

proposed rule change was published for comment in the **Federal Register** on June 1, 2001.⁶ The Commission received no comments on the proposal. This order approves the proposal. The portion of the proposed rule change establishing the trading permits is approved on a pilot basis for a minimum of two years and a maximum of four years, in the event that the Exchange's Seat Fund Committee exercises its authority to renew the permits for an additional two years.

II. Description of the Proposal

The Amex proposes to increase by 25 the number of regular memberships and create 25 two-year permits as a result of a Regular Seat and Two-Year Permit Offering Plan (the "Plan"). The seats and the permits would be allocated as determined by the Exchange's Seat Fund Committee ("Committee"). The Committee would determine the sale price for regular seats would be at least \$600,000. The price for two-year permits would be at least \$14,000, per month.

The Committee would be able to renew the two-year permits once for an additional two years, but the permits would be non-transferable. A two-year permit would terminate if the holder went out of business. Any regular seats offered but not sold would be permitted to be converted into two-year permits as determined by the Committee.⁷ The two-year permits would have no distribution or voting rights.

All prospective seat and/or permit holders would be required to be approved by the Exchange prior to the sale of a seat or the transfer of a permit by the Exchange. The Exchange would receive a \$750 administrative fee for each seat/permit for administering the sale/transfer for prospective seat/permit owners.

Prior to any seat sale or permit transfer by the Exchange, a non-member or a person/organization that was not currently the owner of a regular membership would be required to meet all requirements currently applicable to regular or two-year permit holders. If the purchaser of a seat intended to lease the seat pursuant to a special transfer agreement or transfer the seat to a nominee, the lessee or nominee would also be required to meet all Exchange requirements. All applicable fees due by persons/organizations that are not owners of regular memberships or

members of the Exchange would be required to be paid before the sale of any seat or transfer of any permit.

Sale proceeds will be distributed to all seat owners at a date to be determined by the Committee. The Ex-date for determining distribution of sale proceeds to owners would be the date of approval of the Plan by the Commission.

III. Discussion

The Commission finds that 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.⁸ Specifically, the Commission finds that the proposed rule change is consistent with section 6(b)(5) of the Act,⁹ in that it is designed to remove impediments to and perfect the mechanism of a free and open market.¹⁰

The Commission believes that the proposed rule change will remove impediments to and perfect the mechanism of a free and open market by enhancing the depth and liquidity of the Amex floor by bringing additional capital and market participants to the Amex, which should attract more order flow. In addition, the Commission believes that the proposed rule change will enable the Exchange to better handle increased volume on the Exchange. The Commission believes that increasing the number of seats and providing a limited number of trading permits should enable Exchange members to afford customers an optimal level of service. The Commission notes that there are currently 864 Amex seat holders that have the ability to trade securities pursuant to the Exchange's equity trading rules and approximately 300 equity seat holders.¹¹ These traders are fully represented on the Exchange's Board and key committees. The Commission specifically notes that the proposed trading permits are limited in duration to a maximum of four years and constitute a *de minimis* number in relation to regular members that trade equities.¹² The Commission also notes

⁸ 15 U.S.C. 78f(b).

⁹ 15 U.S.C. 78f(b)(5).

¹⁰ In approving this rule change, the Commission has considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹¹ Options seat holders are permitted to trade exchange traded funds, which trade pursuant to the Exchange's equity rules.

¹² The Act requires an Exchange to "assure a fair representation of its members in the selection of its directors and administration of its affairs. . . ." See section 6(b)(3) of the Act, 15 U.S.C. 78f(b)(3). This requirement serves to ensure that an exchange is administered in a way that is equitable to all those who trade on the exchange. If the trading permits

that a majority of the Exchange's regular and options principal members voted in favor of the proposed rule change.

IV. Conclusion

It is Therefore Ordered, pursuant to section 19(b)(2) of the Act,¹³ that the proposed rule change (SR-Amex-2001-17) is approved. The portion of the proposed rule change establishing trading permits is approved on a pilot basis for a minimum of two years and a maximum of four years.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁴

Margaret H. McFarland.

