

proposed is consistent with section 6(b)(5)⁷ of the Act in that it is 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 notes that the Book Indicator was adopted as part of the CBOE's initiative to provide split-price Retail Automatic Execution System ("RAES") executions for incoming customer orders when the prevailing best bid (offer) is generated by a existing customer order in the CBOE book.⁸ At the time split-price execution functionality was adopted, CBOE's disseminated quote did not display size. Thus, the Book Indicator served to alert a customer that a RAES eligible order might not be executed in its entirety at CBOE's displayed price, and that he might receive a split-price execution. Now that CBOE disseminates quotes with size, the Commission believes that the Book Indicator is no longer necessary. Therefore, the Commission believes that it is appropriate for the Exchange to eliminate the Book Indicator, and remove all references to the Book Indicator from the CBOE rules. The Commission believes that the proposed rule change will streamline and clarify the Exchange rules by eliminating reference to an indicator that no longer is necessary.

It is therefore ordered, pursuant to section 19(b)(2) of the Act,⁹ that the proposed rule change (SR-CBOE-2002-44) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Margaret H. McFarland,

Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46723; File No. SR-ISE-2002-24]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the International Securities Exchange, Inc. Relating to Quotation Size

October 25, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on October 11, 2002, the International Securities Exchange, Inc. ("ISE" 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 ISE. 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 that all ISE's quotations would be firm for all incoming orders for their full disseminated size. The ISE would retain a one-contract minimum size for quotations when they interact with quotations entered by other ISE market makers. The proposed rule change would be implemented when the Commission approves the proposal and grants the Exchange an exemption from Rule 11Ac1-1 (the "Firm Quote Rule") under the Act, and when the Exchange implements technical enhancements to its system necessary to support this change. Below is the text of the proposed rule change. Additions are italicized. Brackets indicate deletions.

* * * * *

Rule 804.—Market Maker Quotations

(a) Options Classes. A quotation only may be entered by a market maker, and only in the options classes to which the market maker is appointed under Rule 802.

(b) Size Associated with Quotes. A market maker's bid and offer for a series of options contracts shall be accompanied by the number of contracts at that price the market maker is willing to buy [from] or sell *(i) upon receipt of an order ("Order Execution Size") and (ii) upon interaction with a quotation entered by another market maker on the Exchange ("Quotation Execution Size")* [to (i) Public Customers (the "Public

Customer Size") and (ii) Non-Customers (the "Non-Customer Size")]. Unless the Exchange has declared a fast market pursuant to Rule 704, a market maker may not initially enter an *Order Execution Size* [a bid or offer with a Public Customer] of less than ten (10) contracts. Where the size associated with a market maker's bid or offer falls below ten (10) contracts due to executions at that price and consequently the size of the best bid or offer on the Exchange would be for less than ten (10) contracts, the market maker shall enter a new bid or offer for at least ten (10) contracts, either at the same or a different price. Every market maker bid or offer must have a *Quotation Execution* [a Non-Customer] Size of at least one (1) contract.

(c) Two-Sided Quotes. A market maker that enters a bid (offer) on the Exchange must enter an offer (bid) within the spread allowable under Rule 803(b)(4).

(d) Firm Quotes. (1) Market maker bids and offers are firm for *orders and Exchange market maker quotations* [Public Customer Orders and Non-Customer Orders] both under this Rule and Rule 11Ac1-1 under the Exchange Act ("Rule 11Ac1-1") for the number of contracts specified [for each] according to the requirements of paragraph (b) above. Market maker bids and offers are not firm under this Rule and Rule 11Ac1-1 if:

(i) a system malfunction or other circumstance impairs the Exchange's ability to disseminate or update market quotes in a timely and accurate manner;

(ii) the level of trading activities or the existence of unusual market conditions is such that the Exchange is incapable of collecting, processing, and making available to quotation vendors the data for the option in a manner that accurately reflects the current state of the market on the Exchange, and as a result, the market in the option is declared to be "fast" pursuant to Rule 704;

(iii) during trading rotations; or

(iv) any of the circumstances provided in paragraph (c)(3) of Rule 11Ac1-1 exist.

