

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.

#### *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.

#### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

The Exchange has neither solicited nor received comments on the proposed rule change.

### III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 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 and Amendment No. 1 thereto, 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 SR-BSE-2001-03 and should be submitted by July 24, 2001.

### IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission finds that the Exchange's proposal to retroactively extend the SPEP Pilot from April 1, 2001 until March 31, 2002 is consistent with the requirements of the Act and the rules and regulation thereunder. Specifically, the Commission finds that the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act,<sup>6</sup> which requires that the rules of the Exchange be designed to promote just

and equitable principles of trade, 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. The Commission believes that the retroactive extension of the SPEP Pilot should allow the Exchange to continue to assess specialist performance without interruption, while allowing the Exchange adequate time to consider amending the SPEP Pilot program in response to decimal pricing.

The Commission expects that during the SPEP Pilot the Exchange will continue to monitor threshold levels and propose adjustments as necessary and continue to assess whether each SPEP measure is assigned an appropriate weight.<sup>7</sup> In addition, the Exchange should continue to closely monitor the conditions for review and should take steps to ensure that all specialists whose performance is deficient and/or diverges widely from the best units will be subject to meaningful review. Finally, the Commission repeats its request that the Exchange incorporate additional objective criteria into the SPEP, most importantly, a measure of quote performance.<sup>8</sup> As previously noted, the Commission would have difficulty granting permanent approval to a SPEP that did not include a satisfactory response to the concerns described above.<sup>9</sup>

The Commission finds good cause for granting the Exchange's request for a twelve-month extension of the SPEP Pilot prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**.<sup>10</sup> Among the obligations imposed upon specialists by the Exchange, and by the Act and the rules promulgated thereunder, is the maintenance of fair and orderly markets in their securities. To ensure that specialists fulfill these obligations, it is important that the Exchange be able to evaluate specialist performance. The Exchange's SPEP Pilot assists the Exchange in conducting its evaluation and accelerated approval of

<sup>7</sup> See Securities Exchange Act Release No. 39730 (March 6, 1998), 63 FR 12847 (March 16, 1998) (order approving amendment to SPEP Pilot). In Securities Exchange Act Release No. 39730, the Commission stated certain terms and conditions for approving the SPEP Pilot program on a permanent basis, including the need to provide a study to the Commission regarding the SPEP Pilot program. Those terms and conditions are hereby incorporated by reference.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> In approving this proposal, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

the proposed rule change permits the SPEP Pilot to continue on an uninterrupted basis. Therefore, the Commission believes good cause exists to approve the extension of the SPEP Pilot from April 1, 2001 until March 31, 2002, on an accelerated basis. Accordingly, the Commission finds that granting accelerated approval of the requested extension is appropriate and consistent with Sections 6(b)(5) and 19(b)(2) of the Act.<sup>11</sup>

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>12</sup> that the proposed rule change, as amended, (SR-BSE-2001-03) is hereby approved on an accelerated basis through March 31, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 01-16637 Filed 7-2-01; 8:45 am]

BILLING CODE 8010-01-M

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-44476; File No. SR-BSE-2001-01]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the Boston Stock Exchange, Inc. Relating to the Trading of Nasdaq Securities on the Floor of the Exchange

June 26, 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 May 15, 2001, the Boston Stock Exchange, Inc. ("BSE" 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 Exchange. On June 15, 2001, the Exchange submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

<sup>1</sup> 15 U.S.C. 78f(b)(5) and 78s(b)(2).

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

<sup>3</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> See Form 19b-4 dated June 14, 2001 ("Amendment No. 1").

<sup>6</sup> 15 U.S.C. 78f(b)(5).

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

The Exchange seeks to add Chapter XXXV, Trading in Nasdaq Securities, to the Rules of the Board of Governors of the Boston Stock Exchange ("BSE Rules"). The proposed chapter sets forth rules governing the trading of Nasdaq securities on the Exchange. The text of the proposed rule change follows in italics.

### Chapter XXXV

#### Trading in Nasdaq Securities

*All of the Rules, Policies, and Procedures, set forth in the Rules of the Board of Governors of the Boston Stock Exchange ("Boston Stock Exchange Rules"), and elsewhere, shall apply to the trading Nasdaq securities in the same way as they do to the trading of non-Nasdaq securities, with the addition of the rules set forth in this Chapter XXXV, detailed below.*

#### Definitions

*Sec. 1. (a) "Nasdaq security"—any security listed on the Nasdaq National Market or Nasdaq Small Cap Market.*

*(b) "Nasdaq System"—the NASD's Automated Quotation System.*

*(c) "listed security"—a stock or bond, other than a Nasdaq security, that has been accepted for trading by the Boston Stock Exchange, or any of the other registered securities exchanges in the United States.*

#### Order Transmission

*Sec. 2. (a)(i) Each Exchange specialist shall provide direct telephone access to the specialist post to Nasdaq System market makers, acting in their capacity as market makers, for each Nasdaq security in which the market maker is registered as a market maker. Access shall include appropriate procedures which assure the timely response to telephonic communications. Nasdaq System market makers may use such telephone access to transmit orders for execution on the Exchange.*

*Any order received on the floor via telephone from a Nasdaq System market maker shall be effected in accordance with the rules applicable to the making of bids, offers and transactions on the Floor (see Chapter II, Dealings on the Exchange, Chapter XV, Specialists). All limit orders shall be immediately displayed upon receipt, in accordance with Chapter II, Dealings on the Exchange, Section 40, Limit Order Display Rule.*

*(ii) Exchange specialists may send orders from the Floor for execution via telephone to any Nasdaq System market*

*maker in each Nasdaq security in which it is registered as specialist. All of the Boston Stock Exchange Rules related to the trading of securities shall be applicable to bids and offers transmitted via telephone, in the same way as they apply to orders transmitted via automated trading systems.*

