

terms, or by an official interpretation of the NASD, to a specific time period outside of the 4 p.m. to 6:30 p.m. time period. This obligation applies with particular force to the requirement to protect customer limit orders set forth in NASD IM-2110-2.

- The NASD's Short Sale Rule (NASD Rule 3350) will not apply during the after-hours session.

Nasdaq staff will continue to initiate trading halts,¹¹ and adjudicate clearly erroneous trade disputes in the after-hours session, using the same standards and methods as employed during traditional market hours.¹²

Nasdaq believes the transparency and investor protection benefits resulting from the availability of Nasdaq's systems and facilities after the traditional trading day have proven their worth and should now become permanent.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,¹³ in general, and with Section 15A(b)(6) of the Act,¹⁴ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, remove impediments to 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

Nasdaq does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

¹¹ Nasdaq notes that this trading halt authority will be limited to individual stocks only and will be undertaken in consultation with other markets operating after 4:00 p.m. Eastern Time. Market-wide trading halt rules currently in effect rely solely on percentage-based declines in the Dow Jones Industrial Average ("DJIA"), which is not calculated after the 4:00 p.m. close. In the event that a circuit breaker halt, triggered during regular market hours, prevents a normal close of U.S. primary markets, there will be no after-hours trading session that day.

¹² As during the pilot period, NASD Regulation, Inc. ("NASD Regulation") is of the view that nothing in the instant proposal modifies or limits an NASD member's obligation to comply with the rules of NASD Regulation's Order Audit Trail System ("OATS") when reporting trading activity taking place between 4:00 p.m. and 6:30 p.m. Eastern Time.

¹³ 15 U.S.C. 78o-3.

¹⁴ 15 U.S.C. 78o-3(b)(6).

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

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁵ and Rule 19b-4(f)(6) thereunder.¹⁶ At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

Nasdaq has requested that the Commission waive the five-day pre-filing notice requirement and the 30-day operative delay. The Commission believes waiving the five-day pre-filing notice requirement and the 30-day operative delay is consistent with the protection of investors and the public interest. Acceleration of the operative date will allow Nasdaq's after-hours trading program to operate without interruption. For these reasons, the Commission designates the proposal to be effective and operative upon filing with the Commission.¹⁷

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal 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

¹⁵ 15 U.S.C. 78s(b)(3)(A).

¹⁶ 17 CFR 240.19b-4(f)(6).

¹⁷ For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to file number SR-NASD-2003-14 and should be submitted by March 4, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁸

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 03-3318 Filed 2-10-03; 8:45 am]

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Securities and Exchange Commission

[Release No. 34-47307; File No. SR-NASD-2002-134]

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Approval to Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 to the Proposed Rule Change Relating to Exemptions from Options Position and Exercise Limits

February 3, 2003.

I. Introduction

On October 1, 2002, the National Association of Securities Dealers, Inc. ("NASD") filed with 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 to amend NASD rule 2860(b)(3)(A) by eliminating options position and exercise limits for positions entered into under certain enumerated hedge strategies and establishing position and exercise limits of five times the standard limit for certain of those strategies when they include an over-the-counter (OTC) option contract. On December 23, 2002, the NASD filed Amendment No. 1 to the proposed rule change.³ The proposed

¹⁸ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See letter from Gary L. Goldsholle, Associate General Counsel, Office of General Counsel, NASD, to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), Commission, dated December 20, 2003 ("Amendment No. 1"). In Amendment No. 1, the

rule change was published for comment in the **Federal Register** on December 30, 2002.⁴ The Commission received no comments on the proposal. This order approves the proposed rule change, and notices and grants accelerated approval to Amendment No. 1 to the proposed rule change.

II. Description of the Proposal

The proposed rule change amends NASD's options position and exercise limits. The proposed rule change establishes six qualified hedge strategies:

1. Where each option contract is "hedged" or "covered" by 100 shares of the underlying⁵ security or securities convertible into the underlying security, or, in the case of an adjusted option, the same number of shares represented by the adjusted contract: (a) Long call and short stock; (b) short call and long stock; (c) long put and long stock; or (d) short put and short stock.

2. *Reverse Conversions*—A long call position accompanied by a short put position, where the long call expires with the short put, and the strike price of the long call and short put is equal, and where each long call and short put position is hedged with 100 shares (or other adjusted number of shares) of the underlying security or securities convertible into such underlying security.