(2) Within thirty seconds of receipt of an *order* [a Public Customer Order (Non-Customer Order)] to buy or sell an option in an amount greater than the *Order Execution Size*, or *within thirty seconds of another Exchange market maker entering a quotation at a price executable against the market maker's quotation* [Public Customer Size (Non-Customer Size)], that portion of the order equal to the *Order Execution Size*, or the *Quotation Execution Size*, as the case may be, [Public Customer Size

⁷ 15 U.S.C. 78f(b)(5).

⁸ See Securities Exchange Act Release No. 43932 (February 6, 2001), 66 FR 10332 (February 14, 2001).

⁹ 15 U.S.C. 78s(b)(2).

¹⁰ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

(Non-Customer Size)] will be executed and the bid or offer price will be revised.

[Supplementary Material to Rule 804

.01 Notwithstanding the provisions of paragraph (b), for the "Enhanced Size Pilot" described in .02 below, a Primary Market Maker may not initially enter a bid or offer for a Public Customer of less than 100 contracts, and a bid or offer for Non-Customers (except for other market makers) of less than 50 contracts. Also for the purposes of the Enhanced Size Pilot, a Competitive Market Maker may not initially enter a bid or offer for a Public Customer of less than 50 contracts, and a bid or offer for Non-Customers (except for other market makers) of less than 25 contracts. Where the size associated with a market maker's bid or offer falls below such specified size, the market maker shall enter a new bid or offer for at least the specified size, either at the same or a different price.

.02 The Enhanced Size Pilot shall operate as follows:

- (1) The Enhanced Size Pilot shall operate until October 31, 2002;
- (2) Securities included in the Enhanced Size Pilot are options on: Nasdaq 100 Trust; Sun Microsystems; EMC Corp.; Qualcomm; Wells Fargo & Co.; Oracle; Lucent; Juniper Networks; Intel; AOL Time Warner; Tyco; Citigroup; Cisco; Applied Materials; Microsoft; General Electric; Broadcom; Nokia; Siebel Systems; Banc of America; Ciena; Dell; Fannie Mae; Motorola; Merrill Lynch; Nvidia; Xilinx; Amazon.com; Halliburton; Nextel Communications; J.P. Morgan Chase; ADC Telecommunication; Best Buy; Calpine; General Motors; and Hewlett Packard; and
- (3) The size requirements in the Enhanced Size Pilot will not apply:
 - (a) To options that expire beyond the nearest three expiration months;
 - (b) To "Deep-in-the-Money" options;

or
(c) On an option's last three trading days prior to expiration.
03. For the purpose of this Rule, "Deep-in-the-Money" means all options with strike prices that are in the money by 12 percent or more in relation to the at-the-money strike price.]

* * * * *

Rule 805.—Market Maker Orders

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(c) *Limitations on Orders.* A market maker shall not enter more than one order every fifteen (15) seconds for its own account in options on the same underlying security; provided, however, that this shall not apply to multiple

orders in different series of options on the same underlying security if such orders are part of a spread.

[Exemptive Authority. Until the earlier of (1) one year from the date on which the Exchange commences operations or (2) the date on which the Exchange opens all options Groups for trading, an Exchange official designated by the Board may grant market makers exemptions from the requirements of subparagraphs (b)(2) and (3) of this rule, subject to the following:

(1) If a market maker has only one Membership, and thus is assigned to only one Group, any exemption would end when the assigned Group is open for trading, regardless of the number of options classes that begin trading in the assigned Group;

(2) If a market maker has multiple Memberships, and thus is assigned to trading in more than one Group, the exemption would end when all the market maker's Groups are open for trading, again regardless of the number of options classes that begin trading in the assigned Groups; as the market maker's assigned Groups open for trading, the amount of trading the market maker would be permitted to execute outside of its assigned Groups would be reduced;

(3) Any exemption would be conditioned on the member performing market maker functions in the classes they trade;

(4) An exemption could be revoked by the Exchange at any time if the market maker is not acting in accordance with the terms of the exemption; and

(5) No exemption would have a term of more than one month, but would be renewable on a monthly basis until the market maker's group(s) was open for trading.]

