

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 will also be available for inspection and copying at the principal office of the Exchange. All submissions should be submitted by February 26, 2004.

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

After careful consideration, 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,⁸ and, in particular, with the requirements of section 6(b) of the Act⁹ and the rules and regulations thereunder. The Commission finds that the proposed rule change is consistent with section 6(b)(4) of the Act,¹⁰ which requires that the rules of the Exchange provide for the equitable allocation of reasonable dues, fees, and other charges among its members and other persons using its facilities. The Commission believes that the extension of the Exchange's Linkage fee pilot program until July 31, 2004 will give the Exchange and the Commission further opportunity to evaluate whether such fees are appropriate.

The Commission finds good cause, pursuant to section 19(b)(2) of the Act,¹¹ for approving the proposed rule change prior to the thirtieth day after the date of publication of the notice of the filing thereof in the **Federal Register**. The Commission believes that granting accelerated approval will preserve the Exchange's existing pilot program for Linkage fees without interruption as the Amex and the Commission further consider the appropriateness of Linkage fees.

V. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹² that the proposed rule change (SR-Amex-2004-

03) is hereby approved on an accelerated basis for a pilot period to expire on July 31, 2004.

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

Jill M. Peterson,

Assistant Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49153; File No. SR-CBOE-2003-50]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the Chicago Board Options Exchange, Inc., Relating to a Pilot Program for Quotation Spreads in Hybrid Classes

January 29, 2004.

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 31, 2003, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange") filed with 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 the Exchange. The CBOE submitted Amendment No. 1 to the proposed rule change on January 7, 2004.³ The CBOE has submitted the proposed rule change under section 19(b)(3)(A) of the Act⁴ and Rule 19b-4(f)(6) thereunder,⁵ which renders the proposal effective upon filing with the Commission.⁶ The Commission is

¹³ 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 Stephen Youhn, CBOE, to Kelly Riley, Senior Special Counsel, Division of Market Regulation, Commission, dated January 6, 2004 ("Amendment No. 1"). In Amendment No. 1, the CBOE proposed to limit its proposed rule change to 200 options classes trading on the CBOE's Hybrid Trading System for a pilot period of six months. In addition, the CBOE agreed to provide the Commission with a pilot program report comparing the Average Quote Width Analysis ("AQWA") scores for each pilot program option prior to the commencement of the pilot with the AQWA scores for each pilot program option during the pilot period. Finally, the CBOE amended Items 7 and 8 of its Form 19b-4 to designate the filing as "non-controversial" pursuant to Rule 19b-4(f)(6) and to indicate that its proposed rule change is substantially similar to an approved pilot program of the International Securities Exchange, Inc.

⁴ 15 U.S.C. 78s(b)(3)(A).

⁵ 17 CFR 240.19b-4(f)(6).

⁶ For purposes of determining the effective date and abrogation date of this filing, the Commission considers January 7, 2004, the date on which the

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

The CBOE proposes to amend CBOE Rule 8.7, "Obligations of Market Makers," to adopt a six-month pilot program through June 29, 2004 that would permit quote spread parameters of up to \$5 on up to 200 option classes traded on the CBOE's Hybrid Trading System ("Hybrid"). The text of the proposed rule change appears below. Proposed new language is *italicized*.

Rule 8.7 Obligations of Market Makers

(a) No change.

(b)

(i)-(iii) No change.

(iv) To price options contracts fairly by, among other things, bidding and/or offering so as to create differences of no more than 0.25 between the bid and offer for each option contract for which the bid is less than \$2, no more than \$0.40 where the bid is at least \$2 but does not exceed \$5, no more than \$0.50 where the bid is more than \$5 but does not exceed \$10, no more than \$0.80 where the bid is more than \$10 but does not exceed \$20, and no more than \$1 where the bid is more than \$20, provided that the appropriate Market Performance Committee may establish differences other than the above for one or more options series. The bid/ask differentials stated above shall not apply to in-the-money series where the underlying securities market is wider than the differentials set forth above. For these series, the bid/ask differential may be as wide as the quotation on the primary market of the underlying security.

(A) *For a six month period expiring on August 5, 2004, the Exchange may designate options on up to two hundred (200) underlying securities that may be quoted with a difference not to exceed \$5 between the bid and offer regardless of the price of the bid. The \$5 quote widths shall only apply to classes trading on the Hybrid system and only following the opening rotation in each security i.e., the widths specified in paragraph (b)(iv) above shall apply during opening rotation.*

CBOE filed Amendment No. 1, to be the filing date of this proposed rule change.

