

the date of a Board determination, the first two years in an easily accessible place, a record of the determination and the basis and information upon which the determination was made. This record will be subject to examination by the Commission and its staff.

7. For six years following the issuance of a Fund's VIPER Shares, the Fund will (a) record and preserve any investor complaints or reports of confusion concerning the Conversion Privilege that are communicated to the Fund, VGI and/or VMC and (b) record data tracking the number of investors that, after VIPER Shares are offered, purchase the Fund's Conventional Shares and, within 90 days, convert those shares into VIPER Shares. The Fund will preserve this information in an easily accessible place, and the information will be subject to examination by the Commission and its staff.

8. Applicants' Web site, which is and will be publicly accessible at no charge, will contain the following information, on a per VIPER Share basis, for each Fund: (a) The prior business day's closing NAV and the midpoint of the bid-asked spread at the time the Fund's NAV is calculated ("Bid-Asked Price") and a calculation of the premium or discount of the Bid-Asked Price in relation to the closing NAV; and (b) data for a period covering at least the four previous calendar quarters (or the life of a Fund, if shorter) indicating how frequently each Fund's VIPER Shares traded at a premium or discount to NAV based on the Bid-Asked Price and closing NAV, and the magnitude of such premiums and discounts. In addition, the Product Description for each Fund will state that applicants' Web site has information about the premiums and discounts at which the Fund's VIPER Shares have traded.

9. The VIPER Prospectus and annual report will include, for each Fund: (a) The information listed in condition 8(b), (i) in the case of the VIPER Prospectus, for the most recently completed calendar year (and the most recently completed quarter or quarters, as applicable), and (ii) in the case of the annual report, for no less than the immediately preceding five fiscal years (or the life of the Fund, if shorter); and (b) the cumulative total return and the average annual total return for one, five and ten year periods (or the life of the Fund, if shorter) of (i) a VIPER Share based on NAV and Bid-Asked Price and (ii) the Fund's Target Index.

For the Commission, by the Division of Investment Management, pursuant to delegated authority.

**Jill M. Peterson,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48740; File No. SR-Amex-2002-09]

### Self-Regulatory Organizations; Order Approving a Proposed Rule Change and Amendments No. 1 through 11 thereto by the American Stock Exchange LLC Relating to Registered Options Traders Use of the Electronic Entry Device

November 3, 2003.

#### I. Introduction

On February 12, 2002, the American Stock Exchange LLC ("Amex" or "Exchange") filed with the Securities and Exchange Commission ("Commission" or "SEC"), 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> a proposed rule change relating to registered options traders use of the electronic entry device. The Exchange submitted Amendments No. 1, 2, 3, 4, 5, 6, 7, 8<sup>3</sup>, 9,<sup>4</sup> 10,<sup>5</sup> and 11<sup>6</sup> on February 25, 2002,

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> For Amendments No. 1 through 8, the Exchange filed a new Form 19b-4 each time, which replaced and superseded the original proposal and all previous amendments in their entirety.

<sup>4</sup> Letter from Claire P. McGrath, Senior Vice President and Deputy General Counsel, Amex, to Elizabeth King, Associate Director, Division of Market Regulation ("Division"), Commission, dated July 24, 2003 ("Amendment No. 9"). Amendment No. 9 transfers to the list of rules enforced by the Amex Enforcement Department under paragraph (g) of Amex Rule 590 the requirement set forth in proposed Amex Rule 933, Commentary .04(d) that the specialist use his best efforts to attempt to ensure that the registered options trader responsible for disseminating the best bid or offer receives an allocation of the next automatic execution.

<sup>5</sup> The Exchange filed a new Form 19b-4, which replaced and superseded the original proposal and all previous amendments in their entirety.