*(iii) Comparisons of transactions effected with a Nasdaq System market maker via telephone access will be made pursuant to procedures to be established between Nasdaq and the Exchange.*

*(b) Orders may be transmitted to a specialist via Nasdaq Workstation II ("NWII") at the election of a Nasdaq market maker originating the order. Orders transmitted through NWII may be executed by the system automatically or on a manual basis in accordance with the provisions of this Chapter XXXV.*

*(c) Specialists will have "Level 3 Service," as defined by the Nasdaq Unlisted Trading Privileges Plan, on the Nasdaq System. As such, specialists will have input and query ability with respect to quotations and sizes in securities included in the Nasdaq System. Access to the specialist via the Nasdaq System will be limited to floor brokers, BSE members, NASD members, NAS non-BSE members (including Electronic Communications Networks), and certain other member firms and other professionals represented by member firms ("clients"). Clients may have access to enter orders to the specialist either electronically, through the Nasdaq System, or telephonically. Any order received by the specialist telephonically, or verbally in any manner other than electronically through the Nasdaq System must be memorialized in accordance with Chapter II, Dealings on the Exchange, Section 2, Recording of Sales, and Section 15, Record of Orders from Offices to Floor.*

*(d) Access to the specialist via the Nasdaq System, or electronic access, includes*

*(i) orders sent by clients through Nasdaq's ACES Pass Thru capability (which consolidates orders sent by various client systems to the Nasdaq System);<sup>4</sup>*

*(ii) orders sent by BSE floor brokers directly through the BSE Nasdaq trading system (currently Nasdaq Tools);<sup>5</sup>*

*(iii) orders sent by clients directly into the Nasdaq System and routed to the specialist; and,*

<sup>4</sup> The Commission notes that Amendment No. 1 contained an incorrect reference, which BSE intends to correct in a future amendment to the proposed rule change.

<sup>5</sup> *Id.*

*(iv) orders sent by Nasdaq and NASD Market Makers through the Nasdaq System.*

#### Reporting of Transactions

*Sec. 3. All transactions in Nasdaq securities shall be reported through the Automated Confirmation Transaction Reporting Service ("ACT"), in accordance with NASD Rule 4630, et. seq., unless other arrangements are made with, and approved by, the Exchange. Any transaction for which electronic submission into ACT is not possible must be reported to the NASD's Market Regulation Department on Form T as specified in paragraph (a)(5) of NASD Rule 4632.<sup>6</sup>*

#### Trading

*Sec. 4. (a) Automatic Execution of Nasdaq orders. If the specialist is quoting at the National Best Bid or Offer ("NBBO") at the time a market or marketable limit order is received, the order shall automatically be filled at the NBBO up to the size of the specialist's bid or offer. The specialist's bid or offer will be decremented by the size of the execution. In the event that the specialist's bid or offer is exhausted, the system will generate a quote at an increment away from the NBBO as determined by the specialist from time to time, for 100 shares. If the specialist is not quoting at the NBBO at the time a market or marketable limit order is received, such order shall be automatically filled at the NBBO up to the size of the auto-execution threshold if the specialist has not, within 20 seconds after receipt of the order, complied with the manual execution requirement detailed below. The automatic-execution guarantee only applies to orders which are equal to or less than the size of the auto-execution parameter.*

*(b) In Nasdaq securities, the auto-execution parameter must be set at 300 shares or greater. For the purposes of this rule, odd-lot orders will be considered to be round lot orders for the purposes of rounding up to the size of the auto-execution guarantee parameter. An odd-lot order shall not increase the size of the execution guarantee to an amount greater than the auto-execution parameter. Rather an odd lot order would be added to any round lots less than the size of the auto-execution parameter and the execution guarantee would apply only to that number of shares, which would be less than or equal to, but in no case greater than, the size of the auto-execution guarantee.*

<sup>6</sup> *Id.*

(c) In unusual trading situations, specialists may switch from automatic execution to manual execution mode. "Manual execution mode" shall include any instance in which a specialist reduces the auto execution threshold below the minimum set forth in paragraph (b) of this section 4. For the purposes of this rule, "unusual trading situations" for Nasdaq securities include the existence of large order imbalances or significant price volatility. If a specialist elects to switch to manual execution mode based on the existence of unusual trading situations, the specialist must (1) document the basis for election of a manual execution mode; and (2) in the event that the specialist remains in manual execution mode for more than ten minutes, seek relief from the requirements of this section 4 from two floor officials.

All automatic execution parameters and practices shall be in accordance with NASD Rule IM-2110-02, Trading Ahead of Customer Limit Orders, and NASD Rule IM-2110-3, Front Running Policy.

Sec. 5. Manual Execution of Nasdaq securities. With respect to agency market or marketable limit orders in Nasdaq securities which have a size equal to or less than the auto execution threshold but which are not auto-executed under the provisions of this Chapter, a specialist shall be obligated to either (i) manually execute such orders at the NBBO in existence when the order is received or better, or (ii) act as agent for such orders in seeking to obtain the best available price for such orders on a marketplace other than the Exchange.

#### **Preopenings/Trading Halts**

Sec. 6. Pre-opening orders in Nasdaq securities must be accepted and filled at the Exchange opening trade price. In trading halt situations, orders will be executed based on the Exchange reopening price. (Note: In the case of a trading halt in a Nasdaq security, notice will be provided via the Nasdaq "NEWS" frame, in accordance with NASD Rule 4120.)

#### **Orders To Buy and Sell the Same Security**

Sec. 7. Pursuant to Chapter II, Section 18, Orders to Buy and Sell the Same Security, for cross transactions in Nasdaq securities,<sup>7</sup> a specialist must refrain from interfering at the cross price with an agency cross which is to be effected at a price between the disseminated Exchange market, unless

the specialist is willing to better one side of the cross.