* * * * *

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 ISE 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 ISE 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 this proposed rule change is to provide that all ISE quotations would be firm for all incoming orders for their full disseminated size. This would be the first time that any options exchange provides non-customers (that is, broker-dealers) with full access to the entire disseminated size of the exchange's quotations for all their orders. The specifics of the proposal are as follows:

- Each ISE Primary Market Maker and Competitive Market Maker would enter a quotation with a single size, available in full for all incoming orders, whether from customers, broker-dealers, ISE market makers or market makers on other exchanges.
- Each market maker also would be able to establish a second quotation size that would be available when its quotation interacts with another ISE market maker quotation. This would limit an ISE market maker's exposure when it establishes a quotation at the same price as an existing ISE market maker quotation in the system. While this interaction of quotations is beneficial from a price-discovery standpoint, there is significant risk in this situation because execution can occur simultaneously in multiple series. While market makers would be able to limit this risk by setting their size to a smaller number of at least one contract, ISE market makers would be able to access the full size of another market maker's quotation by sending an order in that series.³

• The ISE also proposes to prohibit market makers from sending more than one order every 15 seconds in options on the same underlying security. ISE Rule 717(h) currently imposes this limitation on orders that Electronic Access Members send to the Exchange. This limitation reduces a market maker's exposure across multiple series of options.⁴ This restriction, however, does not currently apply to market maker orders since market makers generally have established nominal

³ Implementing this aspect of the proposal would require the Commission to grant an exemption from the Firm Quote Rule. While that rule permits market makers to set smaller sizes for all non-customer orders, it does not permit different quotation sizes for different categories of professionals. Simultaneously with submitting this proposed rule change, the ISE submitted a separate exemption request.

⁴ See Securities Exchange Act Release No.44017 (February 28, 2001), 66 FR 13820 (March 7, 2001) (File No. SR-ISE-2000-20).

quotations for other market makers. Because ISE market makers now would be able to enter orders accessing another market maker's full size, ISE proposes to extend this 15-second limitation to ISE market maker orders.

• Finally, the ISE proposes two technical "clean up" changes to its rules. First, the Exchange proposes to delete language from Rule 804 regarding the "enhanced size pilot" that would expire on October 31, 2002. Second, the Exchange proposes to delete language from Rule 805 regarding limited exemptive authority that expired a year after the Exchange commenced trading.

2. Statutory Basis

The basis for this proposed rule change is the requirement under section 6(b)(5) of the Act⁵ to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

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

The ISE believes that the proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

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 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 in the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of the ISE. All submissions should refer to File No. SR-ISE-2002-24 and should be submitted by November 22, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46732; File No. SR-NASD-2002-137]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. Relating to Technical Corrections to the Trade or Move Process in the Nasdaq Order Collection and Display Facility ("SuperMontage")

October 28, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4² thereunder, notice is hereby given that on October 4, 2002, the National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, the Nasdaq Stock Market, Inc. ("Nasdaq"), submitted to 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 Nasdaq. On October 21, 2002, Nasdaq filed an

amendment to the proposed rule change.³ The proposed rule change, as amended, has been filed by Nasdaq as a "non-controversial" rule change under Rule 19b-4(f)(6)⁴ under the Act. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

Nasdaq is filing with the Commission technical rule changes to NASD Rule 4613(e)(1) to harmonize the language with recent approved rule proposals.

The text of the proposed rule change is available at the Office of the Secretary, the Nasdaq 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, Nasdaq included statements concerning the purpose of and basis for the proposed rule change, as amended, and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. Nasdaq has prepared summaries, set forth in Sections A, B and C below, of the most significant aspects of such statements.

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

1. Purpose

Nasdaq has filed numerous rule proposals relating to NASD Rule 4613(e), and also has filed numerous rule proposals relating to SuperMontage. In the process of compiling the changes to Rule 4613(e), Nasdaq has discovered several

³ See letter from Jeffrey S. Davis, Associate General Counsel, Nasdaq to Terri Evans, Assistant Director, Division of Market Regulation, Commission dated October 18, 2002 ("Amendment No. 1"). In Amendment No. 1, Nasdaq redesignated certain provisions in NASD Rule 4613(e)(1) to correct erroneous references to NASD Rule 4613(e)(2). In addition, the rule text was amended to replace all uses of the word "message" with the word "order" to eliminate inadvertent inconsistencies within Rule 4613(e)(1).

⁴ 17 CFR 240.19b-4(f)(6). For purposes of determining the effective date and calculating the 60-day period within which the Commission may summarily abrogate the proposed rule change under Section 19(b)(3)(C) of the Act, the Commission considers that period to commence on October 21, 2002, the date Nasdaq filed Amendment No. 1. See 15 U.S.C. 78s(b)(3)(C).

⁶ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

⁵ 15 U.S.C. 78f(b)(5).