additional strike prices and months, the existing $1 series will eventually expire. When the near-term month is the only series available for trading, the Exchange may submit a cessation notice to OCC. Upon submission of the notice, the underlying stock will no longer count towards the five stocks that CBOE may select for its Pilot Program. Once the Exchange submits the cessation notice, it will not list any additional month for trading with strikes below $20 unless the underlying again closes below $20, and then, only if the CBOE has not already selected a replacement stock.

According to CBOE, the Options Price Reporting Authority (''OPRA'') has the capacity to accommodate the increase in the number of series that would be added pursuant to the Pilot Program. In addition, CBOE notes that it listed approximately 109,000 series in December 2000 and approximately 100,000 series in September 2001. The CBOE believes that the increase in the number of series resulting from the Pilot Program will be substantially lower than the 9,000 series decrease the CBOE experienced.

III. Summary of Comments

The Commission received one comment letter on the proposed rule change, which supports the proposal.[13] Specifically, the commenter believes that the CBOE's proposal would provide equity investors with the flexibility necessary to hedge their risk as efficiently as possible.

IV. 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.[14] In particular, the Commission believes that the proposed rule change is consistent with section 6(b)(5) of the Act,[15] which requires, among other things, that the rules of a national securities exchange be designed 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. Specifically, the Commission believes that the proposed listing of one point strike price intervals in selected equity options on a pilot basis should provide investors with more flexibility in the trading of equity options overlying stocks trading at less than $20, thereby furthering the public interest by allowing investors to establish equity options positions that are better tailored to meet their investment objectives. The Commission also believes that the Exchange's limited Pilot Program strikes a reasonable balance between the Exchange's desire to accommodate market participants by offering a wide array of investment opportunities and the need to avoid unnecessary proliferation of options series. The Commission expects the Exchange to monitor the applicable equity options activity closely to detect any proliferation of illiquid options series resulting from the narrower strike price intervals and to act promptly to remedy this situation should it occur. In addition, the Commission requests that CBOE monitor the trading volume associated with the additional options series listed as a result of the Pilot Program and the effect of these additional series on market fragmentation and on the capacity of the Exchange's, OPRA's, and vendors' automated systems.

As noted above, the Commission is approving the CBOE's proposal on a one-year pilot basis. In the event that CBOE proposes to extend the Pilot Program beyond June 5, 2004, expand the number of options eligible for inclusion in the Pilot Program, or seek permanent approval of the Pilot Program, it should submit a Pilot Program report to the Commission along with the filing of such proposal.[16] The report must cover the entire time the Pilot Program was in effect, and must include: (1) Data and written analysis on the open interest and trading volume for options (at all strike price intervals) selected for the Pilot Program; (2) delisted options series (for all strike price intervals) for all options selected for the Pilot Program; (3) an assessment of the appropriateness of $1 strike price intervals for the options the CBOE selected for the Pilot Program; (4) an assessment of the impact of the Pilot Program on the capacity of the CBOE's, OPRA's, and vendors' automated systems; (5) any capacity problems or other problems that arose during the operation of the Pilot Program and how the CBOE addressed them; (6) any complaints that the CBOE received during the operation of the Pilot Program and how the CBOE addressed them; and (7) any additional information that would help to assess the operation of the Pilot Program.

V. 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,[17] that the proposed rule change (SR–CBOE–2001–60) is approved, on a pilot basis, through June 5, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[18]

J. Lynn Taylor,

Assistant Secretary.

[FR Doc. 03–14829 Filed 6–11–03; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–47998; File No. SR–GSCC–00–12]

Self-Regulatory Organizations; Government Securities Clearing Corporation; Order Granting Approval of a Proposed Rule Change Relating to Insolvency and Clearing Fund Requirements

June 6, 2003.

I. Introduction

On October 5, 2000, Government Securities Clearing Corporation (''GSCC'')[1] filed with the Securities and Exchange Commission (''Commission'') proposed rule change File No. SR–GSCC–00–12 pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[2] and on December 14, 2000, amended the proposed rule change. Notice of the proposal was published in the **Federal Register** on June 17, 2002.[3] No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description

On January 30, 1996, the Commission issued an order approving GSCC's

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[13] *See* Cornerstone Letter, *supra* note 12.

[14] 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).

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

[16] The Commission expects the CBOE to submit a proposed rule change at least 60 days before the expiration of the Pilot Program in the event the CBOE wishes to extend, expand, or seek permanent approval of the Pilot Program.

[17] 15 U.S.C. 78s(b)(2).

[18] 17 CFR 200.30–3(a)(12).

[1] On January 1, 2003, MBS Clearing Corporation was merged into GSCC under New York law and GSCC was renamed the Fixed Income Clearing Corporation. Securities Exchange Act Release No. 47015 (December 17, 2002), 67 FR 78531 (December 24, 2002) (File Nos. SR–GSCC–2002–10 and MBSCC–2002–01).

[2] 15 U.S.C. 78s(b)(1).

[3] Securities Exchange Act Release No. 46053 (June 10, 2002), 67 FR 41285.

proposed rule change permitting foreign entities to become members of GSCC's netting system.[4] The rule change established application and continuing membership requirements for foreign entities, including the delivery to GSCC of an opinion of foreign counsel addressing the particular jurisdictional concerns raised by the admission of a foreign entity to netting system membership.[5]

Having gained experience from reviewing the legal opinions regarding foreign law that were provided in connection with the applications of the foreign banks that GSCC has admitted to its netting system to date, GSCC has determined to clarify its insolvency rule, rule 22, in the manner described in subsection (i) below so that the insolvency rule more appropriately references the types of insolvency proceedings to which a foreign member might become subject. GSCC will also make conforming language changes to GSCC's rules dealing with applications for membership standards as they apply to foreign members.