When a member has an order to buy and an order to sell an equivalent amount of the same security, and both orders are for 5,000 shares or more and are for accounts other than the accounts of the executing member, the member may cross such orders at a price which is at or within the prevailing bid or offer. The member's bid or offer shall be entitled to priority at such cross price, provided that the proposed cross transaction is of a size greater than the aggregate size of all of the interest communicated on the Exchange floor at that price. Another member may trade with either the bid or offer side of the presented cross transaction only to provide a price which is better than the cross price as to all or part of such bid or offer. A member who is providing a better price to one side of the cross transaction must trade with all other market interest having priority at that price before trading with any part of the cross transaction.

#### **Dealings on Floor—Hours**

Sec. 8. Pursuant to Chapter I-B, Sec. 2, Dealings on the Floor—Hours, no member or member organization shall make any bid, offer or transaction upon the floor of the Exchange, issue a commitment to trade through ITS or send an order for a Nasdaq security to a Nasdaq System market maker other than during the hours the Exchange is open for the transaction of business. Nasdaq securities will not be eligible to participate in the Post Primary Session.

#### **Order Acceptance Guarantee**

Sec. 9. An Order Acceptance Guarantee shall be available to each member firm in all Nasdaq securities traded on the Exchange. Specialists must accept all agency market and marketable limit orders in Nasdaq securities up to and including 1000 shares in accordance with this rule. Specialists must accept all agency non-marketable limit orders in Nasdaq securities up to and including 10,000 shares for placement in the limit order book.

An Exchange specialist in a Nasdaq security shall only be obligated to guarantee execution on the first agency market order placed with him by a Floor broker or other Floor member, at any given best bid or offer. Subsequent to any such execution, the specialist may, but shall not be obligated to, guarantee the execution of such price of other orders placed with him.

#### **Specialist's Responsibilities**

Sec. 10. (a) Orderly Markets. In accordance with the responsibilities of specialists, as set forth in Chapter XV, Specialists, Sec. 2., Responsibilities, in relation to Nasdaq securities, an "orderly market" is defined as one with regularity and reliability of operation manifested by the presence of price continuity and depth exhibited by the avoidance of large and unreasonable price variations between consecutive sales on the Nasdaq system and the avoidance of overall price movements without appropriate accompanying volume.

A specialist in a Nasdaq security is responsible for insuring that each opening and reopening price in respect to Nasdaq securities reflects a professional assessment of market conditions at the time with due consideration being given to the balance of supply and demand as reflected by public orders. Additionally, the specialist should insure that the opening is not unduly hasty, particularly when at a price disparity from the previous close, and that the price reflects a thorough and professional assessment of market conditions at the time.

(b) Best Execution. Specialists dealing in Nasdaq securities shall use diligence to ascertain the best market for a particular security and provide the customer with a price which is as favorable as possible under the prevailing market conditions. Furthermore, no specialist shall interject a third party between himself and the best available market unless he can demonstrate that the total costs of the resultant transactions was better than the prevailing inter-dealer market for the security.

#### **Registration of Specialists**

Sec. 11. Specialists who wish to trade Nasdaq securities must be registered and qualified by the Exchange. As such, they must first make application to and be approved by the Exchange. In addition, and in accordance with the requirements set forth in Chapter XV, Specialists; Chapter XX, Employees for the Solicitation of Business; Chapter XXV, Registration of Member-Corporations; and elsewhere, specialists who trade Nasdaq securities will be required to:

- (1) Be associated with an existing or newly created specialist unit approved by the Exchange, in accordance with all applicable rules, policies and procedures; and,
- (2) Successfully complete the Boston Stock Exchange Floor Exam, including

<sup>7</sup> Id.

the sections regarding Nasdaq trading; and,

(3) Obtain a Series 63, NASAA Uniform State Law Exam, license; and,

(4) If conducting business with the public, obtain a Series 7, General Securities Representative, license under the sponsorship of a NASD registered Broker-Dealer; and,

(5) Complete a training period as deemed adequate by the Market Performance Committee; and,

(6) Ensure that the specialist unit with which he is associated meets all of the Exchange's financial requirements, as set forth in Chapter VII, Minimum Amount of Margin on Transactions Made During the Course of a Single Day in Accounts of Members, Allied-Members and Member-Organizations, Chapter IX, Unissued Securities—Margin Requirements, Chapter XXII, Financial Reports and Requirements—Aggregate Indebtedness—Net Capital, Chapter XXII—A, Blanket and Fidelity Bonds, and elsewhere.

#### **Limitations on Specialists**

Sec. 12. Any individual member who is registered as a specialist is not permitted to maintain a book, as defined in Chapter XV, Specialists, Section 6, The Specialist's Book, in both Nasdaq securities and listed securities. Nasdaq securities must comprise a separate book which must be solely traded by a separate specialist. A specialist who is qualified under the provisions of this Chapter XXXV, and the provisions of Chapter XV, Specialists, Section 1, Registration, to trade either listed or Nasdaq securities, or both, cannot accept orders in, nor effect transactions in, both types of securities, at the same time.

Nothing in this section shall preclude any duly qualified specialist from occasionally substituting for, or acting as an alternate for, another specialist in either listed or Nasdaq securities, in accordance with Article XVI of the Constitution of the Boston Stock Exchange, Officers and Associates, Section 7, Alternatives for Members Absent. A specialist substituting for another specialist in accordance with the provisions of this section will be permitted to trade both Nasdaq and listed securities at the same time, during the period of substitution. In the case of an extended or permanent absence of a specialist qualified to trade Nasdaq securities, the firm from which the specialist is absent must promptly notify the Exchange and make arrangements to permanently replace the absent specialist in a reasonable amount of time, as determined by the Exchange. The Exchange reserves the right to

temporarily reassign some or all of the Nasdaq securities comprising an absent specialist's book in the event that a firm does not make suitable or timely arrangements for the replacement of the absent specialist.

