

### 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. Comments may also be submitted electronically at the following e-mail address: *rule-comments@sec.gov*. All comment letters should refer to File No. SR-GSCC-2002-07. This file number should be included on the subject line if e-mail is used. To help us process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. 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 Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of GSCC. All submissions should refer to File No. SR-GSCC-2002-07 and should be submitted by July 11, 2003.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>4</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 03-15646 Filed 6-19-03; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48033; File No. SR-ISE-2003-17]

### Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change and Amendment No. 1 by the International Securities Exchange, Inc. To Initiate a Pilot Program That Allows the Listing of Strike Prices at One-Point Intervals for Certain Stocks Trading Under \$20

June 16, 2003.

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 June 11, 2003, 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 and II below, which Items have been prepared by the Exchange. The ISE filed Amendment No. 1 to the proposal on June 13, 2003.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons and to grant accelerated approval to the proposed rule change, as amended, through June 5, 2004.

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

The Exchange proposes to initiate a pilot program ("Pilot Program") that will allow the Exchange to list options on selected stocks trading below \$20 at one-point intervals. The text of the proposed rule change appears below. Additions are in *italics*; deletions are in brackets.

<sup>4</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 letter from Michael Simon, Senior Vice President and General Counsel, ISE, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated June 13, 2003 ("Amendment No. 1"). In Amendment No. 1, the Exchange amended its proposed rule text to state that the proposed pilot program will expire on June 5, 2004.

### Rule 504. Series of Options Contracts Open for Trading

\* \* \* \* \*

(d) *Except as otherwise provided in this Rule 504 and Supplementary Material hereto,* [T]he interval between strike prices of series of options on individual stocks will be:

(1) \$2.50 or greater where the strike price is \$25.00 or less;

(2) \$5.00 or greater where the strike price is greater than \$25.00; and

(3) \$10 or greater where the strike price is greater than \$200.00.

\* \* \* \* \*

#### Supplementary Material

.01 *\$1 Strike Pilot Program: The interval between strike prices of series of options on individual stocks may be \$1.00 or greater (" \$1 strike prices") provided the strike price is \$20.00 or less, but not less than \$3. The listing of \$1 strike prices shall be limited to options classes overlying no more than five (5) individual stocks (the " \$1 Strike Pilot Program") as specifically designated by the Exchange. The Exchange may list \$1 strike prices on any other options class if those classes are specifically designated by other securities exchanges that employ a \$1 Strike Pilot under their respective rules.*

*To be eligible for inclusion into the \$1 Strike Pilot Program, an underlying stock must close below \$20 in its primary market on the previous trading day. After a stock is added to the \$1 Strike Pilot Program, the Exchange may list \$1 strike prices from \$3 to \$20 that are no more than \$5 from the closing price of the underlying on the preceding day. For example, if the underlying stock closes at \$13, the Exchange may list strike prices from \$8 to \$18. The Exchange may not list series with \$1 intervals within \$0.50 of an existing \$2.50 strike price (e.g., \$12.50, \$17.50) in the same series, and may not list \$2.50 intervals (e.g., \$12.50, \$17.50) below \$20 under paragraph (d)(1) of Rule 504 for any class included within the \$1 Strike Pilot Program if the addition of \$2.50 intervals would cause the class to have strike price intervals that are \$.50 apart. Additionally, the Exchange may not list long-term option series at \$1 strike price intervals for any option class selected for the \$1 Strike Pilot Program.*

*A stock shall remain in the \$1 Strike Pilot Program until otherwise designated by the Exchange. The \$1 Strike Pilot Program shall expire on June 5, 2004.*

## 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 III 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

ISE Rule 504 establishes the guidelines regarding the addition of series for trading on the Exchange. Under ISE Rule 504(d), the ISE currently has the ability to list \$2.50 intervals for strike prices under \$25, \$5 intervals for strikes between \$25 and \$200, and \$10 intervals for strikes above \$200.<sup>4</sup> The ISE currently lists options on 205 stocks trading under \$20, including Cisco, Oracle, Sun Microsystems, Lucent, Nortel, JDS Uniphase, Amazon, Nextel, AT&T, Motorola and Hewlett-Packard. These stocks are among the most widely held and actively traded equities listed on the New York Stock Exchange, Inc. or Nasdaq, and the options overlying these stocks are actively traded as well.