⁸ In approving this rule, the Commission notes that it has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁹ 15 U.S.C. 78f(b).

¹⁰ 15 U.S.C. 78f(b)(4).

¹¹ 15 U.S.C. 78s(b)(2).

¹² *Id.*

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 IV 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

The purpose of the proposed rule change, as amended, is to establish a six-month pilot program to relax the quotation spread requirements on the CBOE for up to 200 option classes traded on Hybrid. Currently, CBOE Rule 8.7(b)(iv) establishes maximum bid-ask differentials (also referred to as quote spread requirements) that vary from \$0.25 to \$1.00, depending upon the price of the option.⁷ The primary purpose of the quote spread requirements is to help to maintain narrow spreads in options. According to the CBOE, these requirements can have the unintended consequence of requiring market makers to quote at prices that are unnecessarily narrow, thereby exposing them to great risk if markets move quickly.

The CBOE believes that given the competitive market making structure of Hybrid and the existence of vigorous inter-market competition, the mandatory quote spread requirements may not be necessary to ensure narrow and competitive spreads in options. In this regard, the CBOE states that the Hybrid market structure creates strong incentives for competing market makers and other market participants to disseminate competitive prices. The Exchange notes that in Hybrid each market maker quotes independently, and customers and broker-dealers can enter limit orders in the limit order book at prices better than those posted by market makers. The Exchange automatically collects this trading interest information, calculates the CBOE best bid and offer, and

disseminates that value to the Options Price Reporting Authority. Accordingly, the CBOE believes that its Hybrid market is competitive, accessible and transparent.

In addition, the CBOE states that market participants in Hybrid have strong incentives to quote competitively. The CBOE allocates incoming orders based on the price and size of orders and quotes resting in the book. Under the CBOE's Ultimate Matching Algorithm ("UMA"), the larger the size of a market maker's quote at the best price, the greater the size of the allocation he or she receives. Conversely, if a market participant does not quote at the best price, the market participant will not participate in any electronic trade allocations. The CBOE believes, moreover, that given NBBO protections in place at each exchange as well as through the Options Market Linkage plan, market participants have even stronger incentives to quote at the best price, lest incoming orders be filled away. Thus, the CBOE believes that inter- and intra-market competitive forces provide strong incentives for market participants to quote competitively and enter quotes and orders that improve the price and depth of the market.

For these reasons, CBOE proposes a pilot program to expand the allowable spread in Hybrid classes to \$5 for up to 200 classes of options traded on Hybrid. The proposed quote spread requirements will apply after the opening trading rotation. During the opening trading rotation, market makers will be required to quote in accordance with the traditional bid-ask width requirements. The \$5 quotation requirements would become operative immediately following the opening rotation. Non-Hybrid classes will remain subject to the current requirements of CBOE Rule 8.7(b)(iv).

During the pilot program, the CBOE will monitor the quotation quality of all classes in the program and, based on the results, recommend either relaxing the spread requirements for all Hybrid classes, ending the pilot, or adjusting the spread requirements for all Hybrid classes. Immediately following the pilot period, the Exchange will prepare and submit to the Commission a report assessing the operation of the program and, in particular, the quality of the quotations for the pilot options.⁸ In this respect, the CBOE commits to provide to the Commission a report analyzing Average Quote Width Analysis ("AQWA") scores for each of the pilot stocks. The Exchange's report will

compare the AQWA scores for each option prior to implementation of the pilot program versus the AQWA scores for each option during the pilot period. The Exchange believes that this information will provide a meaningful comparison during these relevant periods so that the Exchange may determine the effect that \$5 quote widths have on quote quality.

The CBOE notes that the proposed quotation spread requirements are in effect on a pilot basis at the International Securities Exchange, Inc. ("ISE"). Specifically, on March 19, 2003, the Commission approved a six-month pilot program ("ISE Pilot") permitting ISE market makers to expand the allowable spread in their quotations to \$5.⁹ The ISE Pilot applies to options on 50 underlying stocks and expires on January 31, 2004.¹⁰ In September 2003, the ISE requested permanent approval of the ISE Pilot and sought to expand the terms of the ISE Pilot to all ISE-listed equity options.¹¹ The CBOE represents that its proposed pilot program is similar to that of the ISE.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of section 6(b) of the Act.¹² Specifically, the Exchange believes the proposed rule change is consistent with the section 6(b)(5)¹³ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and, in general, to protect investors and the public interest.