#### **Floor Clerks**

Sec. 13. A qualified clerk under the control and supervision of a specialist may assist the specialist, in accordance with Chapter I—B, Section 3, Dealings on Floor—Persons.

#### **Odd-Lots and Odd-Lot Dealers**

Sec. 14. Notwithstanding any of the requirements regarding Odd-Lots and Odd-Lot dealers set forth in Chapter XII, Odd-Lot Dealers in Securities the Primary Market for Which is on Another Exchange, Chapter XIII, Odd-Lot Dealers in Fully Listed Securities Having a Primary Market on this Exchange, Chapter II, Dealings on the Exchange, Chapter V, Units of Delivery—Payment for Deliveries—Transfers, a member or member organization registered as a specialist in a Nasdaq security shall automatically be registered as the Odd-Lot Dealer in such security. Market orders will be accepted for execution as an odd-lot based on the best bid disseminated pursuant to SEC Rule 11Ac1-1 on a sell order, or the best offer disseminated pursuant to SEC Rule 11Ac1-1 on a buy order in effect at the time the order is presented at the specialist post, provided the order is for a number of shares less than full lot in said stock.

#### **Synchronization of Business Clocks**

Sec. 15. In accordance with NASD Rule 6953, each specialist trading Nasdaq securities shall synchronize his business clocks with a time source as specified by Nasdaq.

#### **Capital and Equity Requirements**

Sec. 16. Pursuant to Chapter XXII, Financial Reports and Requirements—Aggregate Indebtedness—Net Capital, Section 2, Capital and Equity Requirements, each member firm involved in the trading of Nasdaq securities shall maintain a liquidating equity for each specialist account of not less than \$200,000 in cash or securities. This equity requirement, as well as all other provisions of the section (including capital maintenance requirements), applies to each specialist account, without regard to the number of specialist accounts per firm.

#### **Margin Procedures**

Sec. 17. The Boston Stock Exchange Clearing Corporation will provide margin financing for approved

specialists dealing in Nasdaq securities, subject to the requirements and guidelines set forth in Chapter VIII, Minimum Amount of Margin on Transactions Made During the Course of a Single Day in Accounts of Members, Allied-Members, and Member-Organizations. For the purposes of this rule, transactions in Nasdaq securities will be considered to have been effected on the Boston Stock Exchange, and Nasdaq securities will be considered to be classified as stocks.

#### **Limitations on Trading Nasdaq Securities**

Sec. 18. (a) Minimum Number of Nasdaq securities. The first specialist in a firm will be required to register in and trade at least 20 Nasdaq securities. A specialist associated with a member firm, and associated with another specialist registered in the minimum number of BSE traded stocks shall register and act as specialist in not less than 15 Nasdaq securities.

(b) Minimum Holding Period for Nasdaq securities. Any stock awarded or assigned to a specialist must be held by the specialist for at least 6 months (excluding unprotected allocations), and the specialist is required to actively trade and maintain a market in each security in which he is registered.

#### **Application Procedure**

Sec. 19. Specialists are required to apply for registration in Nasdaq securities by utilizing either the UTP Form or the Add/Drop Form, depending on the status of the security being applied for. The allocation process will take place as specified elsewhere in this chapter.

Consistent with general Exchange stock allocation procedures, a specialist who first requests registration in an established Nasdaq security will generally be allocated that security, except where the performance of the specialist has been called into question. In that event, the Stock Allocation Committee may elect to competitively allocate that security.

#### **New Listing or New UTP**

Sec. 20. A specialist may apply to trade a newly admitted Nasdaq security, pursuant to the Nasdaq UTP plan (which permits trading of UTP admitted securities) as well as those newly dually listed. Such application will be subject to the allocation process.

#### **Allocation of Nasdaq Securities**

Sec. 21. The following procedures regarding the initial allocation of Nasdaq securities are designed to ensure an equitable representation of

member support of Nasdaq securities trading on the Boston Stock Exchange. They are structured so as to protect the firms who have established Nasdaq operations on the floor of the Exchange, while at the same time providing an opportunity for new interest and growth of this program in the foreseeable future from firms seeking to trade Nasdaq securities on the Exchange through meaningful stock allocations. Priority for admittance will be based on the date that the new firm becomes qualified to trade Nasdaq securities on the Exchange, as determined by Exchange staff. These procedures will remain in place for a two-year maturation period, following approval and commencement of trading. At the conclusion of this period, the Exchange will review the process and establish permanent Nasdaq security allocation procedures.

It should be understood that the registration rights to any Nasdaq securities awarded under this program through the allocation process may be transferred, rescinded or withdrawn by the Exchange. The initial two-year maturation period, by design, may entail the reallocation of an "unprotected" security. Further, any such specialist unit must continuously maintain fair and equitable markets in all issues assigned to it and may not for any reason transfer, sell or otherwise shift the benefit or responsibilities for trading securities awarded to it to another member firm. The Exchange will promptly initiate steps to reassign such trading privileges as deemed necessary if such circumstances arise. A minimum six-month holding period will be strictly enforced. The intent of this program is to establish competitive and liquid markets through solid support and a sustained commitment by its members.

*Note:* A firm may swap allocated stocks, with other existing and established BSE Nasdaq trading participants, in accordance with Section 25 of this Chapter XXXV. Further, in limited and exceptional circumstances, a member firm may petition the Executive Committee of the Exchange for permission to sell or otherwise transfer its Nasdaq trading privileges to another member firm prior to the end of the mandated six-month holding period. The responsibility to provide sufficient and justifiable reasons to seek such approval will be on the member firm registrant and must overcome the intent of this allocation process for a sustained commitment by such member. (Factors will include length of time trading, number of issues in each category and whether the proposed transferee is a new applicant.) The Executive Committee will evaluate any such request on its merits, and will ultimately base its decision on its determination of whether such a transfer is in the best interests of the

Exchange.\* The Executive Committee's decision in such a case shall be final.