<sup>6</sup> Letter from Claire P. McGrath, Senior Vice President and Deputy General Counsel, Amex, to Elizabeth King, Associate Director, Division, Commission, dated September 11, 2003 ("Amendment No. 11"). Amendment No. 11 revises proposed changes to Amex Rule 590(g) to clarify that a specialist who fails to properly allocate executed contracts to the price-improving registered options trader must pay restitution in amount calculated by multiplying the number of contracts that should have been allocated to the price-improving registered options trader by the number of underlying shares represented by each contract, which would then be multiplied by half of the

May 6, 2002, May 29, 2002, June 18, 2002, July 17, 2002, September 16, 2002, January 21, 2003, July 15, 2003, July 25, 2003, August 26, 2003, and September 12, 2003, respectively. The proposed rule change and Amendments No. 1 through 11 were published for comment in the **Federal Register** on September 25, 2003.<sup>7</sup> The Commission received no comments on the proposal. This order approves the proposed rule change and Amendments No. 1 through 11.

#### II. Description of the Proposed Rule Change

Given the number of series traded for each option class and the necessity for the re-calculating and re-quoting of each series in response to changes in the price of the underlying security, the Exchange developed an automated quotation updating system known as XTOPS. The specialist and registered options traders rely upon XTOPS to calculate and disseminate a single immediately updated quotation for each option series. XTOPS uses option valuation formulas (such as the Black-Scholes Model) to generate options quotations based on a number of variables.<sup>8</sup> It is the specialist's responsibility to determine for each option class the variables used in the XTOPS formula. However, the quotations generated and displayed by XTOPS may result in firm quote obligations of both the specialist and registered options traders to buy or sell options at quoted prices and sizes.<sup>9</sup> The dissemination of an XTOPS quote can be overridden when a customer limit order represents the best bid or offer or when a registered options trader chooses on a series-by-series basis to better the disseminated bid or offer.

The Exchange is now proposing new Commentary .04 to Amex Rule 933, to allow registered options traders' direct access to the Electronic Entry Device ("EE Device") to input their own quotes for dissemination as the best bid or offer.<sup>10</sup> The EE Device would be

spread between the option's bid and offer at the time the order was executed.

<sup>7</sup> Securities Exchange Act Release No. 48495 (September 16, 2003), 68 FR 55422.

<sup>8</sup> These variables include the price of the underlying stock, time remaining to expiration, interest rates (or "cost to carry", the amount of interest on the money used to pay for the options position during the period prior to expiration of the option series), dividends (both declared and anticipated) and volatility.

<sup>9</sup> See Rule 11Ac1-1 under the Act ("Quote Rule"), 17 CFR 240.11Ac1-1, and Amex Rule 958A.

<sup>10</sup> The Exchange submitted the proposed rule change in response to subparagraph IV.B.h(i)(aa) of the Commission's September 11, 2000 Order ("Order"), which requires the Exchange to "adopt new, or amend existing, rules concerning its

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available for registered options traders to use in all option classes traded on the Exchange.<sup>11</sup> In active option classes where there is currently an Exchange-employed systems clerk, registered options traders would either input their own quotes or instruct a systems clerk to do so on their behalf. Only registered options traders physically located in the trading crowd would be permitted to directly input quotes into the EE Device or give such instructions to a systems clerk.

Once the registered options trader or systems clerk inputs the quote into the EE Device, the proposed rule would require that: (i) The price improving registered options trader announce loudly and audibly in the crowd that he has improved the displayed market to ensure that other crowd participants are aware that the market has been improved, enabling other crowd participants to also quote competitively; and (ii) the specialist be specifically alerted so that a "book bid or offer" indicator is activated and the next otherwise Auto-Ex eligible trade is routed directly to the Amex Options Display Book ("AODB") for allocation to the registered options trader that caused the improved quote to be disseminated. In addition to blocking an otherwise eligible Auto-Ex order from being executed and allocated by the Auto-Ex system, activation of the "book bid or offer" indicator would block an XTOPS calculated quote that is worse than the registered options trader's disseminated quote from being disseminated. Activation would not, however, block a quote that is better than the registered options trader's disseminated quote from being disseminated.

Once an execution occurs and/or the price improving registered options trader is no longer entitled to priority, the specialist would be required to remove the "best bid or offer" indicator so that Auto-Ex eligible orders would again be sent to Auto-Ex and the

automated quotation and execution systems which substantially enhance incentives to quote competitively and substantially reduce disincentives for market participants to act competitively." 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).

