

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

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46393; File No. SR-Amex-2002-31]

Self-Regulatory Organizations; Order Granting Approval to Proposed Rule Change by the American Stock Exchange LLC Requesting Permanent Approval of Pilot Program Eliminating Position and Exercise Limits for XMI and XII Index Options and Related Flex Options

August 21, 2002.

On April 12, 2002, the American Stock Exchange LLC ("Amex" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "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 request permanent approval of the pilot program that provides for the elimination of position and exercise limits for the Major Market ("XMI") and Institutional ("XII") broad-based index options, as well as FLEX Options on these indexes.³

The proposed rule change was published for comment in the **Federal Register** on May 30, 2002.⁴ The Commission received no comments on the proposal.

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 exchange⁵ and, in particular, the

requirements of section 6 of the Act⁶ and the rules and regulations thereunder. The Commission finds specifically that the proposed rule change is consistent with section 6(b)(5) of the Act⁷ in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission believes that it is appropriate to eliminate position and exercise limits for XMI and XII options, as well as related FLEX options, on a permanent basis based on the Amex's experience administering the Pilot Program. The Commission's original order approving the elimination of position and exercise limits for the XMI and XII index options (as well as FLEX options on these indexes) on a two-year basis required the Exchange to submit a report to the Commission regarding the status of the Pilot Program so that the Commission could use this information to evaluate any effects of the program.⁸

The Exchange's report indicated that from February 1, 1999 through March 30, 2001, no customer and/or firm accounts reached a level of 100,000 or more options contracts in XMI or XII options. During this review period, the Amex did not discover any instances where an account maintained an unusually large unhedged position. In addition, during the period from April 2, 2001 through February 28, 2002, the Amex did not experience accounts establishing positions in excess of the standard limit applicable to each index at the time the Pilot Program was approved.⁹

In addition to no identifiable problems during the pilot program, the Commission also believes that the factors for approval of the pilot program continue to be met. For example, in approving the pilot, the Commission stated, among other things, that the enormous capitalization of and deep, liquid markets for the underlying securities contained the XMI and XII indexes significantly reduces concerns

regarding market manipulation or disruption in the underlying market.

The Commission also continues to believe that the financial requirements imposed by the Amex and the Commission help to address concerns that a member or its customer may try to maintain an inordinately large unhedged position in a broad-based index option. The Amex has the authority to impose additional margin and/or assess capital charges and should be able to monitor accounts to determine when such action is warranted.

In addition, the Commission notes that the Amex has adopted surveillance¹⁰ and reporting safeguards that will allow it to detect and deter trading abuses arising from the elimination of position and exercise limits for XMI and XII, and FLEX options on these indexes.¹¹ The Commission continues to believe that these enhanced procedures are critical in our determination to permanently approve the pilot. While the pilot report did not note any aberrations or concerns about large unhedged positions, the Commission continues to believe that these procedures will enable the Amex to adequately assess and respond to market concerns at an early stage. In this regard, the Commission continues to expect the Amex to take prompt action, including timely communication with the Commission and other marketplace self-regulatory organizations responsible for oversight of trading in component stocks, should any unanticipated adverse market effects develop.

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹² that the proposed rule change (File No. SR-Amex-2002-31) be, and it hereby is, approved.

¹⁰ Disclosure of specific surveillance procedures could provide market participants with information that could aid potential attempts at avoiding regulatory detection of inappropriate trading activity.

¹¹ The Amex's reporting requirements subject XMI and XII, and FLEX options on those indexes to a 100,000 contract hedge reporting requirement. Each member or member organization that maintains a position on the same side of the market in excess of these contract thresholds for its own account or for the account of a customer must file a report that includes, but is not limited to, data related to the option position, whether such position is hedged and if so, a description of the hedge. If applicable, the report must contain information concerning collateral used to carry the position.

¹² 15 U.S.C. 78s(b)(2).

¹¹ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ On February 1, 1999, the Commission approved the elimination of position and exercise limits for the XMI and XII index options, as well as FLEX options on these indexes on a two-year basis (the "Pilot Program"). See Securities Exchange Act Release No. 41011 (February 1, 1999), 64 FR 6405 (February 9, 1999). The Pilot Program originally ended on February 1, 2001, with extensions for an additional six-month period approved on July 3, 2001 and January 3, 2002, respectively. See Securities Exchange Act Release No. 44507 (July 3, 2001), 66 FR 36348 (July 11, 2001); and Securities Exchange Act Release No. 45234 (January 3, 2002), 67 FR 1377 (January 10, 2002).