\*Under certain circumstances, the Exchange (Executive Committee or its designated representative) may temporarily reassign some or all of the securities in question until an acceptable arrangement can be reached.

#### **Allocation Procedures**

Any member firm currently trading listed securities on the Exchange may apply for Nasdaq trading privileges, but may not drop listed securities in order to seek allocation of Nasdaq securities. The Exchange's goal is to establish a new product, which will expand the number of stocks available for execution on the BSE, rather than to replace or substitute its current market for listed securities.

The following procedures pertaining to the allocation of Nasdaq securities apply on a member firm basis, regardless of the number of specialists trading Nasdaq securities within a particular firm. The minimum number of stocks per book pursuant to this Chapter XXXV, Sec 18, will be 20 for the first specialist in a member firm and 15 for subsequent specialists in that same member firm. The initial allocation of Nasdaq securities will be limited to those member firms approved by the Exchange as of commencement date, and will be limited to those firms for the first 30 days.

Following this initial allocation, other firms may apply for Nasdaq securities, provided that they have met all of the requirements and have been approved by the Exchange to trade Nasdaq securities, as set forth in this Chapter XXXV, and elsewhere. The procedures for the allocation of Nasdaq securities will be based in part on the trading volume in Nasdaq securities and are as follows:

*Note:* The determination of which securities fall within the categories below (i.e., the top 100, top 300, etc.) will be based on the ranking on Nasdaq securities by the National Association of Securities Dealers, and published on the appropriate Nasdaq website as of the end of the preceding calendar quarter.

After the initial 30-day period, commencing on a date the Exchange specifies as the official start date of the trading of Nasdaq securities on the floor of the Exchange ("start date"), other qualified firms may apply for allocation of Nasdaq securities from the pool of unallocated securities. After an ensuing 30-day period (i.e. 60 days from the start date), each firm who is actively trading Nasdaq securities at the time a new firm applies for allocation ("existing firm") of Nasdaq securities may protect

("freeze") securities registered to it within the rankings noted below and at the times as specified below. The remaining ("unprotected") securities that the firm is trading will be available for re-allocation to a new firm (including any new firms which commenced trading 30 days after the start date), although no new firm may take more than 30% from within each of the four rankings of any one existing firm's ("unprotected") securities available for allocation. Thus, existing firms will not have their entire inventory, above the securities it has frozen, subject to reallocation at any one time, by any one firm. Notwithstanding this 30% provision, a new firm may seek reallocation of the at least one unprotected security for an existing firm, if 30% of the existing unprotected securities is less than one, and provided that the number of unprotected securities exceeds the freeze limits as set forth below. An existing firm will be able to freeze securities each time a new firm applies for allocation during the first six months of Nasdaq trading, according to the following restrictions:

Category 1—10 securities of the top 100

Category 2—20 securities from those rated 101–300

Category 3—20 securities from those rated 301–500

Category 4—20 securities from those rated 501 and above

*Note:* After the initial allocation of securities to those firms which are initially participating in the trading of Nasdaq securities, the Exchange reserves the right to reallocate any number of securities above 25 per firm which the firm has been initially allocated from the top 100 ranked securities, if it determines that it is in the best interest of the Exchange and the overall Nasdaq program.

As an example, assume four firms initially apply for, and receive allocations as follows:

Category	1	2	3	4
Firm A .....	25	25	25	25
Firm B .....	20	25	20	20
Firm C .....	25	20	20	20
Firm D .....	25	50	100	0

If Firm E applies for allocations during this initial six month period, Firm A can freeze 10 of the securities it has been allocated from the top 100 and 20 from each of the three remaining categories. Thus 15 securities from category 1, and 5 securities from categories 2, 3, and 4 would be available to Firm E. However, due to the 30% restriction, only 5 securities (30% × 15 unprotected) from category 1 and 2 securities from categories 2, 3, and 4 could be reallocated from Firm A.

**Firm B** would be able to freeze 10 of the 20 securities which it had been allocated from the top 100, although only 3 of the unprotected securities could be reallocated to Firm E. Likewise, Firm B would be able to freeze 20 of the securities which it had been allocated from category 2, and could lose up to 30%, or 2 securities from category 2 to Firm E. Categories 3 and 4 would be protected.

**Firm C** would be able to freeze all of the securities it has been allocated in categories 2, 3, and 4 but could lose 5 of the 15 unprotected securities in category 1.

**Firm D** would be able to freeze 10 of the securities it has been allocated from the top 100 (category 1). 30% of 30, or 9 securities, would be available from category 2, and 24 securities from category 3 would be available.

**Note:** Firm E, and any subsequent new firms applying for allocation, can not exceed the same restriction levels as set forth above (i.e., 10 of the top 100 or 20 from categories 2, 3, or 4) in total from the composite of issues drafted from the allocated but unprotected portions of existing Nasdaq books. It could however, request additional allocation from the remaining "unallocated" issues in any category. The intent here is to maintain an equitable distribution of protected stocks among the participants during this initial period of reallocations to new firms.

Now, assume **Firm G** is approved and applies for allocation one month after Firm E. Firms A through E would all be subject to reallocation under the same guidelines as above. Firms A–E would not be exempt from any future allocations, but would be able to freeze the prescribed amount of securities each time a new firm applies for allocation. Firm G, likewise, is subject to future allocations under the same guidelines.

**Note:** In the event an existing firm seeks additional allocations at any point during the two-year maturation period, notice will automatically be given to all other existing firms of the allocation request, allowing the other existing firms the opportunity to compete for allocation in the requested securities, within a prescribed time frame. The intent of this provision is to ensure fairness to all firms during maturation and evaluation stages of the Nasdaq stock allocation process. Additionally, no existing firm will be permitted to seek reallocation of unprotected securities from any other existing firm(s).

