Commission believes that permitting the Exchange to establish trading differentials for option contracts upon the filing of a proposal under Section 19(b)(3)(A) of the Act will provide flexibility to the Exchange and thereby enhance the quality of the market for affected Amex-listed options. Allowing the Amex to quote in finer increments will facilitate quote competition. This should help produce more accurate pricing of options and should result in tighter quotations. Furthermore, if the quoted markets are improved by reducing the minimum increment, the change could result in added benefits to the markets such as reduced transaction costs.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[7] that the proposed rule change (SR–Amex–97–41) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[8]

Margaret H. McFarland,

Deputy Secretary.

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minimum increment to 1⁄16th for NYSE-listed equity securities).

[7] 15 U.S.C. 78s(b)(2).

[8] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39730; File No. SR–BSE–97–09]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the Boston Stock Exchange, Inc. Relating to its Specialist Performance Evaluation Program

March 6, 1998.

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 December 17, 1997, the Boston Stock Exchange, Inc. (''BSE'' or ''Exchange'') 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 the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and to grant accelerated approval to the proposed rule change.

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

The Exchange seeks to amend its specialist performance evaluation program (''SPEP'') pilot with the addition of several objective measures, the deletion of the floor broker questionnaire, a change from using trade statistics to using share statistics for the price improvement and depth measures, a readjusted point system, readjusted threshold levels and/or weights for all of the measures, and a change in the review period for the program from tri-annual to quarterly. The proposed pilot program is intended to expire on December 31, 1998.[3]

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 self-regulatory organization 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 III below. The self-regulatory organization 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

Since the inception of the pilot program in February 1993, the Exchange has continuously reviewed and fine-tuned the SPEP to ensure that its specialists are providing competitive and quality executions. In addition to looking for new objective measures of performance, the Exchange has periodically changed the threshold levels and weights of the existing measures. After an extensive review of overall Exchange performance in the areas of price improvement and depth, areas which the Exchange's Market Performance Committee and Board of Governors has determined are critical to market quality, the Exchange is proposing to measure price improvement in three categories covering all market spreads (the current program focuses only on greater than eighth spreads) and to heavily weight both the price improvement and depth measures.

As occurs under the current program, only regular way, unconditioned buy and sell market and marketable limit orders will qualify for inclusion in the program, blocks of time will be excluded from the program in the event of trading halts and system problems which impact the validity of quotes; orders will be eligible for measurement only if received after the primary market opens the stock; stocks subject to competition will be included in the program; the same staff and committee review time frames and available actions will apply; and quarterly results will continue to be used in allocating stocks.

The Exchange seeks to change the review periods from tri-annual to quarterly, with each period beginning January, April, July, and October. The Exchange believes that these shortened review periods will permit a more frequent review process and a faster response to evident performance, as well as enable specialists to address potential low performance areas more efficiently.

Turnaround Time, which measures the average number of seconds from the receipt of an order for 1299 shares or less in BEACON until it is executed (in whole or in part), stopped or canceled, will remain unchanged. Holding Orders Without Action, which measures the percentage of orders (all order sizes included) which are neither executed (in whole or in part), stopped nor canceled within twenty-five seconds,

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

[2] 17 CFR 240.19b–4.

[3] The Commission initially approved the BSE's SPEP pilot program in Securities Exchange Act Release No. 22993 (March 10, 1986), 51 FR 8298 (March 14, 1986) (File No. SR–BSE–84–04). The Commission subsequently extended the pilot program in Securities Exchange Act Release Nos. 26162 (October 6, 1988), 53 FR 40301 (October 14, 1988) (File No. SR–BSE–87–06); 27656 (January 30, 1990), 55 FR 4296 (February 7, 1990) (File No. SR–BSE–90–01); 28919 (February 26, 1991), 56 FR 9990 (March 8, 1991) (File No. SR–BSE–91–01); and 30401 (February 24, 1992), 57 FR 7413 (March 2, 1992) (File No. SR–BSE–92–01). The BSE was permitted to incorporate objective measures of specialist performance into its pilot program in Securities Exchange Act Release No. 31890 (February 19, 1993), 58 FR 11647 (February 26, 1993) (File No. SR–BSE–92–04) (''February 1993 Approval Order''), at which point the initial pilot program ceased to exist as a separate program. The current pilot program was subsequently extended in Securities Exchange Act Release Nos. 33341 (December 15, 1993), 58 FR 67875 (December 22, 1993) (''December 1993 Approval Order''); 35187 (December 30, 1994), 60 FR 2406 (January 9, 1995); 36668 (January 2, 1996), 61 FR 672 (January 9, 1996) (January 1996 Approval Order) (Pilot extended until December 31, 1996); and 38128 (January 17, 1997), FR (January, 1997) (Pilot extended until December 31, 1997).

will also remain unchanged. However, the point system and weights for these two measures will be modified as described below.

