Dated: April 4, 2002.

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–45670; File No. SR–CBOE–2002–08]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Inc. Relating to the Allocation of Orders

March 28, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on February 19, 2002, 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. On March 22, 2002, the CBOE submitted Amendment No. 1 to the proposed rule change.[3] On March 27, 2002, the CBOE submitted Amendment No. 2 to the proposed rule change.[4] The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The CBOE proposes to amend its rules governing the priority of bids and offers and to clarify how orders are to be allocated to market participants on the floor.

Below is the text of the proposed rule change. Deleted language is in brackets. Proposed new language is *italicized*.

Rule 6.45 Priority of Bids and Offers—*Allocation of Trades*

Except as provided by Rules, including but not limited to Rule 6.2A, 6.8, 6.9, Rule 6.47, Rule 6.74, Rule 8.87, and CBOE Regulatory Circulars approved by the SEC concerning Participation Rights, the following rules of priority shall be observed with respect to bids and offers:

(a) Priority of bids.

(*i*) The highest bid shall have priority, but where two or more bids for the same option contract represent the highest price and one such bid is displayed in the customer limit order book in accordance with Rules 7.7 *and 8.85(b)*, such bid shall have priority over any other bid at the post. *If more than one public customer order is represented in the customer limit order book at the best price, priority shall be afforded to such orders in the sequence in which they were received by the Order Book Official (''OBO'') or Designated Primary Market-Maker (''DPM'').*

(ii) The following applies with respect to orders being represented by a Floor Broker, DPM acting as agent under Rule 8.85(b), or OBO, or with respect to bids made in response to a specific request from a Market-Maker. With respect to each of the following, the Floor Broker, DPM, OBO, or Market-Maker shall determine the sequence in which the bids were made.

(*1*) If two or more bids represent the highest price and a bid from the customer limit order book is not involved, priority shall be afforded to such bids in the sequence in which they are made.

(2) If the bids were made at the same time, or in the event the Floor Broker, DPM, OBO, or Market-Maker cannot reasonably determine the sequence in which the bids were made, priority shall be apportioned equally.

(3) If the Floor Broker, DPM, OBO, or Market-Maker cannot reasonably determine the sequence in which the bids were made beyond a certain number of market participants, the Floor Broker, DPM, OBO, or Market-Maker shall provide for the remaining contracts, if any, to be apportioned equally among those market participants who bid at the best price at the time the market was established.

(4) *In the event a market participant declines to accept any portion of the available contracts, any remaining contracts shall be apportioned equally among the other market participants who bid at the best price at the time the market was established until all contracts have been apportioned.*

The Floor Broker, DPM, OBO, or Market-Maker shall determine which market participants responded at the best market at the time the market was established.

(iii) Any contracts remaining in an order, if any, after giving effect to paragraph (ii) above, shall be apportioned equally between any other market participants in the trading crowd who bid at the best price in a reasonably prompt manner subsequent to the time the market was established.

(iv) Whenever a member requests from members of a trading crowd a single bid in excess of the RAES order eligibility size for that option class as provided for in Interpretation .11 to Rule 8.7, each member of the trading crowd shall be apportioned a share of the executed order based on an approximate pro rata percentage, to the extent practicable, of the crowd member's portion of the size of the original single bid. The member requesting the single bid shall determine what constitutes an approximate pro rata percentage of the order that is executed with respect to each member of the trading crowd who participated in making the single bid.

(b) Priority of offers.

The lowest offer shall have priority, but where two or more offers for the same option contract represent the lowest price, priority shall be determined in the same manner as specified in paragraph (a) in the case of bids.

(c) No change

(d) No Change

(e) Exception.

Notwithstanding anything in paragraphs (a) and (b) to the contrary, when a member holding a spread order, a straddle order, or a combination order and bidding or offering in a multiple of the minimum increment on the basis of a total credit or debit for the order has determined that the order may not be executed by a combination of transactions with the bids and offers displayed in the customer limit order book or announced by members in the trading crowd, then the order may be executed as a spread, straddle, or combination at the total credit or debit with one other member without giving priority to bids or offers of members in the trading crowd that are no better than the bids or offers comprising such total debit or credit and bids and offers in the customer limit order book provided at least one leg of the order would trade at a price that is better than the corresponding bid or offer in the book. Under the circumstances described above, a stock-option order, as defined in Rule 1.1(ii)(a), has priority over the bids and offers of members in the trading crowd but not over the bids and offers in the customer limit order book. A stock option order as defined in Rule 1.1(ii)(b), consisting of a combination order with stock, may be executed in accordance with the first sentence in this subparagraph (*e*).

* * * Interpretations and Policies:

.01 No Change

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* letter from Madge M. Hamilton, Attorney, CBOE, to Nancy J. Sanow, Assistant Director, Division of Market Regulation (''Division''), Commission, dated March 22, 2002. The changes made by Amendment No. 1 have been incorporated into this notice.

