important to encourage members of the Exchange to become AMMs, because FLEX Index Options are customized and do not have the same liquidity as standardized options, and AMMs are subject to greater risk when quoting such options.

III. Discussion

After careful consideration, the Commission has determined to approve the proposed rule change.[7] For the reasons discussed below, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with Section 6(b)(5) of the Act.[8]

The Commission believes that it is reasonable for the Exchange to offer AMMs a participation guarantee to encourage Exchange members to become AMMs and provide liquidity in FLEX Index Options. The Commission notes that the proposed entitlement of the AMM together with any guaranteed participation granted to the Submitting Member could not exceed 40 percent of an order. The Commission has found with respect to participation guarantees in other contexts that a maximum combined guarantee of 40 percent is not inconsistent with statutory standards of competition and free and open markets.[9]

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[10] that the proposed rule change (SR–CBOE–2002–09) be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[11]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–12981 Filed 5–22–02; 8:45 am]

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[7] In approving this proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[8] 15 U.S.C. 78f(b)(5). Section 6(b)(5) requires that the rules of an exchange, among other things, 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; and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

[9] *See, e.g.*, Securities Exchange Act Release Nos. 42455 (February 24, 2000), 65 FR 11388 (March 2, 2000) at 11398; and 43100 (July 31, 2000), 65 FR 48778 (August 9, 2000) at notes 96–99 and accompanying text.

[10] 15 U.S.C. 78s(b)(2).

[11] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–45935; File No. SR–CBOE–2002–08]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Chicago Board Options Exchange, Inc. Relating to the Allocation of Orders

May 15, 2002.

I. Introduction

On February 15, 2002, the Chicago Board Options Exchange, Inc. (''CBOE'' or ''Exchange'') submitted to the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] a proposed rule change relating to the allocation of orders. On March 22, 2002, and March 27, 2002, the CBOE submitted Amendment Nos. 1 and 2, respectively, to the proposed rule change. The proposed rule change, as amended, was published for comment in the **Federal Register** on April 8, 2002.[3] The Commission received no comments on the proposed rule change. This order approves the proposed rule change.

II. Description of Proposal

CBOE Rule 6.45, to be retitled ''Priority of Bids and Offers—Allocation of Trades,'' includes provisions that govern the allocation of an order on the Exchange when more than one market participant is bidding or offering at the best price to fill that order. As described below, the CBOE is proposing to amend Rule 6.45 by adding a number of provisions concerning specific aspects of the allocation process, and by clarifying how an order is to be allocated in certain situations where the rule currently is silent.

The CBOE is also proposing to amend Rule 6.45 by adding a clause that stipulates that the rule's provisions apply except as provided by certain other CBOE rules concerning the allocation of orders and the participations of various market participants. These other rules include, but are not limited to, CBOE Rule 6.2A (''Rapid Opening System''), CBOE Rule 6.8 (''RAES Operations''), CBOE Rule 6.9 (''Solicited Transactions''), CBOE Rule 6.47 (''Priority on Split Price Transactions''), CBOE Rule 6.74 (''Crossing Orders'') and CBOE Rule 8.87 (''Participation Entitlement of DPMs''), as well as CBOE Regulatory Circulars approved by the Commission concerning participation rights.[4]

The proposed rule change was submitted by CBOE pursuant to subparagraph IV.B.j. of the Commission's Order of September 11, 2000,[5] which requires that the options exchanges adopt new, or amend existing, rules to make express any practice or procedure ''whereby Market-Makers trading any particular option class determine by agreement the spreads or option prices at which they will trade any option class, or the allocation of orders in that option class.''

CBOE Rule 6.45 currently requires that the highest bid or lowest offer (''best bid or offer'') shall have priority. The rule also provides that, with limited exceptions set forth in 6.45(c) and (d), an order representing the best bid or offer in the customer limit order book receives priority over another order at the same best price. The proposed rule change would add CBOE Rule 6.45(a)(i) to provide that if more than one public customer order is represented in the customer limit order book at the best price, priority will be afforded to such orders in the sequence in which they were received by the OBO or DPM.