The existing Trading Between the Quote measure is being replaced by three separate price improvement measures. Each of these categories will measure the percentage of shares [4] executed at a price better than the displayed national best bid or offer (''NBBO'') price at the time the order is received. A separate category of orders will be measures for less than one-eighth spreads, one-eighth spreads, and greater than one-eighth spreads. Qualification in a category will be based on the spread at the time the order is received.

The existing Executions in Size Greater than the Best Bid and Offer (''BBO'') is being renamed as ''Depth'' and modified to measure shares rather than trades. This calculation will measure the percentage of shares exceeding the displayed NBBO size which are executed at or better than the displayed NBBO price.[5] Only orders which at the time of receipt exceed the displayed NBBO size will qualify for this measure. An additional depth measure is being added to the program, called ''Added Depth,'' which will measure the number of shares executed by each specialist at the displayed NBBO price in excess of the displayed NBBO size at the time the order is received, as a percentage of the total number of shares executed by all specialists at the displayed NBBO price in excess of the displayed NBBO price.[6] This measure will also include only those orders that exceed the displayed NBBO at the time of receipt of the order, and will provide the raw score percentage attributable to each specialist relative to all other specialists being evaluated.

The Specialist Performance Evaluation Questionnaire (''SPEQ''), which has been a part of the Exchange's performance evaluation program since 1984, is being eliminated. For some time now, it has been the Market Performance Committee's and BSE staff's view that the Questionnaire is too subjective to have any meaningful value in the overall performance of a specialist. Over time, its weight has been significantly reduced in the overall evaluation program. The Committee intends to redevelop the questionnaire and reintroduce it at some point in the future, possibly as a tool to aid the Committee in effectively assessing the performance of specialists required to appear as a result of deficient performance in the objective measures and overall program.

The current ten point scale that is applied to the raw scores for each measure is also being changed in an effort to better differentiate among scores. Ranges of scores will be given points of either 0, 5, 10, 15 or 20 points, with 5 points being at the threshold level for each measure. Specialists who fall below the threshold level will receive 0 points, whereas under the current scale can be given for unacceptable performance. The Exchange believes that these changes will provide an incentive to specialists to improve lower levels of performance and will reward those specialists who are significantly outperforming their peers.

The proposed range point scales for each of the measures is as follows:

1. TURNAROUND TIME

Time in seconds	Points
>=21.0	0
16.0–20.9	5
11.0–15.9	10
0–10.9	15

2. HOLDING ORDERS WITHOUT ACTION

Percentage of orders	Points
>=21.0	0
16.0–20.9	5
11.0–15.9	10
6.0–10.9	15
0–5.9	20

3. PRICE IMPROVEMENT (<⅛ SPREADS)

Percentage of orders	Points
<2.0	0
2.0–3.9	5
4.0–5.9	10
6.0–9.9	15
>=10.0	20

4. PRICE IMPROVEMENT (⅛ SPREADS)

Percentage of orders	Points
<15.0	0
15.0–19.9	5
20.0–24.9	10
25.0–29.9	15
>=30.0	20

5. PRICE IMPROVEMENT (>⅛ SPREADS)

Percentage of orders	Points
<25.0	0
25.0–34.9	5
35.0–39.9	10
40.0–44.9	15
>=45.0	20

6. DEPTH

Percentage of orders	Points
<75.0	0
75.0–79.9	5
80.0–84.9	10
85.0–89.9	15
>=90.0	20

7. ADDED DEPTH

Percentage of orders	Points
<1.0	0
1.0–1.9	5
2.0–3.9	10
4.0–5.9	15
>=6.0	20

The following minimum threshold levels have been set, at which a Specialist will be deemed to have adequately performed:

Overall Program—at or above weighted score of 5.00

Turnaround Time—below 21.0 seconds (5 points)

Holding Orders Without Action—below 21.0% (5 points)

[4] The Commission notes that the current Trading Between the Quote criterion measures a specialist's performance in terms of trades, not shares.

