(b) of the Securities Exchange Act, and indicated that the requests should be granted by the staff if the exchanges set up separate subsidiaries so that the systems arguably were not "facilities" of the exchange.

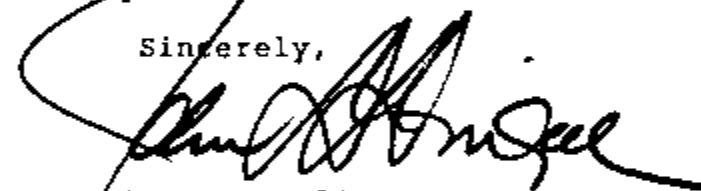
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Critics complain that the Commission's approval of nonexchange exchanges threatens to undermine the Congressional intent behind the Securities Acts Amendments of 1975, in reforming and strengthening the unique system of self-regulation in the securities industries and the method and manner by which the self-regulatory organizations operate. Under that system, the principal markets for securities, i.e., registered exchanges, are also the principal regulators of the activities in and users of those markets, and are in turn subject to SEC oversight of the performance of their regulatory responsibilities.

In order to assist the Subcommittee in evaluating the need for hearings or legislative action, we request that you provide the Subcommittee with two copies of the staff action memorandum and any other documents submitted to the Commission in connection with the Security Pacific National Bank matter and the transcript of last Friday's open Committee meeting as to the discussion of and vote on item 1 on the open meeting agenda. Please provide the Subcommittee with copies of the documents by the close of business on Monday, August 18, 1986, and advise us how soon you will have the transcript prepared.

Thank you for your cooperation and attention to our request.

Sincerely,



JOHN D. DINGELL
CHAIRMAN
Subcommittee on Oversight
and Investigations

cc: Honorable Timothy E. Wirth ✓
Honorable Norman F. Lent ✓
Honorable Fernand J. St Germain