CBOE is also proposing to add CBOE Rule 6.45(a)(ii) to apply with respect to bids or offers for orders represented by a Floor Broker, a Designated Primary Market-Maker (''DPM'') acting as agent under CBOE Rule 8.85(b), or an Order Book Official (''OBO''), or bids or offers made in response to a specific request from a Market-Maker. In these instances, the proposed rule change would provide that the Floor Broker, DPM, OBO, or Market-Maker will determine which market participants responded at the best market at the time the market was established. This provision would further state that the Floor Broker, DPM, OBO, or Market-Maker will determine the sequence in which bids (offers) were made, subject to the following:

(1) If there are two or more bids (offers) at the best price, and an order in the customer limit order book is not involved, priority is afforded to the

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Securities Exchange Act Release No. 45670 (March 28, 2002), 67 FR 16782 (April 8, 2002) (''Notice'').

[4] The current participation rights of Designated Primary Market-Makers (''DPMs'') under CBOE rules are detailed in CBOE Regulatory Circular RG 00–193, dated December 28, 2000. *See* Securities Exchange Act Release No. 43750 (December 20, 2000), 65 FR 82420 (December 28, 2000).

[5] Order Instituting Public Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions, Securities Exchange Act Release No. 43268 (September 11, 2000).

orders in the sequence in which they were made.

(2) If the bids (offers) were made at the same time, or in the event the Floor Broker, DPM, OBO, or Market-Maker cannot reasonably determine the sequence in which the bids (offers) were made, priority will be apportioned equally.

(3) If the Floor Broker, DPM, OBO, or Market-Maker cannot reasonably determine the sequence in which the bids (offers) were made beyond a certain number of market participants, the Floor Broker, DPM, OBO, or Market-Maker will provide for the remaining contracts, if any, to be apportioned equally among those market participants who bid (offered) at the best price at the time the market was established.

(4) In the event a market participant declines to accept any portion of the available contracts, the proposed rule change would provide that any remaining contracts will be apportioned equally among the other market participants who bid (offered) at the best price at the time the market was established until all contracts have been apportioned.

The CBOE is also proposing to add CBOE Rule 6.45(iii) to provide that any contracts remaining in an order after the operation of CBOE Rule 6.45(ii) will be apportioned equally between any other market participants in the trading crowd who bid (offered) at the best price in a reasonably prompt manner subsequent to the time the market was established.

CBOE Rule 6.45(iv) would further provide that whenever a member requests from members of a trading crowd a single bid in excess of the RAES order eligibility size for that option class, as provided for in Interpretation .11 to CBOE Rule 8.7, each member of the trading crowd will be apportioned a share of the executed order based on an approximate pro rata percentage, to the extent practicable, of the crowd member's portion of the size of the original single bid. The new rule provision also would provide that the member requesting the single bid will determine what constitutes an approximate pro rata percentage of the order that is executed with respect to each member of the trading crowd who participated in making the single bid.

Finally, the proposed rule change would add Interpretation and Policy .02 to CBOE Rule 6.45, to clarify that the provisions of CBOE Rule 6.45 are subject to the operation of CBOE Rules 8.7, Interpretation and Policy .05,[6] and CBOE Rule 8.51 (''Firm Disseminated Market Quotes'').

III. Discussion

After careful consideration, the Commission has determined to approve the proposed rule change.[7] For the reasons discussed below, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b)(5) of the Act.[8]

The Commission believes that the provision of the proposed rule change specifying the allocation sequence where more than one public customer order is represented in the customer limit order book clarifies that priority in such situations is established according to the sequence in which the orders were received by the OBO or DPM and is consistent with other Exchange rules that reflect the principle of time priority.

The Commission also believes that other provisions of the proposed rule change better specify the Exchange's priority rules by setting forth how an order is to be allocated among market participants bidding or offering at the best price in situations when: (1) Their competing bids or offers are made simultaneously; (2) the sequence in which their bids or offers were made cannot be reasonably determined; or (3) the sequence cannot be reasonably determined beyond a certain number of participants. The Commission believes that the proposed amendment establishes a fair and equitable manner of apportioning an order in these situations by providing that the bids or offers have equal priority, so that each participant receives an equal share of the order.