The ISE notes that when a stock underlying an option trades at a lower price, it takes a larger percentage gain in the stock for an option to become in-the-money. For example, when a stock trades at \$8, an investor who wants to buy a slightly out-of-the-money call option would need to buy the call with a \$10 strike price. At these levels, the stock price would need to register a 25% change before it reached \$10 (*i.e.*, in-the-money status). The ISE notes that a 25% gain in the underlying is especially large given the lessened degree of volatility that has accompanied many stocks and options over the past several months. Due to the recent preponderance of low priced stocks, member firms have expressed an interest in listing additional strike prices on these classes so that they can provide their customers with greater flexibility in their investment choices. For this reason, the Exchange proposes

to implement a Pilot Program, as described below.

*Pilot Program Eligibility:* The Exchange proposes to add Supplementary Material .01 to ISE Rule 504 to allow the ISE to list series with \$1 strike price intervals on equity option classes that overlie up to five individual stocks, provided that the strike prices are \$20 or less, but not less than \$3. The Exchange would make the determination of which underlying stocks are to be included in the Pilot Program. A class becomes eligible for inclusion in the Pilot Program when the underlying stock price closes below \$20 in its primary market on the previous business day. Underlying stocks trading under \$20 that are not a part of the Pilot Program would continue to be eligible for trading in \$2.50 and \$5.00 intervals.

Although the ISE may select only up to five individual stocks to be included in the Pilot Program, the Exchange would not be precluded from also listing options on other individual stocks at \$1 strike price intervals if other options exchanges listed those series pursuant to their respective rules.

*Procedures for Adding \$1 Strike Price Intervals:* The Exchange proposes to adopt new Supplementary Material .01 to ISE Rule 504 to specify the standards that will apply when adding additional \$1 strike price intervals under the Pilot Program.<sup>5</sup> Under the proposal, the closing price of the underlying stock serves as the reference point for determining which \$1 strike prices the Exchange may open for trading. Specifically, the Exchange will only list \$1 strike prices that fall within a \$5 range of the underlying stock price, and no strike prices will be added outside of the \$5 range. For example, if the underlying stock trades at \$6, the Exchange could list \$1 strikes from \$3 to \$11.<sup>6</sup> The ISE believes that this proposed range-format will significantly restrict the number of series that may be added at any one time.

Under ISE Rule 504, the Exchange may list strike prices with \$2.50 intervals when an underlying stock trades below \$25. Accordingly, several options classes have \$7.50, \$12.50 and \$17.50 strike prices (the "\$2.50 series" or "\$2.50 intervals"). To further avoid

<sup>5</sup> ISE Rule 504(c) provides for the addition of series "when the Exchange deems it necessary to maintain an orderly market, to meet customer demand, or when the market price of the underlying stock moves substantially from the initial exercise prices." If the Exchange initiates options trading on a new class whose underlying stock is below \$20, Rule 504(b) governs the establishment of strike prices.

<sup>6</sup> As indicated above, strike prices for options included in the Pilot Program may not be less than \$3 or greater than \$20.

the proliferation of series, the Exchange does not intend to list \$1 strike prices at levels that "bracket" existing \$2.50 intervals (*e.g.*, \$7 and \$8 strikes would not be added if there is an existing \$7.50 strike). Accordingly, the Exchange will not list \$7, \$8, \$12, \$13, \$17 and \$18 levels in an expiration month where there are corresponding \$2.50 intervals. As the \$2.50 intervals are "phased-out," as described below, the Exchange would introduce the \$1 levels that bracket the phased-out price. For example, when the \$7.50 series expires, the Exchange would replace it by issuing a new month with \$7 and \$8 intervals.