After the first six months from commencement of trading, and at each six-month anniversary interval through the remainder of the two-year maturation period, firms will be able to freeze an additional number of securities, as established by the Exchange, within each category. As the

**example** below indicates these additional protective limits will depend upon the remaining number of unprotected securities available in each category.

Category 1—3 additional securities within the top 100

Category 2—6 additional securities from those rated 101–300

Category 3—6 additional securities from those rated 301–500

Category 4—6 additional securities from those rated 501 and above

In certain, limited circumstances, an existing specialist may object to the re-allocation of a particular unprotected security or securities. In such a case, both the existing firm and the new firm will be asked to present to the Market Performance Committee ("MPC") their reasons for objecting to or supporting the allocation request. Existing firms will not be permitted to make blanket objections to having their unprotected securities reallocated, and they will be required to set forth tangible rationale justifying their objections. Likewise, new firms must justify their allocation requests. The firms will be allowed to present any documentation, testimonials or other relevant evidence supporting their position which they feel would benefit the MPC in their determination of whether the security[ies] in question should be allocated as requested, including, but not limited to, reasons based on market quality, payment for order flow, customer relationships, or other factors considered to be in the best interests of the Exchange's markets. The MPC will, based on the presentations and evidence, ultimately decide whether or not a particular security[ies] should be allocated to the new firm. The decision of the MPC can be appealed to the Board of Governors of the Exchange, whose decision shall be final. During the allocation request period, and any subsequent periods of committee deliberations and/or appeals, the security[ies] in question shall remain in the control of, and actively traded by, the existing firm.

The Exchange may limit the frequency and dates for allocation to additional participants in order to evaluate the impact of reallocations during this two-year maturation period. Although more than one new firm may be approved to begin trading Nasdaq securities on the floor of the Exchange at the same time, the first firm to be approved, chronologically, will be the first allowed to seek reallocation of securities from existing firms. Any such reallocation which may take place will result in new compositions of existing firm's books. Subsequently approved

new firms may seek reallocations from the newly composed books of the existing firms. In this way, existing firms are further protected from the possible burden of contemporaneous reallocations. The Exchange will monitor the effectiveness of the program in order to ensure that no disruption of markets will result from frequent reallocations among member firm specialists, and reserves the right to alter this stock allocation process at any time.

Finally, in the event that the number of protected securities (i.e., 10 firms with 10 each in the top 100) matches the limit within a particular category prior to the two year maturation period, the Exchange may re-evaluate those remaining securities unprotected to provide some form of meaningful competitive allocation process to ensure continued growth of this program. Following the two-year period the Exchange will examine its overall program to ensure competitive quality markets are maintained. All allocations regardless of the class or category of registration are subject to review by the Exchange pursuant to its Specialist Performance Evaluation Program ("SPEP").

#### **Criteria for Stock Allocation Committee To Consider During Nasdaq Security Allocation**

Sec. 22. In considering the allocation of Nasdaq securities, the Stock Allocation Committee shall consider the following factors, among other, giving proper weight to each of these measures as it sees fit, while maintaining consistency with previous decisions:

- Specialist Performance (SPEP)
- Specialist experience generally
- Specialist experience trading Nasdaq securities
- Specialist contributions to the market quality of the Boston Stock Exchange
- Specialist's reputation as to quality to executions
- Length of time elapsed since last allocation to specialist
- "Quality" of Nasdaq securities in specialist's book, in terms of volume, liquidity and volatility
- Specialist's reasons for seeking to trade the security, as set forth in his application and/or supplemental materials
- Documented marketing concerns of specialists form, e.g., order flow arrangements which are contingent on the retention of certain securities
- Market Quality criteria as set forth under the requirements of SEC Rules 11Ac1-5 and 11Ac1-6

### **Change in Listing Status of Nasdaq Security**

Sec. 23. (a) If a company which has its security solely registered as a Nasdaq exchange listed security, or in the event of a merger of a Nasdaq security company with a listed security company whereby the listed company is the "survivor" of the merger, the firm whose specialist was registered in the Nasdaq security shall be given preference to register to trade the listed security (subject to acceptable performance), provided that:

(1) the firm is eligible to trade, and currently registered in at least the minimum number of, as well as involved in the trading of, listed securities on the Exchange;

(2) no other member firm is currently registered in and trading the listed security of the surviving company. If another member firm is currently registered in the surviving company's listed security, that member firm will be allowed to continue to trade the security, whether registered as a primary or a competing specialist. The firm who originally traded the Nasdaq security of the company which was not a survivor of a merger, or which transferred its status and became an exchange listed security, will be eligible to apply as a competing specialist in that security, provided that all of the other requirements related to the trading of listed securities on the floor of the Exchange are met.

(b) In the event that a company changes its status from a listed security to become registered as a Nasdaq security, allocation preference will be provided to the firm which traded the listed security prior to its status change, provided that the firm is eligible to trade, and engaged in the trading of, Nasdaq securities. If the firm is not eligible to trade the newly registered Nasdaq security, the security's allocation will be subject to standard allocation procedures as outlined in this section, including, if necessary, deliberation and determination of allocation by the Stock Allocation Committee.

### **Merger of Two Nasdaq Securities**

Sec. 24. In the event of a merger of two companies whose securities are both registered as Nasdaq securities, with the resultant company's security remaining registered as a Nasdaq security, the surviving company's security shall be subject to Exchange allocation procedures governing such actions. As such, if two separate member firms are registered in the separate Nasdaq securities prior to the

merger, the allocation of the resultant security shall be subject to the following:

(1) If the surviving company remains in control of the newly formed or merged company, as determined by Exchange staff, the member firm, which was originally registered in the security of the surviving company, shall retain that security.

(2) If Exchange staff cannot determine the control of the surviving company, the Stock Allocation Committee, taking all relevant factors into consideration, shall determine the allocation of the security of the surviving company.

