

available for inspection and copying at the principal office of the Exchange.

All submissions should refer to the File No. SR-Amex-00-47 and should be submitted by March 7, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-45427; File No. SR-CBOE-2001-71]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Inc. to Incorporate Certain Principal Considerations in Determining Sanctions and to Incorporate in the Exchange's Minor Rule Violation Plan Violations of the Exchange's Order Handling Rules

February 8, 2002.

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 26, 2001, the Chicago Board of Options Exchange, Inc. ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 Exchange proposes to amend Exchange Rule 17.11 (Judgment and Sanction) to adopt sanctioning guidelines that the Exchange believes will promote consistency and uniformity in determining appropriate remedial sanctions through the resolution of disciplinary matters through offers of settlement or after formal disciplinary hearings. In addition, the Exchange proposes to amend Exchange Rule 17.50 (Imposition of Fines for Minor Rule Violations) to incorporate in its Minor Rule Violation Plan violations of the Exchange's order handling rules. The text of the proposed

rule change is available at the CBOE's Office of the Secretary 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 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 places 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

The purpose of the proposed rule change is to amend CBOE Rule 17.11 (Judgment and Sanction) to incorporate certain Principal Considerations in Determining Sanctions ("Principal Considerations") to promote consistency and uniformity in determining appropriate remedial sanctions through the resolution of disciplinary matters through offers of settlement or after formal disciplinary hearings. In addition, the proposed rule change would amend CBOE Rule 17.50 (Imposition of Fines for Minor Rule Violations) to incorporate in its Minor Rule Violation Plan violations of the Exchange's order handling rules, including violations of firm quote requirements pursuant to Exchange Rule 8.51; failure to promptly book and display limit orders that would improve the disseminated quote pursuant to Exchange Rules 7.7 and 8.85(b); failure to honor the priority of marketable customer orders maintained in the Customer Limit Order Book pursuant to Exchange Rule 6.45; and failure to use due diligence in order execution pursuant to Rules 6.73 and 8.85(b).

The Exchange filed this proposed rule change in accordance with Section IV.B.i of the Commission's September 11, 2000 Order Instituting Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934 ("Order"),<sup>3</sup> which required the Exchange to adopt rules establishing, or modifying existing, sanctioning guidelines such that they

are reasonably designed to effectively enforce compliance with options order handling rules. The Exchange believes that the Principal Considerations, as set forth in proposed Exchange Rule 17.11, codify the historical considerations the Exchange's Business Conduct Committee ("BCC") has applied in determining appropriate sanctions.

With respect to violations of the Exchange's order handling rules, the Exchange proposes that these violations covered under the plan should be included in a rolling twenty-four month "look-back" period. With respect to the failure to submit trade information on time and failure to submit trade information to the price reporter pursuant to Exchange Rule 6.51, the Exchange does not propose to amend the current "look-back" period or fine schedule as set forth in Exchange Rule 17.50(g)(4) at this time.<sup>4</sup> With respect to fines imposed upon Market-Makers or Floor Brokers for the conduct resulting in violations of the order handling rules as set forth in Exchange Rule 17.50(g)(5), the following fine schedule would be applied:

Number of offenses in any rolling twenty-four-month period	Fine amount
1st Offense ....	\$500 to \$1,500.
2nd Offense ...	\$1,000 to \$3,000.
3rd Offense ....	\$2,000 to \$5,000.
Subsequent Offenses.	\$3,500 to \$5,000 or Referral to Business Conduct Committee <sup>5</sup> .

The Exchange intends to use an automated surveillance program in the detection of order handling violations and a rolling twenty-four month look-back period in the determination of recidivist conduct.<sup>6</sup> As a result, the

<sup>4</sup> For violations of any of the Exchange's order handling rules, the BCC would consider the party's entire disciplinary history for purposes of determining whether violations should constitute a first, second or subsequent disciplinary action as set forth in CBOE's Internal BCC Sanction Guidelines. See letter from Pat Sexton, Assistant General Counsel, CBOE, to Deborah Lassman Flynn, Assistant Director, Division of Market Regulation ("Division"), Commission, dated February 8, 2002.