3. *Conversions*—A short call position accompanied by a long put position where the short call expires with the long put, and the strike price of the short call and long put is equal, and where each short call and long put position is hedged with 100 shares (or other adjusted number of shares) of the underlying security or securities convertible into such underlying security.

4. *Collars*—A short call position accompanied by a long put position, where the short call expires with the long put and the strike price of the short call equals or exceeds the strike price of the long put position and where each short call and long put position is hedged with 100 shares (or other adjusted number of shares) of such the underlying security or securities convertible into such underlying

security. Neither side of the short call/long put position can be in-the-money at the time the position is established.

5. *Box Spreads*—A long call position accompanied by a short put position with the same strike price and a short call position accompanied by a long put position with a different strike price.

6. *Back-to-Back Options*—A listed option position hedged on a one-for-one basis with an OTC option position on the same underlying security. The strike price of the listed option position and corresponding OTC option position must be within one strike price interval of each other and no more than one expiration month apart.

Under the proposed rule change, there would be no position and exercise limits when such qualified hedge strategies are effected solely with standardized equity options. In addition, the proposed rule change establishes standardized equity option position and exercise limits of five times the standard limit when one component of such strategies is an OTC option contract. Further, within the list of proposed hedge strategies, NASD proposes that the option component of a reversal, a conversion or a collar position can be treated as one contract rather than as two contracts.

The proposed rule change also modifies the conventional equity options position and exercise limits. First, the proposed rule change expands the hedge exemption for conventional options to include all of the qualified hedge strategies. Second, the proposed rule change increases the conventional equity options position and exercise limits for such qualified hedge strategies to five times the standard limits. Third, the proposed rule change provides that conventional equity options positions under the hedge strategies not be aggregated with other options positions similar to the way that positions under the current equity option hedge exemption and OTC collar aggregation exemption are not aggregated with other options positions.

Under the proposed rule change, the standard position and exercise limits will remain in place for unhedged equity options positions. Once an account reaches the standard limit, positions identified as a qualified hedge strategy would be subject to the increased position limits, or exempted from position limit calculations, as appropriate. The exemption would be automatic (*i.e.*, it will not require pre-approval from NASD) to the extent that a member identifies that a pre-existing qualified strategy is in place or is employed from the point that an account's position reaches the standard

limit and provides the required supporting documentation to NASD.⁶ The exemption would remain in effect to the extent that the exempted position remains intact and NASD is provided with any required supporting documentation.

III. Discussion

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 associations⁷ and, in particular, the requirements of section 15A of the Act⁸ and the rules and regulations thereunder. The Division finds specifically that the proposed rule change is consistent with section 15A(b)(6) of the Act⁹ because it is designed to promote just and equitable principles of trade, and to protect investors and public interest.

Position and exercise limits serve as a regulatory tool designed to address potential manipulative schemes and adverse market impact surrounding the use of options. The NASD proposes to expand the hedge exemption from position and exercise limits. The NASD also proposes to modify the conventional equity options position and exercise limits. The Commission believes it is permissible to expand the current equity hedge exemption without risk of disruption to the options or underlying cash markets. The Commission believes that existing position and exercise limits, procedures for maintaining the exemption, and the reporting requirements imposed by the NASD will help protect against potential manipulation. The Commission notes that the existing standard position and exercise limits will remain in place for unhedged equity option positions. To further ensure against market disruption, the NASD will establish a position and exercise limit equal to no greater than five times the standard limit for those hedge strategies that include an OTC option component.

In addition, according to the NASD, once an account reaches the standard

NASD corrected grammatical errors in the rule language text of the proposed rule change.

⁴ See Securities Exchange Act Release No. 47080 (December 23, 2002), 67 FR 79676 (December 30, 2002).

⁵ NASD represents that the phrase "securities convertible into the underlying security" does not include single stock futures products. Telephone Conversation between Gary L. Goldsholle, Associate General Counsel, Office of General Counsel, NASD and Tim Fox, Law Clerk, Division, Commission on December 6, 2002.

⁶ Under the proposed rule change, the existing reporting procedures that serve to identify and document hedged positions above a certain threshold continue to apply. Paragraph (b)(5) of NASD rule 2860 requires reporting to NASD of aggregate positions of 200 more contracts of the put class and the call class on the same side of the market covering the same underlying security.