In the Commission's view, the proposed rule change further provides important clarification as to who is responsible, in any given trade, to determine which market participants responded with bids or offers at the best market at the time a market was established, and to allocate the trade according to the applicable priority rules. As discussed above, the proposed rule change assigns this responsibility to the Floor Broker, the DPM acting as agent, the OBO that is representing the order to which market participants are responding, or to a market maker with respect to bids made in response to his specific request. The Commission believes that this is a reasonable method of assigning responsibility for allocating a trade, particularly because the market participant representing the order or initiating the trade generally is in the best position to determine the identity and sequence of who responded. The CBOE has represented that it has the ability to determine the identity of the individual who allocated a particular trade,[9] and the Commission believes that the ability to identify such individual is important to the Exchange's ability to monitor for any violation of Exchange allocation rules.

The proposed rule change further specifies how participation in a trade is allocated in the situation where a member requests a single bid from members of a trading crowd and the trade is effected pursuant to Interpretation .11 to CBOE Rule 8.7.[10] The Commission believes that the proposed amendment, which would provide that the order be allocated based on an approximate pro rata percentage, to the extent practicable, of the respective sizes that crowd participants have indicated they are willing to buy or sell, is a reasonable way to apportion participation in such trades. The Commission believes that it is reasonable, as provided by the proposed rule change, to assign the member who requested the single bid the responsibility to determine what constitutes an approximate pro rata percentage of the order for each participant.

The proposed rule change also would make clear that in the event a market participant declines to accept a portion of the contracts to which he or she is entitled, the remainder is to be apportioned equally among the participants who bid or offered at the best price when the market was established. The Commission notes, in this connection, that the CBOE's proposed Interpretation and Policy .02

[6] Interpretation and Policy .05 to CBOE Rule 8.7 provides: Unless an options class is exempted by the appropriate Market Performance Committee, under normal market conditions a Market-Maker's bid or offer for a series of options of unspecified size is for five contracts except that a Market-Maker may be compelled to buy or sell a specific number of contracts at the disseminated bid or offer pursuant to his obligations under Rule 8.51.

[7] In approving this proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[8] 15 U.S.C. 78f(b)(5). Section 6(b)(5) of the Act requires that the rules of an exchange, among other things, be 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 of a free and open market and a national market system, and, in general, to protect investors and the public interest; and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

[9] *See* Notice, *supra* note 3, at n.6.

[10] *See* Securities Exchange Act Release No. 45800 (April 22, 2002), 67 FR 21305 (April 30, 2002) (SR–CBOE–2001–65).

to CBOE Rule 6.45 provides that the provisions of CBOE Rule 6.45 are subject to CBOE Rule 8.7, Interpretation and Policy .05, and CBOE Rule 8.51, which set forth market maker responsibilities and firm quote requirements.

The Commission further notes that the CBOE has made clear that a DPM that already has been allocated its DPM participation entitlement amount would not receive a share of the declined contracts unless the other market participants do not wish to participate in the declined contracts.[11] The Commission believes that this will help assure fair allocation of orders and maintain a competitive environment on the Exchange.

The Commission also finds reasonable CBOE's proposal to apportion equally among any other market participants in the trading crowd who bid at the best price in a reasonably prompt manner subsequent to the time the market was established, any contracts that remain in an order after giving effect to the priority rules described above.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[12] that the proposed rule change (SR–CBOE–2002–08) be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[13]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–12982 Filed 5–22–02; 8:45 am]

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[11] *See* Notice, *supra* note 3, at n.8.

[12] 15 U.S.C. 78s(b)(2).

[13] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–45936; File No. SR–CBOE–2002–10]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Chicago Board Options Exchange, Inc. Relating to the Allocation of Orders for Lead Market-Makers and Supplemental Market-Makers Logged On to the Exchange's Rapid Opening System

May 15, 2002.