⁴ See Securities Exchange Act Release No. 45975 (May 23, 2002), 67 FR 37882 (May 30, 2002).

⁵ 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).

⁶ 15 U.S.C. 78f.

⁷ 15 U.S.C. 78f(b)(5).

⁸ See Securities Exchange Act Release No. 41011 (February 1, 1999), 64 FR 6405 (February 9, 1999).

⁹ Telephone call between Jeffrey P. Burns, Assistant General Counsel, Amex, and Susie Cho, Special Counsel, Division of Market Regulation, Commission, August 21, 2002. At the time the Commission approved the Pilot Program, the position limits for XMI and XII were 34,000 and 200,000, respectively.

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

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46390; File No. SR-ISE-2002-18]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by the International Securities Exchange LLC Relating to the Execution of Complex Orders Involving Options and Single Stock Futures

August 21, 2002.

I. Introduction

On June 27, 2002, the International Securities Exchange, Inc. ("ISE" or "Exchange") 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 adopt rules and procedures governing the execution of complex orders involving options and single stock futures. The proposed rule change was published for comment in the **Federal Register** on July 17, 2002.³ The Commission received no comments on the proposed rule change. This order approves the proposed rule change.

II. Description of the Proposal

The proposed rule change would permit Exchange members to enter option-stock future complex orders. As is the case with stock-option complex orders, the option leg of the transaction would have priority over non-customer orders at the same price. The Exchange would execute the option leg of the trade and the parties then would seek to execute the stock futures leg on an appropriate exchange. Because the stock futures products may not be fungible between markets, the member would be required to specify the market of execution for the stock futures leg of the complex order. In addition, as with stock-option complex orders, if the parties are unable to execute the stock futures leg of the transaction due to a change in market conditions, the Exchange would cancel the option leg of

the transaction at the request of a party to the trade. The proposed rule change would become part of the complex order pilot program, which the Commission has approved to operate through October 18, 2002.⁴

III. Discussion

After careful review, 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.⁵ In particular, the Commission believes that the proposed rule change is consistent with section 6(b)(5) of the Act,⁶ which requires, among other things, that the Exchange's rules be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

In general, the Commission believes that rules permitting the execution of complex orders serve to reduce the risk of incomplete or inadequate executions, while increasing efficiency and competitive pricing. At the same time, they protect the priority of orders of public customers by permitting the legs of complex orders to trade ahead of bids and offers established in a market place only under specific restrictions. The rule change authorizes the execution of complex orders involving options and single stock futures pursuant to procedures that are virtually identical procedures for complex orders involving options and stocks. The Commission believes that these types of orders are of a similar degree of complexity to those approved in the past for special priority rules, and it is therefore appropriate to afford them the same treatment.

IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and rules and regulations thereunder.

It is therefore ordered, pursuant to section 19(b)(2) of the Act,⁷ that the proposed rule change (SR-ISE-2002-18) is approved.

⁴ See Securities Exchange Act Release No. 44955 (October 18, 2001), 66 FR 53819 (October 24, 2001) (File No. SR-ISE-2001-18).

⁵ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁶ 15 U.S.C. 78f(b)(5).

⁷ 15 U.S.C. 78s(b)(2).

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

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46398; File No. SR-NASD-2002-114]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to the Availability of Nasdaq Services and Facilities Until 6:30 PM Eastern Time After the Introduction of Nasdaq's SuperMontage System

August 22, 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 August 19, 2002, the National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II and III 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) thereunder,⁴ which renders the proposal effective upon filing with the Commission.⁵ 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 filed this proposed rule change setting forth the operation of Nasdaq's current after-hours pilot program extending the availability of several Nasdaq services and facilities until 6:30 PM⁶ after the introduction of Nasdaq's SuperMontage system. Although the proposed rule change is

⁸ 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 The NASD provided the Commission with notice of its intent to file the proposed rule change on May 24, 2002. See Rule 19b-4(f)(6)(iii). 17 CFR 240.19b-4(f)(6)(iii). Nasdaq asked the Commission to waive the 30-day operative delay.

⁶ All references to time are Eastern Time.

¹³ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 46181 (July 11, 2002), 67 FR 47010.