

obviously erroneous as compared to the price being displayed by the primary options exchange for the option.

Where a participant enters a quotation or order in error that executes against standing interest on the Exchange, the contra side to the transaction had no notice of an erroneous price and took no action to execute at the erroneous price. In this instance, the adjustment price will be the bid (offer) price from the exchange providing the most volume in the case of an erroneous offer (bid) price entered on the Exchange. The ISE believes that this will result in a more favorable adjustment price for the participant with standing interest in the book than the participant that made the error. As a result, in the previous example, if the erroneous bid of \$7 executed against an offer in the system at \$6.50, the adjustment price would be \$5.20 (the offer price) instead of 5 (the bid price). Again, the only time an adjustment will be made to the price of a transaction is in the case where both parties were ISE market makers or where both parties agree to the adjustment.

Finally, proposed ISE Rule 720 specifies that each market maker firm will designate at least one person that is knowledgeable about options market making on the ISE to be called upon by the Exchange to participate on an obvious error panel.<sup>8</sup> Proposed ISE Rule 720 provides that an obvious error panel will have the authority to: (1) Determine a theoretical price when there is no quote for an option on another options exchanges; and (2) upon request by a party to a potential obvious error, review whether the correct theoretical price was used and whether an adjustment was made at the correct price. A party to a potential obvious error may also request that the obvious error panel provide relief under the proposed rule in cases where the party failed to give notice within the required time periods, but there must be unusual circumstances to merit this special consideration. All determinations by an obvious error panel will be made on the same day as the transaction in question and shall be final.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>9</sup> in general, and furthers the objectives of Section

6(b)(5)<sup>10</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, 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

The Exchange did not solicit or receive written comments on the proposed rule change.

## III. Date of Effectiveness of the Proposed Rule Change and Timing of 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 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 at

the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-ISE-00-19 and should be submitted by February 8, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>1</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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**BILLING CODE 8010-01-M**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43831; File No. JR-NASA-00-72]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Nasdaq's Transaction Credit Pilot Program

January 10, 2001.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on December 13, 2000, the National Association of Securities Dealers, Inc. ("NASD" or "Association"), through its wholly owned subsidiary The Nasdaq Stock Market, Inc. ("NASD"), filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. Nasdaq has designated this proposal as one establishing or changing a due, fee, or other charge imposed by the Association under Section 19(b)(3)(A)(ii) of the Act,<sup>3</sup> which renders the proposal effective upon filing with the Commission. 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

Nasdaq proposes to amend NASD Rule 7010, System Services, to extend Nasdaq's transaction credit pilot program for an additional three months for Tape A and B reports. The text of the proposed rule change is below. Proposed new language is in italics. Proposed deletions are in brackets.

<sup>1</sup> 17 CFR 200.30-3(a)(12).

<sup>2</sup> 15 U.S.C. 78s(b)(1).

<sup>3</sup> 17 CFR 240.19b-4.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>8</sup> In no case shall an obvious error panel include a person related to a party to the obvious error in question. To the extent reasonably possible, the Exchange shall call upon representatives of each market maker to participate on an obvious error panel on an equally frequent basis.

<sup>9</sup> 15 U.S.C. 78f(b).

<sup>10</sup> 15 U.S.C. 78f(b)(5).

## 7010. System Services

(a)-(b) No Change.

(c) \* \* \*

(1) No Change.

(2) Exchange-Listed Securities

Transaction Credit. For a pilot period, qualified NASD members that trade securities listed on the NYSE and Amex in over-the-counter transactions reported by the NASD to the Consolidated Tape Association may receive from the NASD transaction credits based on the number of trades so reported. To qualify for the credit with respect to Tape A reports, an NASD member must account for 500 or more average daily Tape A reports of over-the-counter transactions as reported to the Consolidated Tape during the concurrent calendar quarter. To qualify for the credit with respect to Tape B reports, an NASD member must account for 500 or more average daily Tape B reports of over-the-counter transactions as reported to the Consolidated Tape during the concurrent calendar quarter. If an NASD member is so qualified to earn credits based either on its Tape A activity, or its Tape B activity, or both, that member may earn credits from one or both pools maintained by the NASD, each pool representing 40% of the revenue paid by the Consolidated Tape Association to the NASD for each of Tape A and Tape B transactions. A qualified NASD member may earn credits from the pools according to the member's pro rata share of the NASD's over-the-counter trade reports in each of Tape A and Tape B for each calendar quarter starting with July 1, 2000 for Tape A reports (April 1, 2000 for Tape B reports) and ending with the calendar quarter starting on [October 1, 2000] *January 1, 2001.*