### **Swapping Stocks**

Sec. 25. Specialists shall be permitted to swap stocks on an "as requested" basis, subject to the following:

(1) Specialists who are interested in swapping stocks with another specialist are responsible for initiating and engaging in negotiations to arrange for the swap.

(2) Swapping of stocks must take place between two separate specialist firms.

(3) Specialists, may swap up to three stocks every six months, and must retain any swapped stocks for at least six months.

(4) Swapping for the intention of circumventing assignment, reassignment or any other procedures regarding Nasdaq securities is strictly forbidden.

(5) All swap arrangements must be submitted to the MPC for review, on the Stock Swap Agreement form.

(6) Repetitive stock swaps between two or more firms, or otherwise, for stock retention or any other purpose, are forbidden.

### **Specialist Request to Deregister in a Nasdaq Security**

Sec. 26. Generally, a specialist will be permitted to drop an allocated Nasdaq security, provided that a period of at least six months has elapsed since the original assignment. If a specialist is approved for deregistration in a Nasdaq security, the effective date of the deregistration will be no earlier than 5 days after notice is provided to all order sending firms and other floor specialists registered to trade Nasdaq securities that the specialist is deregistering in such security.

### **Disciplinary Action**

Sec. 27. As detailed in Chapter XV, Dealer Specialists, Section 17, Specialist Performance Evaluation Program, one possible sanction in the Exchange's disciplinary system regarding poor performance of specialists is the temporary or permanent cancellation of a specialist's registration in one or more

securities. Should this occur, the MPC will temporarily assign the security[ies] affected to another specialist. If the disciplinary action is, or becomes, permanent, the security[ies] will be available for assignment under the current stock allocation procedures.

### **Short Sales**

Sec. 28. No specialist shall effect a short sale for the account of a customer or for his own account in a Nasdaq security at or below the current best (inside) bid when the current best (inside) bid is below the preceding best (inside) bid in the security.

The provisions of this rule shall not apply to short sales by specialists that are in furtherance of the specialist's bona fide market making activities. Bona fide market making activity does not include activity that is unrelated to market making functions, such as index arbitrage and risk arbitrage that is independent from a member's market making functions. In the event that a short sale does occur pursuant to this bona fide market making exception, the burden is on the specialist to show that such sale was in furtherance of their bona fide market making activities.

### **Discussion**

Any activity by a specialist which is designed to circumvent this Short Sale rule through indirect actions, such as executions with other specialists or the facilitation of customer orders while being protected from loss are antithetical to the purposes of this rule, as are any manipulative type actions. For example, it would be considered a manipulative act, and in violation of this rule if either of the following occurred:

(1) A specialist alone at the inside best bid lowered its bid and then raised it to create an "up-bid" for the purpose of facilitating a short sale.

(2) A specialist with a long position raised its bid above the inside bid and then lowered it to create a "down-bid" for the purpose of precluding other market participants from selling short.

(3) a specialist agrees with another specialist or a customer to raise its bid in order to effect a short sale for the other party and is protected against loss on the trade or any other executions effected at its new bid price.

(4) a specialist entered into an agreement with another market participant or customer whereby it uses its exemption from this rule to sell short at successively lower prices, accumulating a short position, and subsequently offsetting those sales through a transaction at a prearranged

price, for the purpose of avoiding compliance with this rule, and with the understanding that the specialist would be guaranteed against losses on those trades.

### **Non-Liability of Exchange**

*Sec. 29. In accordance with Article IX, Section 10 of the Exchange Constitution, the Exchange shall not be liable for any loss sustained by a member or member organization resulting from the use of, or reliance on, the system through which the Exchange provides its members access to trade Nasdaq securities. Generally, a loss pertaining to an order that is entered through the BSE Nasdaq trading system that does not appear on a saved file will be absorbed by the entering member organization. A loss pertaining to an order that is entered through the BSE Nasdaq trading system which was designated for a particular specialist's post and which does appear on a saved file within the system will generally be absorbed by the specialist.*

## **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 Exchange 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 place specified in Item IV below. The Exchange 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**

According to the Exchange, the purpose of the proposed rule change is to set forth rules regarding the trading of certain over-the-counter ("OTC") securities, Nasdaq securities, on the floor of the Exchange, pursuant to unlisted trading privileges ("UTP") under Section 12(f) of the Act.<sup>8</sup> To facilitate this process, the Exchange is proposing to add Chapter XXXV to the BSE Rules. The rules set forth in Chapter XXXV specifically govern the trading of Nasdaq securities, with references to various sections of other Exchange rules relating to the trading of equity securities, as well as references to selected NASD rules, where

appropriate. Included within the Chapter are provisions for a two-year maturing Nasdaq stock allocation process, designed so as to provide meaningful allocation opportunities for firms that wish to become members of the Exchange and trade Nasdaq securities throughout the two-year maturation period. The following series of provisions appear in Chapter XXXV.

*Section 1:* defines various terminology used throughout the Chapter XXXV;

*Section 2:* discusses how orders for Nasdaq securities are to be transmitted to and from Exchange specialists. This section references other sections of the BSE Rules related to order display rules. Additionally, this section addresses the telephonic transmission of orders;

*Section 3:* references NASD Rule 4630, and sets forth the reporting requirements for Nasdaq securities transactions;

*Sections 4 & 5:* address automatic and manual execution of Nasdaq securities, and sets the minimum size parameter for automatic execution;

*Section 6:* discusses preopening orders and trading halts;

*Section 7:* discusses how cross transactions in Nasdaq securities are to be handled, with references to other BSE rules;

*Section 8:* designates the hours of business for the trading of Nasdaq securities on the floor of the Exchange, pursuant to Exchange rule;

*Section 9:* sets forth the parameters and conditions for guaranteed order acceptance and execution;

*Section 10:* pursuant to Exchange and NASD rules, designates various specialist responsibilities regarding orderly markets and best execution practices;