<sup>11</sup> The EE Device is currently used by Exchange-employed systems clerks in busy option classes to input individual quotes from the specialist on a series by series basis that better the quote being calculated and disseminated by XTOPS. A quote entered using the EE Device is sent directly to the Exchange's Market Data System for immediate dissemination to the Options Price Reporting Authority. This quote, when it betters the market being disseminated by XTOPS, will override or displace the XTOPS quote.

dissemination of XTOPS calculated quotes is resumed. The EE Device would not automatically decrement the size of the disseminated quote when an execution occurs. The quote would be required to be manually adjusted to reflect any revision to the disseminated size.

The price improving registered options trader would be permitted to cancel his quote at any time prior to the execution of a trade through the use of the EE Device (regardless of whether inputted by the registered options trader or the systems clerk), if that was the method in which the quote was entered, or through the specialist, if that was the method chosen. The registered options trader would be required also to alert the specialist that he is removing his quote, so the specialist can in turn remove the "book bid or offer" indicator in XTOPS, and announce loudly and audibly that he is canceling his quote.

Pursuant to the requirements of the Quote Rule and Exchange Rule 958A, the registered options trader as the responsible broker or dealer is obligated to execute any customer order at his bid or offer up to the disseminated size. To be relieved of that obligation with respect to a specific quote, one of the exceptions to the Quote Rule must apply, which generally provide that the responsible broker or dealer must communicate a revised quotation to the Exchange prior to the presentation of an order. Thus, a registered options trader using the EE Device to disseminate quotes would continue to be obligated pursuant to the Quote Rule until he has communicated a revised quote to the Exchange through the removal or cancellation of the quote on the EE Device.

Registered options traders would be required to improve the best bid or offer by an amount equal to at least the minimum price variation as set forth in Exchange Rule 952 for the quote to be inputted into the EE Device. The minimum size quote that could be inputted into the EE Device by or on behalf of a registered options trader would be 20 contracts, unless the Auto-Ex eligible size parameter for that option class is less than 20 contracts, in which case the minimum quote size would be the same as the lesser Auto-Ex eligible size parameter for that option class. Currently, the EE Device disseminates a default size for each new quote. The disseminated size may be set at a higher or lower amount or increased by the specialist to reflect additional liquidity at that quote. The default size would be set at the minimum quote size as discussed above.

The Exchange represents that there is at least one EE Device unit at every trading post and multiple units at posts where active option classes trade and that the number of devices currently in place on the trading floor would be sufficient to provide registered options traders with ready and easy access to a means for disseminating their quotes. However, since this is a new use for the EE Device, the Exchange represents that it will monitor the uses of the EE Device by registered options traders and activity in the option classes at each trading post and will add additional devices when necessary. The Exchange is able to install additional EE Devices at the trading posts with, preferably, a one-day notice so that they can be installed either before or after trading hours.

The specialist in a given option class may also disseminate or cause to be disseminated his own individual, price improving quote separate from the XTOPS calculated quote, provided he is physically located at the trading post at the time he inputs his quote, has only disseminated one quote per series on the same side of the market, has announced loudly and audibly to the crowd that he has improved the disseminated bid or offer, has improved the best bid or offer by an amount equal to at least the minimum price variation set forth in Rule 952, and has disseminated the minimum quote size. The specialist would not be able to use the EE Device to disseminate his individual price improving quote since he already has the means to input a quote into the Market Data System through XTOPS in the same manner used today to disseminate a customer limit order. Once the specialist has caused his individual quote to be disseminated, he will activate the "book bid or offer" indicator and the next otherwise Auto-Ex eligible trade is routed directly to the AODB for allocation to the specialist.

The specialist would be required to use best efforts to attempt to ensure that the registered option trader responsible for disseminating the best bid or offer receives an allocation of the next incoming order for the amount he is entitled to pursuant to Exchange rules. A specialist who failed to use best efforts to attempt to ensure that the next Auto-Ex execution is appropriately allocated to the price improving registered options trader would be fined pursuant Amex Rule 590(g) of the Exchange's Minor Rule Violation Fine System. In addition to the fine assessed pursuant to the Minor Floor Violation Fine System, violations of this provision would require the payment of

restitution. Restitution would be calculated by multiplying the number of contracts that should have been allocated to the price-improving registered options trader by the number of underlying shares represented by each contract, which would then be multiplied by half of the spread between the option's bid and offer at the time the order was executed.