[5] For example, assume the NBBO size is 500 shares displayed and the BSE specialist receives an order for 1200 shares. Under the current test, if the specialist executed 700 shares at the NBBO price, he would effectively receive credit for executing the whole order at the NBBO or better even though part of the order may have been executed at a price inferior to the NBBO. (He would receive credit for 1 trade out of 1 trade, or 100%). Under the proposed revised test, measured in terms of shares versus trades, if the specialist executed 600 shares at the NBBO price, the specialist would receive credit for 600 shares out of 1200 shares, or 50%. If the specialist executed 900 shares at the NBBO price, he would receive credit for 900 out of 1200, or 75%.

[6] For example assume the NBBO size is 500 shares displayed and the BSE specialist receives an order for 1200 shares, and that the specialist executes 600 shares at the displayed NBBO price. Calculate how many shares over the NBBO size the specialist executed by subtracting 500 from 600; the specialist has 100 shares of ''added depth.'' Then calculate the added depth for each qualifying order for each specialist, add the added depth for each specialist for each qualifying order, and total the added depth for all specialists combined. Next, you compare each specialist's added depth to the overall added depth for the floor to arrive at the percentage for each specialist relative to the other specialists. For example: 100 added depth for specialist A ÷ 10,000 added depth for all specialists = 10% added depth for specialist A.

Price Improvement (<⅛—at or above 2.0% (5 points)
Price Improvement (⅛)—at or above 15.0% (5 points)
Price Improvement (>⅛—at or above 25.0% (5 points)
Depth—at or above 75.0% (5 points)
Added Depth—at or above 1.0% (5 points)

Assuming that a specialist performed at the above minimum threshold levels for each measure, the breakdown of weighted points would be as follows:

Measure	Weight (percent)	Points	Weighted points
Turnaround Time	5	5	0.25
Holding Orders Without Action	5	5	0.25
Price Improvement (<⅛)	20	5	1.00
Price Improvement (⅛)	15	5	0.75
Price Improvement (>⅛)	15	5	0.75
Depth	20	5	1.00
Added Depth	20	5	1.00
Overall Weighted Score			5.00

The Exchange is requesting accelerated approval of the proposed rule change pursuant to Section 19(b)(2) of the Act. The Exchange believes that such action is appropriate in that the existing Specialist Performance Evaluation Program's heavily weighted objective measure regarding price improvement in greater than one-eighth markets has become obsolete as the sole determinant of price improvement statistics. That category alone accounts for only ten percent of the Exchange's overall trade volume. The Exchange also believes that the current program's use of trade data is less effective than using share data will be because share data will present a better overall picture of execution quality. In addition, the Exchange believes that the proposed changes will create a more meaningful and effective overall program for evaluating its specialists, with the heavily weighted market quality measures for price improvement and depth. Finally, the Exchange seeks to implement this amended program as soon as possible and has informed its specialists that such changes have been proposed to the Commission for approval on an accelerated basis, and has begun making the system programming changes necessary to accumulate, calculate and store statistics for the program.

2. Statutory Basis

The Exchange believes that the statutory basis for the proposed rule change is Section 6(b)(5) of the Act,[7] in that it is designed 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; and is not designed to permit unfair discrimination between customers, issuers, brokers and dealers.

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.

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

No written comments were either solicited or received.

III. 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. 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 Exchange. All submissions should refer to File No. SR–BSE–97–09 and should be submitted by April 6, 1998.

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

For the reasons discussed below, the Commission finds that the BSE's proposal to extend the revised SPEP pilot program until December 31, 1998 is consistent with the requirements of Sections 6 and 11 of the Act and the rules and regulations thereunder applicable to a national securities exchange. Specifically, the Commission finds that the proposed rule change is consistent with the Section 6(b)(5)[8] requirement that the rules of the Exchange be designed 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, in general, to protect investors and the public interest.

Further, the Commission finds that the proposal is consistent with Section 11(b) of the Act[9] and Rule 11b–1 thereunder[10] which allow securities exchanges to promulgate rules relating to specialists in order to maintain fair and orderly markets and to remove impediments to and perfect the mechanism of a national market system.