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-45128; File No. SR-ISE-2001-31]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change by the International Securities Exchange LLC and Amendment No. 1 Thereto Relating to Payment for Order Flow Fees

December 4, 2001.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on November 16, 2001, the International Security Exchange LLC (the "Exchange" or the "ISE") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which the ISE has prepared. On November 28, 2001, the ISE submitted Amendment No. 1 to the proposed rule change. The Commission is publishing this notice to solicit comments from interested persons on the proposed rule change, as amended.

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

The ISE is proposing to establish a ceiling of \$750,000 in each of the ten payment-for-order-flow funds that the ISE maintains. The text of the proposed

had an unlimited term or more than a *de minimis* number of trading permits were being issued, the permit holders would be entitled to fair representation.

¹³ 15 U.S.C. 78s(b)(2).

¹⁴ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

⁶ Securities Exchange Act Release No. 44341 (May 23, 2001), 66 FR 29848.

⁷ Consequently, if the Exchange did not sell any of the authorized seats, a maximum of 25 additional trading permits could be authorized, for a total of 50.

rule change is available at the ISE and the Commission.

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 ISE 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 ISE 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

Under ISE Rule 802(b), the ISE has divided the options it trades into 10 groups, with one Primary Market Maker ("PMM") assigned to each group. The ISE maintains a payment-for-order-flow fund for each group, consisting of the fees collected from market makers trading options in that group. The PMM for the group is responsible for arranging and making all payments to Electronic Access Members for order flow sent to the ISE in options in that Group.

The purpose of the proposed rule change is to establish a ceiling of \$750,000 in each of the ten payment-for-order-flow funds that the ISE maintains. To date, the ISE has been paying out of these funds less money than has been collected, thus building a balance in the individual funds. The ISE believes that capping each fund at \$750,000 will provide sufficient money for PMMs to maintain the payment-for-order-flow program while lessening the economic burden on market makers to continue to pay payment-for-order-flow fees. The funds for most of the ten groups of options either currently are at, or the ISE anticipates soon will reach, the \$750,000 level. Once a fund reaches this level, market makers trading options in that group will pay the payment-for-order-flow fee only when the imposition of such fee is necessary to replenish the fund to the \$750,000 level.

The ISE will implement the rule change so that market makers economically will not pay the payment-

for-order-flow fee whenever the fund for a particular group reaches \$750,000. In this regard, the ISE anticipates that soon all the group funds will reach this level. From that time forward, market makers will pay this fee only to the extent necessary to replenish a fund after the ISE makes its monthly payments to order flow providers. To the extent that collections exceed payments in a given month, market makers in a group will be responsible for the payment-for-order-flow fee only for that portion of the month necessary to return the fund to the \$750,000 level.

The ISE will implement this process by working both with individual market makers and their clearing firms, who handle the payment of fees for their market maker clients. This could result in more than one operational process to implement this fee cap. For example, the ISE could cease charging the fee on the day that a fund reaches \$750,000; alternatively, the ISE could continue to impose the fee for the entire month and then credit members for excess payments in their monthly bill. The ISE may adopt one or more of these processes (or a similar process) depending on the particular needs and practices of its market makers and clearing firms.

2. Basis

The ISE states that the basis for the proposed rule change is the requirement under Section 6(b)(4) of the Act³ that an exchange have an equitable allocation of reasonable dues, fees, and other charges among its members and other persons using its facilities.

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

The ISE believes that the 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 parties.

³ 15 U.S.C. 78f(b)(4).

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

The foregoing rule change, which establishes or changes a due, fee, or other charge applicable to members of the Exchange, has become effective pursuant to section 19(b)(3)(A) of the Act⁴ and Rule 19b-4(f)(2) thereunder.⁵ At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate the 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 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 the filing will also be available for inspection and copying at the principal office of the ISE. All submissions should refer to SR-ISE-2001-31 and should be submitted by January 2, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,
Deputy Secretary.

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⁴ 15 U.S.C. 78s(b)(3)(A).

⁵ 17 CFR 240.19b-4(f)(2).

⁶ 17 CFR 200.30-3(a)(12).