*Section 11:* in accordance with other Exchange rules, sets forth the registration requirements for Nasdaq specialists;

*Section 12:* discusses, in light of other Exchange Rules, limitations on specialists;

*Section 13:* discusses, in light of other Exchange Rules, limitations on floor clerks;

*Section 14:* addresses odd-lot orders and dealers, in reference to other similar Exchange rules;

*Section 15:* discusses the synchronization of business clocks, in concert with NASD Rule 6953;

*Section 16:* pursuant to Exchange rules, sets forth minimum capital and equity requirements for Nasdaq specialists;

*Section 17:* references existing BSE rules regarding margin procedures for all specialists;

*Section 18:* sets forth limitations on the number of Nasdaq securities held by

a specialist, and the amount of time a specialist must hold and actively trade a Nasdaq security;

*Sections 19 & 20:* explain the application procedure for registration in Nasdaq securities;

*Section 21:* sets forth the Exchange's procedures regarding the allocation of Nasdaq securities. The procedures are designed to cover the initial two-year period of Nasdaq trading on the floor of the Exchange. At the conclusion of the two-year period, the Exchange intends to re-examine the process and adopt permanent Nasdaq stock allocation procedures;

*Section 22:* lists the criteria which the Stock Allocation Committee can consider during Nasdaq security allocation;

*Sections 23 & 24:* discuss the procedures to be followed in the event that a Nasdaq security experiences certain corporate actions, or changes its listing status;

*Section 25:* explains the limitations on the swapping of Nasdaq securities between specialists;

*Section 26:* sets forth requirements for a specialist regarding deregistering in a Nasdaq security;

*Section 27:* references another Exchange rule in explaining possible disciplinary action in relation to the trading of Nasdaq securities;

*Section 28:* sets forth the Exchange's Short Sale Rule regarding Nasdaq securities; and

*Section 29:* explains the Exchange's liability limitations regarding the trading system used for the trading of Nasdaq securities.

#### **2. Basis**

The Exchange believes that the basis for the proposed rule change is Section 6(b)(5)<sup>9</sup> of the Act, along with Sections 6(b)(8),<sup>10</sup> 11A,<sup>11</sup> and 12(f)<sup>12</sup> of the Act. Specifically, the Exchange believes that the proposed rule change is consistent with Section 6(b)(5)<sup>13</sup> of the Act because permitting BSE specialists to trade eligible Nasdaq securities will promote just and equitable principles of trade and facilitate transactions in securities, thereby removing impediments to and perfecting the mechanism of a free and open market in a manner consistent with the protection of investors and the public interest.

<sup>9</sup> 15 U.S.C. 78f(b)(5).

<sup>10</sup> 15 U.S.C. 78f(b)(8).

<sup>11</sup> 15 U.S.C. 78k-1.

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

<sup>13</sup> 15 U.S.C. 78f(b)(5).

<sup>8</sup> 15 U.S.C. 78l(f).

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

The Exchange does not believe that the proposed rule change will impose any inappropriate burden on competition.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

The Exchange has neither solicited nor received comments on 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 self-regulatory organization 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-BSE-2001-01 and should be submitted by July 24, 2001.

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

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 01-16672 Filed 7-2-01; 8:45 am]

**BILLING CODE 8010-01-M**

## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-44469; File No. SR-CBOE-2001-25]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the Chicago Board Options Exchange, Inc. Relating to Marketing and Administrative Fees**

June 22, 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 May 21, 2001, the Chicago Board Options Exchange, Inc. (CBOE) filed with the Securities and Exchange Commission the proposed rule change as described in Items I, II, and III below, which Items the CBOE has prepared. The CBOE submitted Amendment No. 1 to the proposed rule change on June 18, 2001. The Commission is publishing this notice to solicit comments from interested persons on the proposed rule change, as amended.

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

The CBOE proposes to pay interest on the funds collected through its marketing fee program, to obtain the authority to refund periodically the excess collected balances in the marketing fee accounts, and to assess an administrative fee, effective July 1, 2001, to cover the costs of implementing these steps and to offset the overall cost of administering the marketing fee program. The text of the proposed rule change is available at the principal offices of the CBOE 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 CBOE 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 CBOE 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*

In August 2000, the CBOE instituted a marketing fee program that imposed a \$.40 per contract marketing fee on various options transactions executed on the CBOE. Under the plan, the proceeds from the fee were to be used by the appropriate Designated Primary Market Maker ("DPM") for marketing its services and attracting order flow to the CBOE.<sup>3</sup> The funds have been placed in separate accounts for each DPM according to the class of options involved in each transaction in which the fee was imposed. The fees collected in a particular class of option are applied only to the marketing expenses applicable to that class of option.

At times, some accounts have taken in more money than the DPMs have chosen to spend for marketing. The CBOE wishes periodically to refund account balances of \$50 or more to those who contributed the fees. Moreover, in collecting these fees over the last nine months, the CBOE has found that the proceeds from the fee are typically received into separate DPM accounts and kept there for at least several days before the DPM uses them. At the request of the association representing the CBOE's DPMs, the CBOE has determined to credit the accounts with interest earned from the collected funds. Finally, effective July 1, 2001, the CBOE intends to impose a monthly \$10,000 administrative fee to fund the implementation of these steps and to offset the overall costs related to its marketing fee program.

The CBOE proposes periodically to refund proceeds collected through the marketing fee program that exceed a specific percentage of the amounts collected in the previous three months. The refunds would be made on a *pro rata* basis to the market makers that contributed the funds. Currently, the CBOE anticipates refunding account balances that exceed 15% of the amount collected in each account from February 1, 2001 through April 30, 2001. The CBOE also proposes to implement any

<sup>14</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> Securities Exchange Act Release No. 43112 (August 3, 2000) 65 FR 49040 (August 10, 2000) (File No. SR-CBOE-2000-28).