The Commission believes that specialists play a crucial role in providing stability, liquidity, and continuity to the trading of stocks. Among the obligations imposed upon specialists by the Exchange, and by the Act and the rules promulgated thereunder, is the maintenance of fair and orderly markets in their designated securities.[11] To ensure that specialists fulfill these obligations, it is important that the Exchange conduct effective

[7] 15 USC. 78f(b)–(5).

[8] 15 U.S.C. 78f(b)(5).

[9] 15 U.S.C. 78k(b).

[10] 17 CFR 240.11b–1.

[11] Rule 11b–1, 17 CFR 240.11b–1; BSE Rules Ch. XV, ¶ 2155.01.

oversight of their performance. The BSE's SPEP is critical to this oversight.

The Commission believes that the Exchange's development of two new objective criteria, Price Improvement and Added Depth, is a positive step forward in establishing meaningful objective specialist performance criteria. These new objective measures are designed to measure market quality in two important areas of specialist performance, price improvement and depth. By replacing Trading Between the Quote with Price Improvement, the amount of time the specialist executes orders at a price better than the NBBO [12] will be measured in three categories covering all market spreads, rather than just in greater than ⅛th markets. The Added Depth measure will allow BSE to measure in percentage terms, how often a specialist executes an order at a size greater than the NBBO size, at the NBBO price, relative to all the other specialists. In addition, the Commission believes it is reasonable to measure Price Improvement and Depth and Added Depth in terms of shares executed, rather than trades, because it should give a better picture of a specialist's execution quality by giving specialists credit for the number of shares in a trade actually executed above the NBBO size at the NBBO price, rather than for an entire trade where the specialist may have only executed part of the trade at or better than the NBBO price.[13]

The Commission believes it is reasonable under the Act to amend the point system for all of the objective measures of specialist performance. The Commission believes that the revised test, where specialists who fall below the adequate threshold levels will not receive any points, as compared to the current scale where points are still awarded for performance below the adequate threshold level, should provide an added incentive to specialists to receive partial credit for unacceptable performance. Regarding BSE's proposed reliance on share statistics (versus trade statistics), the Commission believes that the threshold levels set for each objective measure are reasonable. The Commission nevertheless reiterates its previous request that BSE continually monitor the adequate threshold levels and propose adjustments as necessary. The Commission also believes that the change in the weighting of each objective measure is reasonable, in that the Price Improvement and depth measures, which measure market quality and liquidity, are more highly weighted than Turnaround Time and Holding Orders Without Action, which have been reduced to 10% combined weight. The Commission believes it is reasonable for BSE to eliminate the current SPEQ, a subjective measure of specialist performance, particularly given the breadth of the proposed performance measures, which rely on objective criteria. The Commission also believes it is consistent with the Act to allow the Exchange to review the specialist performance quarterly, rather than tri-annually. By allowing for more frequent review of specialist performance, BSE should be able to respond more rapidly and efficiently in order to identify deficient performance by specialists.

Extending the pilot program until December 31, 1998 will allow the Exchange to gain experience in administering the new specialist performance program and provide sufficient time for BSE to respond to the Commission's continuing concerns about the SPEP. In particular, the Commission expects the BSE to incorporate additional objective criteria into the SPEP, most importantly, a measure of quote performance [14] The Commission recently observed, in its study on the practice of preferencing, that BSE specialists' quotes are only equal to the NBBO a very low percentage of the time.[15] In response to a request from the Division of Market Regulation to address the issue of measuring specialist quote performance, BSE has stated that it is currently developing the technological means to evaluate quote performance and will submit a rule amendment in September 1998 modifying its SPEP to include an objective measure of quote performance.[16]

During the next year of the pilot's operation, BSE should continue to assess whether each SPEP measure is assigned an appropriate weight.[17] In addition, the Commission expects the Exchange to continue to conduct an on-going examination of its minimum adequate performance thresholds, in order to ensure that they continue to be set at appropriate levels.[18] The Commission notes its continued belief that relative performance rankings that subject the bottom 10% of all specialist units to review by an Exchange committee are important part of an effective evaluation program. The BSE should continue to closely monitor the conditions for review and should take steps to ensure that all specialists whose performance is deficient and/or diverges widely from the best units will be subject to meaningful review. In the Commission's opinion, a meaningful review process would ensure that adequate corrective actions are taken with respect to each deficient specialist.[19] The Commission would have difficulty granting permanent approval to a SPEP that did not include a satisfactory response to the concerns described above.