[4] *See* letter from Madge M. Hamilton, Attorney, CBOE, to Nancy J. Sanow, Assistant Director, Division, Commission, dated March 22, 2002. The changes made by Amendment No. 2 have been incorporated into this notice.

.02 The provisions of this rule are subject to Rule 8.7, Interpretation and Policy .05, and Rule 8.51.

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

CBOE submits the proposed change to CBOE Rule 6.45 pursuant to subparagraph IV.B.j. of the Commission's Order of September 11, 2000,[5] which requires that the options exchanges adopt new, or amend existing, rules to make express any practice or procedure ''whereby market makers trading any particular option class determine by agreement the spreads or option prices at which they will trade any option class, or the allocation of orders in that option class.''

CBOE Rule 6.45 currently requires that the highest bid or lowest offer (''best bid or offer'') shall have priority. CBOE Rule 6.45 also provides that, with limited exceptions set forth in 6.45(c) and (d), an order representing the best bid or offer in the customer limit order book receives priority over another order at the same best price. Proposed CBOE Rule 6.45(a)(i) would add that if more than one public customer order is represented in the customer limit order book at the best price, priority shall be afforded to such orders in the sequence in which they were received by the OBO or DPM.

The Exchange also proposes to adopt CBOE Rule 6.45(a)(ii) to apply to those orders represented by a Floor Broker, a DPM acting as agent under CBOE Rule 8.85(b), or an OBO, or with respect to bids made in response to a specific request from a market maker. In these instances, the proposed rule change provides that the Floor Broker, DPM, OBO, or Market-Maker shall determine which market participants responded at the best market at the time the market was established.[6] Accordingly, this provision provides that the Floor Broker, DPM, OBO, or market maker shall determine the sequence in which bids (offers)[7] were made, subject to the following:

(1) If there are two or more bids (offers) at the best price, and an order in the customer limit order book is not involved, priority is afforded to the orders in the sequence in which they were made. *See* Proposed CBOE Rule 6.45(ii)(1).

(2) If the bids (offers) were made at the same time, or in the event the Floor Broker, DPM, OBO, or market maker cannot reasonably determine the sequence in which the bids (offers) were made, priority shall be apportioned equally. *See* Proposed CBOE Rule 6.45(ii)(2).

(3) If the Floor Broker, DPM, OBO, or market maker cannot reasonably determine the sequence in which the bids (offers) were made beyond a certain number of market participants, the Floor Broker, DPM, OBO, or Market-Maker shall provide for the remaining contracts, if any, to be apportioned equally among those market participants who bid (offered) at the best price at the time the market was established. *See* Proposed CBOE Rule 6.45(ii)(3).

(4) In the event a market participant declines to accept any portion of the available contracts, any remaining contracts shall be apportioned equally among the other market participants who bid (offered) at the best price at the time the market was established until all contracts have been apportioned.[8] *See* Proposed CBOE Rule 6.45(ii)(4).

Proposed CBOE Rule 6.45(iii) provides that any contracts remaining in an order after the operation of CBOE Rule 6.45(ii) shall be apportioned equally between any other market participants in the trading crowd who bid (offered) at the best price in a reasonably prompt manner subsequent to the time the market was established.

Proposed CBOE Rule 6.45(iv) provides that whenever a member requests from members of a trading crowd a single bid in excess of the RAES order eligibility size for that option class as provided for in Interpretation .11 to CBOE Rule 8.7, each member of the trading crowd shall be apportioned a share of the executed order based on an approximate pro rata percentage, to the extent practicable, of the crowd member's portion of the size of the original single bid. The member requesting the single bid shall determine what constitutes an approximate pro rata percentage of the order that is executed with respect to each member of the trading crowd who participated in making the single bid.

The proposed amendment to CBOE Rule 6.45 also identifies all other Exchange Rules that may have bearing on the allocation of an order. These Rules include CBOE Rule 6.2A (''Rapid Opening System''), CBOE Rule 6.8 (''RAES Operations''), CBOE Rule 6.9 (''Solicited Transactions''), CBOE Rule 6.47 (''Priority on Split Price Transactions''), CBOE Rule 6.74 (''Crossing Orders'') and CBOE Rule 8.87 (''Participation Entitlement of DPMs''), as well as CBOE Regulatory Circulars approved by the Commission concerning participation rights.[9]

Finally, the Exchange proposes to add Interpretation and Policy .02 to CBOE Rule 6.45. This interpretation will clarify that the provisions of CBOE Rule 6.45 are subject to the operation of CBOE Rules 8.7, Interpretation and Policy .05, and CBOE Rule 8.51.

2. Statutory Basis

The proposed rule change provides comprehensive information concerning the priority of trades, which furthers the objectives of section 6(b)(5) of the Act[10]

[5] 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).