⁷ In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁸ 15 U.S.C. 78o-3.

⁹ 15 U.S.C. 78o-3(b)(6).

limit, positions identified as a qualified hedge strategy would be subject to the increased position limits, or exempted from position limit calculations, as appropriate. The exemption would be automatic (*i.e.*, it will not require pre-approval from NASD) to the extent that a member identifies that a pre-existing qualified strategy is in place or is employed from the point that an account's position reaches the standard limit and provides the required supporting documentation to NASD.¹⁰ The exemption would remain in effect to the extent that the exempted position remains intact and NASD is provided with any required supporting documentation.

The Commission notes that it has previously approved changes to similar rules of the options exchanges that eliminated standardized equity option position and exercise limits for certain qualified hedge strategies and established position and exercise limits of five times the standard limit for certain of those strategies when they include an over-the-counter (OTC) option contract.¹¹ The Commission does not believe that the proposed rule changes raises novel regulatory issues that were not already addressed and should benefit NASD members by permitting them greater flexibility in using hedge strategies advantageously, while providing an adequate level of protection against the opportunity for manipulation of these securities and disruption in the underlying market.

The Commission finds good cause for approving Amendment No. 1 to the proposed rule change prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. Amendment No. 1 merely provides technical corrections and clarification to the proposed rule text. The Commission, therefore, believes that granting accelerated approval of Amendment No. 1 is appropriate and consistent with section

15A(b)(6)¹² and section 19(b)¹³ of the Act.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether it 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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR-NASD-2002-134 and should be submitted by March 4, 2003.

V. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹⁴ that the proposed rule change (File No. SR-NASD-2002-134), as amended, be and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03-3319 Filed 2-10-03; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47310; File No. SR-NASD-2003-12]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc., To Extend the Pilot for Limit Order Protection of Securities Priced in Decimals

February 4, 2003.

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 January 31, 2003, the National Association of Securities Dealers, Inc. (“NASD” or “Association”), through its subsidiary, the Nasdaq Stock Market, Inc. (“Nasdaq”), filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by Nasdaq. Nasdaq filed the proposal pursuant to Section 19(b)(3)(A) of the Act,³ and Rule 19b-4(f)(6)⁴ thereunder, which renders the proposal effective upon filing with the Commission. 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

Nasdaq proposes to extend through May 31, 2003, the current pilot price-improvement standards for decimalized securities contained in NASD Interpretative Material 2110-2—Trading Ahead of Customer Limit Order (“Manning Interpretation” or “Interpretation”). Without such an extension these standards would terminate on January 31, 2003. Nasdaq does not propose to make any substantive changes to the pilot; the only change is an extension of the pilot's expiration date through May 31, 2003. Nasdaq requests that the Commission waive both the 5-day notice and 30-day operative requirements contained in Rule 19b-4(f)(6)(iii)⁵ of the Act. If such waivers are granted by the Commission, Nasdaq will implement this rule change immediately.

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 its proposal and discussed any comments it received regarding the proposal. 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.

¹⁰ Under the proposed rule change, the existing reporting procedures that serve to identify and document hedged positions above a certain threshold continue to apply. Paragraph (b)(5) of NASD rule 2860 requires reporting to NASD of aggregate positions of 200 more contracts of the put class and the call class on the same side of the market covering the same underlying security.

¹¹ See Securities Exchange Act Release No. 45603 (March 20, 2002), 67 FR 14751 (March 27, 2002) (CBOE-2000-12); Securities Exchange Act Release No. 45650 (March 26, 2002), 67 FR 15638 (Apr. 2, 2002) (AMEX-2001-71); Securities Exchange Act Release No. 45737 (April 11, 2002), 67 FR 18975 (Apr. 17, 2002) (PCX-2000-45); Securities Exchange Act Release No. 45899 (May 9, 2002), 67 FR 34980 (May 16, 2002) (PHLX-2002-33); and Securities Exchange Act Release No. 46228 (July 18, 2002), 67 FR 48689 (July 25, 2002) (ISE-2002-15).

¹² 15 U.S.C. 78o-3(b)(6).

¹³ 15 U.S.C. 78s(b).

¹⁴ 15 U.S.C. 78s(b)(2).

¹⁵ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).

⁵ 17 CFR 240.19b-4(f)(6)(iii).