The Commission therefore requests that the BSE submit a report to the

[12] In Trading Between the Quote, the performance was measured against BSE's BBO rather than the NBBO.

[13] *See supra* example note 5. In that example, under the current regime, a specialist who executed 600 out of the 1200 shares would receive the same credit as one who executes 800 out of 1200. However, under the proposed rule change, the specialist who executed 800 shares would receive a higher score than the one who executes 600 shares.

[14] For example, the BSE could develop additional measures of market depth, such as how often the specialist's quote exceeds 500 shares or how often the BSE quote, in size, is larger than the NBBO (excluding quotes for 100 shares). Another possible objective criteria could measure quote performance; how often the BSE specialist's quote, in price, is alone at or the same as the NBBO. *See* January 1996 Approval Order.

[15] *See* Report on the Practice of Preferencing Pursuant to Section 510(c) of the National Securities Markets Improvement Act of 1996, Commission, April 11, 1997 at Table V–5 (BSE specialists' quotes are equal to the NBBO approximately only 5% of the time).

[16] *See* letter from Karen A. Aluise, Vice President, BSE, to Howard Kramer, Associate Director, Market Regulation, Commission, dated February 13, 1998.

[17] The Commission had recommended in its January 1996 Approval Order that the BSE consider either having only one measure out of the Turnaround Time and Holding Orders Without Action categories or reducing the weights of these existing measures, which together accounted for 30% of the current SPEP, given the substantial overlap between those two measures. In response to this recommendation, the BSE first reduced the weights of two measures to 25% of the overall program, and decreased the weight of the SPEQ to 5% and increasing the weight of each of the other objective criteria from 25% to 35%. *See* August 1996 Release. In addition, the current proposed rule change further reduces the weights of the two measures to 5% each.

[18] In August 1996, in response to this same recommendation the BSE some of the minimum adequate performance levels to provide a higher benchmark for acceptable specialist performance on the Exchange. *See* August 1996 Release.

In the current proposed rule change, BSE has further amended the performance level of price improvement (which replaces Trading Between the Quote) and the two depth measures by slightly lowering them, to reflect the change from measuring performance in terms of trades to shares.

[19] In response to these comments, the BSE previously revised its review process by tightening the standards for committee review for substandard specialist performance both in the overall program and in individual measures. The criteria for PIAC review for substandard performance in any one objective measure was reduced from two out of three consecutive review periods to any one review period. The crieteria for MPC review of substandard performance in any one objective measure was reduced from three out of four consecutive review periods to two out of three consecutive review periods, while MPC review for substandard overall performance was reduced from two out of three consecutive review periods to any one review period. *See* August 1996 Release.

Commission, by September 17, 1998, describing its experience with the pilot. At a minimum, this report should contain data, for the last review period of 1997 and the first two review periods of 1998, on (1) the number of specialists who fell below acceptable levels of performances for each objective measure, [20] the questionnaire (for the last review period of 1997) and the overall program, and the specific measures in which each such specialist was deficient; (2) the number of specialists who, as a result of the objective measures, appeared before the PIAC for informal counseling; (3) the number of such specialists then referred to the MPC and the type of action taken; (4) the number of specialists who, as a result of the overall program, appeared before the MPC and the type of action taken; (5) the number of specialists who, as a result of the questionnaire (for the last review period of 1997) or falling in the bottom 10% were referred by the Exchange staff to the PIAC and the type of action taken (this should include the number of specialists then referred to the MPC and the type of action taken by that Committee); and (6) a list of stocks reallocated due to substandard performance and the particular unit involved. The report also should discuss the specific action taken by the BSE to develop additional objective measures and address the other concerns noted above. Any requests to modify this pilot, to extend its effectiveness or to seek permanent approval for the SPEP should be submitted to the Commission by September 17, 1998, as a proposed rule change pursuant to Section 19(b) of the Act.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. This will permit the pilot program to continue and allow the BSE time to consider improvements to its program. In addition, the rule change that implemented the pilot program was published in the **Federal Register** for the full comment period, and no comments were received.[21] Accordingly, the Commission believes that it is consistent with the Act to accelerate approval of the proposed rule change.