\* \* \* \* \*

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

In its filing with the Commission, Nasdaq 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. Nasdaq 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

Nasdaq proposes to extend through March 31, 2001, its pilot program to provide a transaction credit<sup>4</sup> to NASD members that exceed certain levels of trading activity in exchange-listed securities. Nasdaq's InterMarket is a quotation, communication, and execution system that allows NASD members to trade stocks listed on the New York Stock Exchange ("NYSE") and the American Stock Exchange ("Amex"). The InterMarket competes with regional exchanges like the Chicago Stock Exchange ("CHX") and the Cincinnati Stock Exchange ("CSE") for retail order flow in stocks listed on the NYSE and the Amex. The NASD collects trade reports from broker-dealers trading these securities in the over-the-counter ("OTC") market and provides the trade reports to the Consolidated Tape Association ("CTA") for inclusion in the Consolidated Tape. As a participant in the CTA Plan, the NASD is entitled to a portion of the revenue that the CTA generates by selling this market data information. NASD's share of the revenues is based on trades that it reports on behalf of these broker-dealers in NYSE-listed securities ("Tape A") and in Amex-listed securities ("Tape B").

The Transaction Credit Pilot Program began in 1999.<sup>5</sup> Under the Program, NASD shares a portion of these tape revenues by providing a transaction credit to NASD members who exceed certain levels of OTC trading activity in NYSE and Amex securities. The Program helps InterMarket market makers and investors lower costs associated with trading listed securities. The Program also is an important tool for Nasdaq to compete against other exchanges (particularly CSE and CHX) that offer similar programs<sup>6</sup> and thereby

<sup>4</sup> The transaction credit can be applied to any and all charges imposed by the NASD or its non-self-regulatory organization affiliates. Any remaining balance may be paid directly to the member.

<sup>5</sup> See Securities Exchange Act Release No. 41174 (March 16, 1999), 64 FR 14034 (March 23, 1999) (SR-NASD-99-13). The Program was subsequently extended. See Securities Exchange Act Release Nos. 42095 (November 3, 1999), 64 FR 61680 (November 12, 1999) (SR-NASD-99-59); 42672 (April 12, 2000), 65 FR 21225 (April 20, 2000) (SR-NASD-00-10); and 42907 (June 7, 2000), 65 FR 37445 (June 14, 2000) (SR-NASD-00-32).

<sup>6</sup> See Securities Exchange Act Release No. 38237 (February 4, 1997), 62 FR 6592 (February 12, 1997) (SR-CHX-97-01) and 39395 (December 3, 1997), 62 FR 65113 (December 10, 1997) (SR-CSE-97-12).

maintain market share in listed securities.

The Program works as follows: Nasdaq calculates two separate pools of revenue from which credits can be earned: one representing 40% of the gross revenues received by the NASD from the CTA for providing trade reports in NYSE-listed securities executed in the InterMarket for dissemination by CTA (Tape A), and the other representing 40% of the gross revenue received from the CTA for reporting Amex trades (Tape B).

Eligibility for transaction credits is based on concurrent quarterly trading activity. For example, an InterMarket participant that enters the market for Tape A or Tape B securities during a particular quarter and prints an average of 500 daily trades of Tape A securities during the time it is in the market, or that averages 500 Tape B prints during such quarter, would be eligible to receive transaction credits based on its trades during the third quarter. Only those NASD members who continue to average an appropriate daily execution level are eligible for transaction credits and thus able to receive a pro-rata portion of the appropriate pool.<sup>7</sup> These thresholds permit the NASD to recover appropriate administrative costs related to NASD members that do not exceed the threshold and to provide an incentive for NASD members to actively trade in these securities.