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

The CBOE does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange 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.

⁹ See Securities Exchange Act Release No. 47532 (March 19, 2003), 68 FR 14728 (March 26, 2003) (order approving File No. SR-ISE-2001-15).

¹⁰ See Securities Exchange Act Release No. 48514 (September 22, 2003), 68 FR 55685 (September 26, 2003) (notice of filing and immediate effectiveness of File No. SR-ISE-2003-21).

¹¹ See File No. SR-ISE-2003-22.

¹² 15 U.S.C. 78f(b).

¹³ 15 U.S.C. 78f(b)(5).

⁷ The allowable bid-ask differentials are: \$0.25 for options under \$2, \$0.40 for options between \$2 and \$5, \$0.50 for options between \$5 and \$10, \$0.80 for options between \$10 and \$20, and \$1.00 for options above \$20. See CBOE Rule 8.7(b)(iv).

⁸ See Amendment No. 1, *supra* note 3.

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

The CBOE has filed ¹⁴ the proposed rule change pursuant to section 19(b)(3)(A) of the Act ¹⁵ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹⁶ Because the foregoing proposed rule change: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) is not proposed to become operative for 30 days, or such shorter time as the Commission may designate, and the CBOE provided the Commission with written notice of its intent to file the proposed rule change at least five business days prior to the filing date, the proposed rule change has become effective pursuant to section 19(b)(3)(A) of the Act and Rule 19b-4(f)(6) thereunder.

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative prior to 30 days after the date of filing. However, Rule 19b-4(f)(6)(iii) permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The CBOE has requested that the Commission waive the 30-day operative delay to allow the CBOE to implement its pilot program, which is similar to the ISE Pilot, without delay.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest.¹⁷ Specifically, the Commission believes that allowing the CBOE to establish a pilot program that is similar to the ISE Pilot will help the CBOE to compete with the ISE. In addition, the Commission notes that the CBOE's pilot program is substantially similar to the ISE Pilot, which the Commission approved previously on a six-month pilot basis and subsequently extended through January 31, 2004.¹⁸ The Commission believes that the CBOE's proposal raises no new issues or regulatory concerns that the Commission did not consider in approving the ISE Pilot. For these reasons, the Commission designates that the proposal become operative

immediately, with the pilot program to extend through June 29, 2004.

At any time within 60 days of the filing of such proposed rule change,¹⁹ 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.

IV. 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. 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-CBOE-2003-50. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, your 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 will also be available for inspection and copying at the principal office of the CBOE. All submissions should refer to File No. SR-CBOE-2003-50 and should be submitted by February 26 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁰

J. Lynn Taylor,

Assistant Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49150; File No. SR-EMCC-2003-04]

Self-Regulatory Organizations; Emerging Markets Clearing Corporation; Order Approving a Proposed Rule Change Creating an Inactive Member Category

January 29, 2004.

On August 7, 2003, the Emerging Markets Clearing Corporation ("EMCC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ (File No. SR-EMCC-2003-04). Notice of the proposal was published in the **Federal Register** on September 18, 2003.² No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description

The proposed rule change will create a new membership category for inactive members. From time to time, participants find that their activity level in EMCC-cleared instruments does not warrant active membership status and the costs and risks associated with such status. At the same time, however, they are reluctant to terminate their membership because of the amount of time, effort, and cost that would be required to provide EMCC with the membership documents required to regain their membership status should they later choose to take advantage of EMCC's services. To accommodate this need, EMCC proposes to add to its rules a new section for "inactive status" and a new definition for the term "inactive member."³

In order to be eligible to be an inactive member, the participant must have no pending or fail positions and no unpaid money obligations. After a participant requests that it be placed in inactive status, management will act upon its request. Management's decision to grant a participant's request for inactive status will not require approval by EMCC's Membership and Risk Management Committee, but this committee will be notified.

A participant that requests to be placed on inactive status will be entitled to a refund of its clearing fund deposit

¹⁴ See *supra* note 6.

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).

¹⁸ See *supra* notes 8 and 9, and accompanying text.

¹⁹ See *supra* note 6.

²⁰ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 48463 (Sept. 9, 2003), 68 FR 54761.

³ EMCC Rule 2 (Members), sec. 10 (Inactive Status); EMCC Rule 1 (Definitions).