It is therefore ordered, pursuant to Section 19(b)(2) [22] that the proposed rule change is hereby approved on an accelerated basis, through December 31, 1998.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[23]

Margaret H. McFarland,

Deputy Secretary.

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[20] For objective measure, the Commission also requests that the BSE provide the mean and median scores.

[21] *See* February 1993 Approval Order, *supra* note 4.

[22] 15 U.S.C. 78s(b)(2).

[23] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39736; File No. SR–CBOE–97–49]

Self-Regulatory Organizations; Chicago Board Options Exchange, Inc.; Order Granting Approval to Proposed Rule Change Relating to Trading Differentials for Option Contracts

March 9, 1998.

On October 21, 1997, the Chicago Board Options Exchange, Inc. (''CBOE'' or ''Exchange'') submitted to the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Exchange Act'' or ''Act'') [1] and Rule 19b–4 thereunder,[2] a proposed rule change to allow the Exchange to establish, upon the filing of a rule change proposal pursuant to Section 19(b)(3)(A) of the Exchange Act, the trading differentials for option contracts traded on the Exchange.

The proposed rule change was published for comment in the **Federal Register** on December 1, 1997.[3] No comments were received on the proposal. This order approves the proposal, as amended.

The Exchange is proposing to amend Exchange Rule 6.42 to give the Board of Directors the authority to establish the minimum trading increments for option contracts. Currently, Rule 6.42 that bids and offers shall be express in eighths of $1 unless a different increment is approved by the Floor Procedure Committee for an option contract of a particular series. An interpretation to the Rule states that bids and offers for all option series trading below $3 shall be expressed in sixteenths of a dollar. Until such time as the Board determines to make a change, the current standards will apply.

The proposed change would allow the Exchange to change the trading increments on an expedited basis and thus, allow the Exchange to respond appropriately to changes in the minimum trading increment in the markets for the securities underlying CBOE options or to changes in the minimum trading increments for one of the other options exchanges. When the Board of Directors determines to change the trading increments, the Exchange will designate such change as a stated policy, practice, or interpretation with respect to the administration of Rule 6.42 within the meaning of subparagraph (3)(A) of subsection 19(b) of the Exchange Act and will file a rule change for immediate effectiveness upon filing with the Commission.

The Exchange notes that there has been a movement within the industry to reduce the minimum trading and quotation increments imposed by the various SROs.[4] As derivative securities, the prices of options are determined in reference to the prices of the underlying securities. Consequently, the Exchange believes that where practicable, the Exchange should have minimum increments comparable to those applicable to the securities underlying CBOE options.

The Exchange also believes that the proposed rule change would give the Exchange the flexibility to follow the suit of the principal exchanges for the underlying securities without having to update its rules continually but at the same time would give the Exchange the flexibility it needs to deviate from the minimum increments established by the principal markets for the underlying securities in the event that the CBOE's systems were not immediately able to handle such increments. The Exchange, therefore, believes the quality of the market for CBOE options will be

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

[2] 17 CFR 240.19b–4.

[3] *See* Exchange Act Release No. 39348 (November 21, 1997), 62 FR 63577 (December 1, 1997). The Exchange submitted on amendment to the proposed rule change on November 17, 1997. *See* Letter from Timothy H. Thompson, CBOE, to Christine Richardson, Division of Market Regulation, Commission (Nov. 14, 1997). The amendment was published for comment along with the originally submitted filing. By adding the term ''appropriate'' before the term ''Floor Procedure Committee'' in the text of proposed Rule 6.42, the amendment clarifies that the decision to change the increments with respect to a particular class of options will be made by whichever Floor Procedure Committee has jurisdiction over trading in that option class. The amendment also replaced Exhibit 1 to the submitted filing with a revised Exhibit 1.

[4] *See* Exchange Act Release No. 38571 (May 5, 1997), 62 FR 25682 (May 9, 1997) (Commission order approving a change in the minimum increment to 1⁄16th for equity securities listed in the American Stock Exchange); Exchange Act Release No. 38678 (May 27, 1997), 62 FR 30363 (June 3, 1997) (Commission order approving a change in the minimum increment to 1⁄16th for Nasdaq-listed equity securities); and Exchange Act Release No. 38897 (Aug. 1, 1997), 62 FR 42847 (Aug. 8, 1997) (Commission order approving a change in the minimum increment to 1⁄16th for NYSE=listed equity securities).