[6] The Exchange has represented that it has the ability to determine the identity of the individual who allocated a trade executed on the Exchange. Telephone conversation between Madge Hamilton, Attorney, the CBOE, and Ira Brandriss, Special Counsel, Division, Commission, on March 21, 2002.

[7] Paragraph (b) of this Rule 6.45 provides generally that in cases where two or more offers represent the lowest price, priority is determined in the same manner as specified in paragraph (a) in the case of bids.

[8] In this respect, the Exchange notes that the number of contracts the DPM may receive if a participant declines to accept an allocation (''unallocated portion'') is still capped by the DPM participation entitlement amount (i.e., 30%, 40%, or 50%) unless the other participants decline to accept any of the unallocated portion. For example, if there is an order in which it has been determined that market makers A, B, C, and D are entitled to receive an allocation along with the DPM, the order would be allocated as follows: 30% to DPM and 17.5% each to A, B, C, and D. If D declines to receive an allocation, D's portion would be allocated evenly among A, B, and C. The DPM would not be entitled to receive any portion of D's allocation because it would result in an allocation to the DPM in excess of the 30% participation entitlement. If, however, A, B, and C decline to accept any of D's unallocated contracts, the DPM could then take those additional contracts.

[9] The current participation rights of DPMs under CBOE rules are detailed in CBOE Regulatory Circular RG 00–193, dated December 28, 2000. *See* Securities Exchange Act Release No. 43750 (December 20, 2000), 65 FR 82420 (December 28, 2000).

[10] 15 U.S.C. 78(b)(5).

to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and to protect investors and the public interest.

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

The Exchange does not believe that the proposed rule change will 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 Exchange has neither solicited nor received written comments on the proposed rule change.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

(A) by order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the CBOE. All submissions should refer to file number SR–CBOE–2002–08 and should be submitted by April 29, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[11]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–8367 Filed 4–5–02; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–45671; File No. SR–NASD–2002–01]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. Relating to the Automatic Refreshing of Quotations in Nasdaq's SuperMontage System and the Withdrawal of Market Makers That Fail To Maintain a Clearing Relationship

March 28, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on January 3, 2002, 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, II and III below, which Items have been prepared by Nasdaq. Nasdaq submitted Amendment No. 1 on March 5, 2002.[3] The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

Nasdaq proposes to amend NASD Rules 4710(b)(5) and 4619(c) to modify the procedures for refreshing exhausted market maker quotes in, and withdrawing market makers that fail to maintain proper clearing arrangements from, Nasdaq's future Order Display and Collector Facility (collectively referred to as the Nasdaq National Market System ''NNMS'' or ''SuperMontage''). Below is the text of the proposed rule change. Proposed new language is in *italics;* proposed deletions are in [brackets].

* * * * *

4710. Participant Obligations in NNMS

(a) through (b)(4) No Change.

(5) If an NNMS Market Maker's Attributable Quote/Order is reduced to zero on one side of the market due to NNMS executions, the NNMS will close the Market Maker's quote in the NNMS [with respect to both sides of its market] *on that side of the market,* and the NNMS Market Maker will be permitted a grace period of [three minutes] *30 seconds* within which to take action to restore its Attributable Quote/Order if the market maker has not authorized use of the QR functionality or does not otherwise have an Attributable Quote/Order on that side[s] of the market in the system. An NNMS Market Maker that fails to transmit an Attributable Quote/Order in a security within the allotted time will have [its] the *exhausted side of its* quotation restored by the system at *a price $0.01 inferior* to the lowest displayed bid price [and] *or* the highest displayed offer price in that security *as appropriate. If all bids and/or offers are exhausted so that there are no longer any Quote/Orders displayed on the bid and/or offer side of the market, the system will refresh a market maker's exhausted bid or offer quote to a normal unit of trading priced $0.01 inferior to the lesser of either: (a) The last valid displayed inside bid/offer in the security before all such bids/offers were exhausted; or b) the market maker's last displayed bid/offer before exhaustion. If the resulting bid/offer quote would create a locked or crossed market, NNMS will instead re-open the exhausted market maker's bid/offer quote at a price $0.01 inferior to the unexhausted inside bid/offer in that security. If at any time this automatic quote restoration process would result in the creation of a bid/offer of less than $0.01, the system will refresh that bid/offer to a price of $0.01.* Except as provided in subparagraph (b)(6) of this rule, an NNMS Market Maker that withdraws from a security may not re-register in the system as a market maker in that security for twenty (20) business days. The requirements of this subparagraph shall not apply to a market maker's Agency Quote.

(6) through (10) No Change.

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[11] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Letter from Thomas P. Moran, Associate General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission, dated March 4, 2002 (''Amendment No. 1''). In Amendment No. 1, Nasdaq modified its filing, as originally-proposed, by removing the words ''at least'' from each reference to the phrases ''at least $0.01 inferior'' and ''at least one penny inferior'' in both Nasdaq's proposed amendments to NASD Rule 4710(b)(5) and the text of Nasdaq's Form 19b–4.