The current Program will expire on December 31, 2000. Because the Program has helped Nasdaq maintain market share in listed securities, Nasdaq proposes to extend the current Program through the first quarter of 2001. Nasdaq's transaction credit program is being proposed on a pilot basis only. There can be no guarantee that transaction credits will be available to qualifying NASD members beyond the term of the pilot.

#### 2. Statutory Basis

Nasdaq believes the proposed rule change is consistent with section 15A(b)(6) of the Act<sup>8</sup> in the proposal is designed to promote just and equitable principles of trade and to remove impediments to and perfect the mechanism of a national market system and, in general, to protect investors and the public interest. Nasdaq also believes

<sup>7</sup> As explained in Nasdaq's original pilot filing, the qualification thresholds were selected based on Nasdaq's belief that such numbers represent clear examples of a member's commitment to operating in the InterMarket and competing for order flow. See Securities Exchange Act Release No. 41174 (March 16, 1999), 64 FR 14034 (March 23, 1999) (SR-NASD-99-13).

<sup>8</sup> 15 U.S.C. 78o-3(b)(6).

the proposal is consistent with Section 15A(b)(5) of the Act<sup>9</sup> in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility of system which the Association operates or controls.

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

Nasdaq does not believe that the proposed rule change will result in 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 were neither solicited nor received.

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

The proposed rule change has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act<sup>10</sup> and subparagraph (f)(2) of Rule 19b-4 thereunder,<sup>11</sup> because it establishes or changes a due, fee, or other charge imposed by the Association. At any time within 60 days of the filing of the 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 Act.

### **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, 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 Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to file number SR-NASD-00-72 and should be submitted by February 8, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

**[Release No. 34-43822; File No. SR-PHLX-01-01]**

### **Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to the Dissemination of Options Quotations With Size**

January 8, 2001.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 8, 2001, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. 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 Phlx, pursuant to Rule 19b-4 of the Act, proposes to amend, on a temporary basis, Exchange Options Floor Procedure Advice ("OFPA") F-7, Bids and Offers, to state that the size of any bid or offer in a quotation disseminated by the Exchange shall be equal to the AUTO-X guarantee for the quoted option and shall be firm, except that the disseminated size of bids and offers of customer limit orders shall be ten (10) contracts and shall be firm, regardless of the actual size of such orders.

The complete text of the proposed rule change is available at the Office of the Secretary, Phlx and at the Commission.

#### **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 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. The 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 codify the Exchange's initial program for the dissemination of options quotations with size. It is anticipated that, on or about January 22, 2001, the Option Price Reporting Authority ("OPRA") will begin to support the dissemination of options quotations that include the size, or the number of contracts, represented in disseminated bids and offers on the Exchange.

On November 17, 2000, the Commission amended the Quote Rule<sup>3</sup> to require options exchanges and options market makers to publish firm quotes. The amended Quote Rule will require options exchanges to either: (1) Comply with the Quote Rule as it applies in the equity markets and collect from their members and make available to vendors the size associated with each quotation; or (2) establish by rule and periodically publish the quotation size for which their members' quotations are firm. The compliance date for the amendments to the Quote Rule is April 1, 2000.

While it is anticipated that OPRA will have the necessary systems capacity to accept and disseminate quotations with size by late January 2001, and that one or more options exchanges will be in a position to disseminate actual quotation size at that time, the Phlx will not have completed its application of the systems changes necessary to permit it to disseminate actual quotation size for a number of months.

Therefore, until the Exchange's systems disseminate actual quotation size on a quote-by-quote basis, the Phlx seeks herein to establish by rule and

<sup>9</sup> 15 U.S.C. 78o-3(b)(5).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>11</sup> 17 CFR 240.19b-4(f)(2).

<sup>12</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.

<sup>3</sup> Exchange Act Rule 11Ac1-1; 17 CFR 240.11Ac1-1; see Securities Exchange Act Release No. 43591 (November 17, 2000), 65 FR 75439 (December 1, 2000) (File No. S7-17-00).