*Procedures for Phasing-Out \$2.50 Strike Price Intervals:* When a stock becomes part of the Pilot Program, the Exchange will begin the corresponding process of phasing-out the existing \$2.50 intervals on the same stock in favor of \$1 intervals. To phase-out the \$2.50 intervals, the Exchange would first delist those \$2.50 series for which there is no open interest. Second, the Exchange would no longer add new expiration months at \$2.50 intervals below \$20 when the existing months expire. This would cause the \$2.50 strike price intervals below \$20 to be phased-out when the farthest-out month with a \$2.50 interval eventually expires.

*\$1 Strikes for Long-Term Options:* The ISE will not list long-term options (also known as "LEAPS") in equity options classes at \$1 strike price intervals.

*Procedures for Adding Expiration Months:* ISE Rule 504(e) will continue to govern the addition of expiration months for all options, including those included in the Pilot Program. Pursuant to this rule, the Exchange generally opens four expiration months for each class upon initial listing of an options class for trading, and upon expiration of the near-term month, the Exchange lists an additional expiration month. With respect to options in the Pilot Program, the Exchange may list an additional expiration month for a \$1 strike series provided that the underlying stock price closes below \$20 on its primary market on expiration Friday. If the underlying closes at or above \$20 on expiration Friday, the Exchange would not list an additional month for a \$1 strike series until the stock again closes below \$20.

*Procedures for Deleting \$1 Strike Price Intervals:* At any time, the Exchange may cease trading options series, including series with \$1 strike prices, by submitting a cessation notice to The Options Clearing Corporation ("OCC").<sup>7</sup> As discussed above, if the

<sup>7</sup> Among the reasons for submitting a cessation notice are the expiration of available \$1 strikes (*i.e.*,

<sup>4</sup> ISE Rule 504(g) establishes guidelines for listing \$2.50 strikes for a set number of options classes with series trading between \$25 and \$50.

underlying closes at or above \$20 on expiration Friday, the Exchange would not list any additional months with \$1 strike prices until the stock subsequently closed below \$20. If the underlying does not subsequently close below \$20, thereby precluding the listing of additional strike prices and months, the existing \$1 series will eventually expire. When the near-term month is the only series available for trading, the Exchange may submit a cessation notice to OCC. Upon submission of that notice, the underlying stock would no longer count towards the five stock Pilot Program, thereby allowing the Exchange to list classes on an additional stock. Once the Exchange submits the cessation notice, it would not list any additional months for trading with \$1 strikes below \$20 (unless the underlying once again closed below \$20).<sup>8</sup>

**OPRA Capacity:** The ISE believes that OPRA has the capacity to accommodate the increase in the number of series added pursuant to the Pilot Program. The Pilot Program is limited to only five underlying securities, and the Pilot Program will result in an increase of between seven and 14 additional strikes for each underlying (depending on the number of existing \$2.50 strikes listed). Thus, the Pilot Program will result in a maximum of 70 additional series, which is a small increase in the approximately 47,000 thousand series currently traded on the ISE. Currently, OPRA's one-minute peak has been less than one-third of its total capacity.

## 2. Basis

The Exchange believes that the addition of \$1 strike prices would stimulate customer interest in options overlying lower-priced stocks by creating greater trading opportunities and flexibility. The Exchange further believes that \$1 strike prices would provide customers with the ability to more closely tailor investment strategies to the precise movement of the underlying security. For these reasons, the Exchange believes the proposed rule change is consistent with the Act and the rules and regulations thereunder and, in particular, the requirements of

the underlying stock price remains at or above \$20), series proliferation concerns, and delisting because of low price, merger, takeover or other events. In any event, with prior notice to the membership and customers, ISE would continue to have the ability to cease trading series that become inactive and have no open interest.

<sup>8</sup> If the underlying stock trades below \$20 after submission of the cessation notice by the Exchange, the ISE could list \$1 strike prices again provided it included the class as one of the five classes permitted under the Pilot Program.

section 6(b) of the Act.<sup>9</sup> Specifically, the Exchange believes the proposed rule change is consistent with section 6(b)(5)<sup>10</sup> requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, 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 this 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*

The ISE has not solicited, and does not intend to solicit, comments on this proposed rule change. The ISE has not received any unsolicited written comments from members or other interested persons.