<sup>5</sup> The Exchange has agreed to submit an amendment to clarify that after a maximum of 6 offenses, subsequent offenses would be referred to the BCC. See telephone conversation between Mary L. Bender, Senior Vice President and Chief Regulatory Officer, CBOE, and Deborah Flynn, Assistant Director, Division, Commission, on February 6, 2002.

<sup>6</sup> The Exchange has agreed to submit an amendment to proposed Rule 17.50(a) to clarify this point. See telephone conversation between Mary L. Bender, Senior Vice President and Chief Regulatory Officer, CBOE, and Deborah Flynn, Assistant

<sup>11</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 Securities Exchange Act Release No. 43268 (September 11, 2000), Administrative Proceeding File No. 3-10282.

Exchange believes it is appropriate, at times, to aggregate individual violations of particular rules and treat such violations as a single offense.<sup>7</sup> The Exchange believes that aggregation would enable its staff to analyze large amounts of regulatory data and craft appropriate remedies, including minor fines, without being held to rigid schedules or being required to bring formal disciplinary action based on a minimal number of surveillance breaks. Similarly, the Exchange would, if no exceptional circumstances are present, impose a fine based upon a determination that there exists a pattern or practice of violative conduct. The Exchange would also be permitted to aggregate similar violations if the conduct was unintentional, incurred no injury to public investors, or the violations resulted from a single systemic problem or cause that has been corrected.

According to the Exchange, the proposed change to Exchange Rule 17.50 would allow any member who is issued a summary fine notice for conduct covered in paragraph (g)(5) of its rule, and also meets one of the levels described below, to have the opportunity to submit one written offer of settlement to the BCC in accordance with the provisions of Exchange Rule 17.8(a) (Submission of Offer), provided, however, that the Interpretations and Polices to Rule 17.8 would not apply to an offer made under Exchange Rule 17.50 and the member would be required to submit the offer within 30 days of the date of service of the written notice informing the member of the fine(s) imposed. The member would also be permitted to appear once before the BCC to make an oral statement in support of the offer. According to the Exchange, this is consistent with the current application of the rule as set forth in Exchange Rule 17.50 and Interpretation and Policy .01(b) under the Exchange's Minor Rule Violation Plan. Under the proposal, a member would be permitted to make one offer of settlement:

(1) When the summary fine amount is greater than \$2,500 but not more than \$5,000 for a single offense, regardless of

whether the single offense is the result of one violation or multiple violations aggregated together; or

(2) When the total fine for multiple offenses is greater than \$10,000 in the aggregate and not more than \$5,000 for any single offense, again regardless of whether any single offense is the result of one violation or multiple violations aggregated together.

The Exchange notes that to the extent that other Exchange rules or effective Regulatory Circulars include different schedules for summary fines related to the same types of conduct addressed herein, this rule change is intended to supersede all other existing provisions. Should the Commission approve this filing, the Exchange will file proposed rule changes effective upon filing to correct any discrepancies in the provisions of other Exchange rules or Regulatory Circulars.

#### (2) Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act,<sup>8</sup> in general, and furthers the objectives of sections 6(b)(5)<sup>9</sup> and 6(b)(7),<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 foster cooperation and coordination with persons engaged in regulating, clearing, settling, and processing information with respect to transactions in securities, to protect investors and the public interest, and enhances the effectiveness and fairness of the Exchange's disciplinary procedures. Lastly, the Exchange believes that the proposed rule change will refine and enhance the Exchange's Minor Rule Violation Plan to make it more efficient and effective.

#### *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 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*

No written comments were solicited or received with respect to 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 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 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 Exchange. All submissions should refer to File No. SR-CBOE-2001-71 and should be submitted by March 7, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

**Margaret H. McFarland,**  
Secretary.

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Director, Division, Commission, on February 6, 2002.

<sup>7</sup> The Exchange submitted to the Commission a letter, for which it requested confidential treatment, proposing how its regulatory staff would aggregate violations of the order handling rules, where the violations are identified through the Exchange's automated surveillance system. See letter from Mary L. Bender, Senior Vice President and Chief Regulatory Officer, CBOE, to John McCarthy, Associate Director, Office of Compliance, Inspections and Examinations, Commission, dated December 21, 2001.

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

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

<sup>10</sup> 15 U.S.C. 78f(b)(7).

<sup>11</sup> 17 CFR 200.30-3(a)(12).