I. Introduction

On February 15, 2002, the Chicago Board Options Exchange, Inc. (''CBOE'' or ''Exchange'') submitted to the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'') [1] and Rule 19b–4 thereunder,[2] a proposed rule change relating to the allocation of orders for Lead Market-Makers (''LMMs'') and Supplemental Market-Makers (''SMMs'') logged on to the Exchange's Rapid Opening System (''ROS''). On March 15, 2002 and March 22, 2002, CBOE submitted Amendment Nos. 1 and 2, respectively, to the proposed rule change. The proposed rule change and Amendment Nos. 1 and 2 were published for comment in the **Federal Register** on April 2, 2002.[3] The Commission received no comments on the proposed rule change. This order approves the proposed rule change.

II. Description of Proposal

CBOE is proposing changes to Interpretation and Policies .01 of CBOE Rule 6.2A (''Interpretation .01''), relating to the allocation of orders for LMMs and SMMs logged onto ROS.[4] The proposed rule change was filed by the CBOE pursuant to subparagraph IV.B.j. of the Commission's Order of September 11, 2000, which requires that respondent options exchanges adopt new, or amend existing, rules to make express any practice or procedure ''whereby market makers trading any particular option class determine by agreement * * * the allocation of orders in that option class.'' [5]

Currently, Interpretation .01 limits the use of ROS to LMMs and SMMs in S&P 100 (''OEX'') Options. The proposed rule change would establish that ROS may be used by LMMs and SMMs appointed pursuant to CBOE Rule 8.15 to conduct rotations in any options class. The proposed rule change would also clarify that despite CBOE Rule 6.2A(b), which assigns ROS contracts to trade to participating market-makers, ROS contracts to trade will be assigned only to the LMMs and SMMs logged onto ROS in crowds to which LMMs and SMMs are appointed.

The proposed rule change would also permit the appropriate Floor Procedure Committee to establish a participation right for the LMM who determines the formula for generating automatically updated market quotations during the trading day and provides the primary quote feed for an option class during the current expiration month. This participation right would apply only to ROS contracts to trade, and would be subject to the following conditions: (1) The LMM would receive this participation right only during the time it is actually providing the primary quote feed for an option class; and (2) the LMM must log onto ROS the minimum number of times established by the appropriate Floor Procedure Committee.

As part of the proposed rule change, the CBOE also submitted the draft text of a Regulatory Circular that would establish a specific entitlement formula for qualifying LMMs, and would be used by the appropriate Floor Procedure Committee to adopt the participation entitlement. The formula provides for participation entitlements that range from 34 percent to 40 percent for the LMM providing the primary quote feed, depending on the total number of appointed LMMs and SMMs in the option, when the number is three or more. If the number is two, each of the two will be assigned an equal portion of ROS contracts, and if there is only one, all ROS contracts to trade will be assigned to the appointed LMM or SMM.[6]

In explaining the purpose of the participation guarantee, the CBOE stated that it has introduced a vendor quote program in OEX to replace the Autoquote system. The vendor system accepts a quote stream from a firm's proprietary quote system and then sends this quote information to the Trading Support System to be disseminated as market quotes. The CBOE believes that the LMM that provides the primary quote feed for an option class during the current expiration cycle provides a valuable service that ensures that the quotes are being updated in timely fashion to reflect the current state of the market.

III. Discussion

After careful consideration, the Commission has determined to approve the proposed rule change.[7] For the reasons discussed below, the Commission finds that the proposed

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Securities Exchange Act Release No. 45640 (March 25, 2002), 67 FR 15644 (April 2, 2002) (''Notice'').

[4] ROS is the Exchange's automated system for opening classes of options at the beginning of the trading day or for re-opening classes of options during the trading day. *See* CBOE Rule 6.2A.

[5] *See* Order Instituting Public Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions. Securities Exchange Act Release No. 43268 (September 11, 2000).

[6] The Exchange has stated that changes to this Regulatory Circular, including changes to a participation entitlement formula, will be submitted to the Commission pursuant to Section 19(b) of the Exchange Act. *See* Notice.

[7] In approving this proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).