## 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, 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 filings will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-ISE-2003-17 and should be submitted by July 11, 2003.

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

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

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

After careful review, 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.<sup>11</sup> In particular, the Commission finds that the proposed rule change is consistent with section 6(b)(5) of the Act,<sup>12</sup> which requires, among other things, that the rules of a national securities exchange be designed 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. Specifically, the Commission believes that the proposed listing of one point strike price intervals in selected equity options on a pilot basis should provide investors with more flexibility in the trading of equity options overlying stocks trading at more than \$3 but less than \$20, thereby furthering the public interest by allowing investors to establish equity options positions that are better tailored to meet their investment objectives. The Commission also believes that the Exchange's limited Pilot Program strikes a reasonable balance between the Exchange's desire to accommodate market participants by offering a wide array of investment opportunities and the need to avoid unnecessary proliferation of options series. The Commission expects the Exchange to monitor the applicable equity options activity closely to detect any proliferation of illiquid options series resulting from the narrower strike price intervals and to act promptly to remedy this situation should it occur. In addition, the Commission requests that the ISE monitor the trading volume associated with the additional options series listed as a result of the Pilot Program and the effect of these additional series on market fragmentation and on the capacity of the Exchange's, OPRA's, and vendors' automated systems.

As noted above, the Commission is approving the ISE's proposal on a pilot basis. In the event that ISE proposes to extend the Pilot Program beyond June 5, 2004, expand the number of options eligible for inclusion in the Pilot Program, or seek permanent approval of the Pilot Program, it should submit a Pilot Program report to the Commission

<sup>11</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

along with the filing of such proposal.<sup>13</sup> The report must cover the entire time the Pilot Program was in effect, and must include: (1) Data and written analysis on the open interest and trading volume for options (at all strike price intervals) selected for the Pilot Program; (2) delisted options series (for all strike price intervals) for all options selected for the Pilot Program; (3) an assessment of the appropriateness of \$1 strike price intervals for the options the ISE selected for the Pilot Program; (4) an assessment of the impact of the Pilot Program on the capacity of the ISE's, OPRA's, and vendors' automated systems; (5) any capacity problems or other problems that arose during the operation of the Pilot Program and how the ISE addressed them; (6) any complaints that the ISE received during the operation of the Pilot Program and how the ISE addressed them; and (7) any additional information that would help to assess the operation of the Pilot Program.

The Commission finds good cause for approving the proposal prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. The ISE's Pilot Program is identical to a CBOE pilot program ("CBOE Pilot") that the Commission approved.<sup>14</sup> Notice of the CBOE Pilot was published for comment<sup>15</sup> and the Commission received one comment letter, which supported the CBOE's proposal. Accordingly, the Commission believes that the ISE's Pilot Program proposal raises no issues of regulatory concern. Amendment No. 1 to the proposal clarifies the proposal by specifying the date on which the Pilot Program will expire. For these reasons, the Commission believes that there is good cause, consistent with sections 6(b)(5) and 19(b) of the Act,<sup>16</sup> to approve the ISE's proposal, as amended, on an accelerated basis.

## V. Conclusion

*It is therefore ordered*, pursuant to section 19(b)(2) of the Act,<sup>17</sup> that the proposed rule change (SR-ISE-2003-17) and Amendment No. 1 thereto are hereby approved, on an accelerated

<sup>13</sup> The Commission expects the ISE to submit a proposed rule change at least 60 days before the expiration of the Pilot Program in the event the ISE wishes to extend, expand, or seek permanent approval of the Pilot Program.

<sup>14</sup> See Securities Exchange Act Release No. 47991 (June 5, 2003), 68 FR 35243 (June 12, 2003) (order approving File No. SR-CBOE-2001-60).

<sup>15</sup> See Securities Exchange Act Release No. 47753 (April 29, 2003), 68 FR 23784 (May 5, 2003).

<sup>16</sup> 15 U.S.C. 78f(b)(5) and 78s(b).