If more than one registered options trader and/or the specialist has disseminated or caused to be disseminated the same price improving quote, priority would be established for the registered options traders in the order in which the quotes were announced loudly and audibly to the trading crowd. If, however, the sequence in which the disseminated quotes were made cannot be reasonably determined, priority would be afforded to the price improving registered options traders and/or specialist as a group. Exchange Rule 950(d), Commentary .06 and Exchange Rule 950(n), Commentary .03 govern allocations of contracts when more than one registered options trader and/or the specialist has disseminated the same price improving quote and time priority cannot be established.

However, pursuant to the proposed rule change, the price improving registered options traders' quote would retain priority until one of the following occurs: (i) Auto-Ex execution depleted the disseminated size; (ii) an amount equal to the minimum quote size has been allocated; (iii) the registered options trader withdraws the quote; (iv) the quote is matched or improved by the specialist's automated quotation system quote, provided specialists using an Exchange-approved proprietary automated quotation updating system have not programmed the system to immediately match or improve the price improving registered options trader's quote; (v) the quote is improved by another registered options trader; or (vi) the market is improved by an order placed on the limit order display book. With respect to subparagraph (iv) above, the Exchange represents that it will monitor the use of proprietary automated quotation updating systems through the review of complaints from members in the trading crowd as well as observations of Floor Officials and Exchange personnel to determine if the system has been programmed to immediately match or improve the price improving registered options trader's quote.

The Exchange notes that Exchange rules regarding customer priority and parity would continue to apply to the allocation of trades pursuant to the proposed rule change. Exchange Rule

111, Commentary .07 provides that a registered options trader, when establishing or increasing a position, may not retain priority over or have parity with an off-Floor order. Thus, only registered options traders closing or decreasing a position may be on parity with a customer order.

### III. Discussion

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the Act and the rules and regulations promulgated thereunder applicable to a national securities exchange and, in particular, with the requirements of Section 6(b) of the Act.<sup>12</sup> Specifically, the Commission finds that approval of the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act<sup>13</sup> in that it is designed to facilitate transactions in securities; 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, processing information with respect to, and facilitating transactions in securities; 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 proposed rule change, by permitting registered options traders to use an EE Device at the trading post to input their own quotes for dissemination as the best bid or offer and then providing price improving registered options traders with an allocation of the next Auto-Ex execution, should help to encourage competitive quoting. In addition, the Commission believes that providing a method for specialists to input their own price improving quotes separate from the autoquote, and then routing the next otherwise Auto-Ex eligible order to the AODB for allocation to the specialist, should provide an additional incentive for specialists to quote competitively. The Commission believes that the proposal is an important first step towards achieving compliance with the Order's directive to substantially enhance incentives to quote competitively and substantially reduce disincentives for market participants to act competitively.

The Commission notes that the proposal requires the specialist to use best efforts to ensure that a price

improving registered options trader receives his allocation. The Commission believes that imposition of a fine, under the Exchange's Minor Rule Violation Plan, on a specialist who fails to use best efforts to ensure that the next Auto-Ex execution is appropriately allocated, as well as the requirement that such specialist pay restitution to the injured registered options trader, should provide sufficient safeguards to help ensure that the manual allocation to the appropriate registered options trader occurs.

### IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, 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.<sup>14</sup>

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>15</sup> that the proposed rule change (SR-Amex-2002-09) and Amendments No. 1 through 11 are approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48733; File No. SR-BSE-2003-16]

### Self-Regulatory Organizations; Notice of Filing of a Proposed Rule Change and Amendment Nos. 1 and 2 Thereto and Order Granting Accelerated Approval to a Proposed Rule Change and Amendment Nos. 1 and 2 Thereto by the Boston Stock Exchange, Inc. Relating to Shareholder Approval of Equity Compensation Plans

October 31, 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 September 15, 2003, the Boston Stock Exchange, Inc. ("BSE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described

<sup>12</sup> 15 U.S.C. 78f(b). In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

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

<sup>14</sup> 15 U.S.C. 78f(b)(5).

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

<sup>16</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.