<sup>17</sup> 15 U.S.C. 78s(b)(2).

basis and as a pilot program, through June 5, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>18</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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**BILLING CODE 8010-01-P**

## DEPARTMENT OF STATE

[Public Notice 4384]

### Bureau of Political-Military Affairs; Export of Defense Articles and Defense Services to India and Pakistan

**AGENCY:** Department of State.

**ACTION:** Notice.

**SUMMARY:** Notice is hereby given that requests for export and retransfer of defense articles, defense services and related technical data to India or Pakistan pursuant to section 38 of the Arms Export Control Act (AECA) will be considered on a standard case-by-case basis. This notice reverses the policy of denial set forth in **Federal Register** Notices published on May 20, 1998 and June 17, 1998.

**EFFECTIVE DATE:** June 20, 2003.

**FOR FURTHER INFORMATION CONTACT:**

Peter J. Berry, Director, Office of Defense Trade Controls Licensing, Directorate of Defense Trade Controls, Bureau of Political-Military Affairs, Department of State (202) 663-2700.

**SUPPLEMENTARY INFORMATION:** In 1998, pursuant to a Presidential determination under section 102(b) of the AECA, two **Federal Register** notices were published (63 FR 27781, May 20, 1998; and 63 FR 33122, June 17, 1998) that revoked all licenses and approvals to export or otherwise transfer defense articles and defense services to India and Pakistan, respectively. These **Federal Register** notices set forth a policy of denial for new requests for such licenses/approvals.

The President issued a waiver of the Glenn Amendment sanctions on India and Pakistan on September 22, 2001. Pursuant to section 9001(b) of the Department of Defense Appropriations Act, 2000 (Pub. L. 106-79), the President determined and certified to Congress that the sanctions and prohibitions in subparagraphs (B), (C), and (G) of section 102(b)(2) of the AECA would not be in the national security interests of the United States. (66 FR 50095, October 2, 2001.)

<sup>18</sup> 17 CFR 200.30-3(a)(12).

Section 9001(e) of the Department of Defense Appropriations Act, 2000, specifies that the issuance of a license for the export of defense articles, services, or technology to India or Pakistan pursuant to the waiver authority is subject to the same requirements as are applicable to the export of items described in section 36(c) of the AECA, including the transmittal of information and the application of Congressional review procedures. Consistent with this requirement, the Department provided a certification to Congress of proposed licenses or other approvals for the export of defense articles and defense services for India or Pakistan, regardless of the dollar value of the export.

The Foreign Relations Authorization Act, Fiscal Year 2003 (Pub. L. 107-228) amended the congressional notification requirements stated in section 9001(e) of the Department of Defense Appropriations Act, 2000. Pursuant to section 1405(b) export licenses to Pakistan or India must be reported to Congress only if they meet or exceed the dollar value thresholds of section 36(c) of the AECA. These thresholds are \$14,000,000 for major defense equipment and \$50,000,000 for defense articles or services.

Finally, on November 21, 2002 Missile Technology Control Regime (MTCR) Category I missile sanctions imposed on the Pakistani Ministry of Defense (MOD) and the Space and Upper Atmosphere Research Commission (SUPARCO) expired. These sanctions were imposed for engaging in missile-related cooperation with Chinese entities (Section 73(a)(1) of the Arms Export Control Act (AECA) and Section 11B of the Export Administration Act (EAA) of 1979, as amended). Therefore, licenses for the transfer of items on the United States Munitions List (USML) to the Pakistani MOD and SUPARCO will no longer be denied based on these sanctions.

In light of the Presidential waiver of the Glenn Amendment sanctions, the reestablishment of the dollar thresholds for congressional notification, and the expiration of the MTCR Category I missile sanctions, it is the policy of the Department to consider, on a standard case-by-case basis, applications and other requests for approval pertaining to defense articles/defense services for export/transfer to India or Pakistan.

Dated: June 25, 2003.

**Lincoln P. Bloomfield, Jr.,**

*Assistant Secretary, Bureau of Political-Military Affairs, Department of State.*

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**BILLING CODE 4710-25-P**