Some of the legal opinions referred to in the previous paragraph have indicated that GSCC would be exposed to ''legal risk'' as a result of the application of the particular jurisdiction's law to a foreign member's insolvency or bankruptcy. The legal risk can take the form of prohibiting or delaying GSCC from: Accessing some or all of the clearing fund deposit of the member; performing its netting, close-out, or liquidation of transactions; or setting off obligations as set forth in its clearing fund rule (rule 4), its ceasing to act rule (rule 21), or its insolvency rule (rule 22) or taking any other action contemplated by these rules. GSCC is amending its rules to better protect itself and its members from these types of legal risk in the circumstances where GSCC reasonably determines based upon factors such as outside legal advice or discussions with a relevant regulator that such legal risk exists. The proposed rule changes are described more fully in subsection (ii) below.

GSCC's experience in connection with the admission of U.S. branches of foreign banks has also indicated that certain issues that are described in these opinions could affect GSCC's rights in the event of the insolvency or bankruptcy of a domestic member. GSCC believes, given the importance of its being able to exercise its rights as set forth in its clearing fund rule, its ceasing to act rule, and its insolvency rule that the proposed rule changes discussed below in subsection (ii) should also apply to domestic members that present GSCC with legal risk. GSCC would reasonably determine that such legal risk exists based upon factors such as outside legal advice or discussions with a relevant regulator.

GSCC is also adding language to its clearing fund rule clarifying its right to rehypothecate the cash deposits of its clearing fund.

(i) Changes to Insolvency Rule

GSCC's insolvency rule contains a section that lists the various types of events or proceedings that would permit GSCC to treat a member as insolvent. The rule was written utilizing terms common in United States insolvency or bankruptcy proceedings. GSCC is amending its insolvency rule to add language so that the rule more appropriately references the types of insolvency proceedings to which a foreign member might become subject.

GSCC's foreign membership agreements have already been expanded to incorporate the insolvency triggering events that GSCC is now making part of its rules. The changes will bring the rules into conformity with the foreign membership agreements and specifically give GSCC the right pursuant to its rules to declare a foreign member to be insolvent under the requisite circumstances.[6]

(ii) Clearing Fund Requirements

One of GSCC's most important risk management tools is its clearing fund, which is comprised of cash, certain netting-eligible securities, and eligible letters of credit. The purposes served by the clearing fund are: (1) To have on deposit from each netting member assets sufficient to satisfy any losses that may be incurred by GSCC as the result of the default by the member and the resultant close-out of that member's settlement positions; (2) to maintain a total asset amount sufficient to satisfy potential losses to GSCC and its members resulting from the failure of more than one member (and the failure of such members' counterparties to pay their pro rata allocation of loss); and (3) to ensure that GSCC has sufficient liquidity at all times to meet its payment and delivery obligations.

A member's clearing fund deposit, to serve its intended purpose, should be immediately accessible by GSCC in the event of the member's bankruptcy or insolvency. However, the application of certain domestic or foreign laws could delay or prevent GSCC from accessing the portion of the member's clearing fund deposit that is in the form of cash and securities. The portion of the member's clearing fund deposit that is in the form of letters of credit (''LCs'') is generally not subject to the same risk because LCs are typically not considered to be part of the bankrupt/insolvent entity's estate.

The rules with respect to the calculation of a member's clearing fund deposit do not currently address this legal risk. In order to better protect itself and its members, GSCC is amending its rules to require a domestic or foreign member that in management's reasonable view (which may be based upon factors such as outside legal advice or discussions with a relevant regulator) presents heightened legal risk to GSCC to deposit additional collateral over what would normally be required under GSCC's clearing fund rule and/or to post some additional portion of its clearing fund deposit requirement in the form of an LC.[7]

(iii) Clarification of Rehypothecation Right With Respect to Cash Deposits

GSCC's clearing fund rule contains a provision that permits GSCC to rehypothecate, transfer, or assign its clearing fund collateral in the event that GSCC needs to secure a loan or to satisfy an obligation incurred by it incident to its clearance and settlement business. GSCC is clarifying the provision with respect to the portions of the clearing funds that may be rehypothecated, transferred, or assigned by GSCC. The provision refers to the securities and the LCs that members pledge or deposit to the clearing fund as well as to the ''deposits or other instruments in which the cash deposits'' are invested. GSCC believes that this language could be read to not actually refer to the cash deposits themselves. Therefore, GSCC believes that it is prudent to specifically add a reference in the rule to ''cash deposits'' in order to eliminate any doubt as to GSCC's ability to use the cash portion of the clearing fund in the manner set forth in the clearing fund rule.

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the

[4] Securities Exchange Act Release No. 36788 (January 10, 1996), 61 FR 4500 (February 6, 1996) (File No. SR–GSCC–95–05).

[5] GSCC also requires each prospective foreign member to provide a legal opinion on insolvency discussing applicable U.S. Federal and State laws.

[6] In addition, the proposed rule change makes conforming language changes to GSCC's rule 2 (Members) and rule 3 (Financial Responsibility and Operational Capability Standards) as they apply to foreign members.

[7] GSCC's clearing fund rule requires that LCs constitute no more than 70 percent of a member's clearing fund deposit. GSCC is amending its rule so that it may ask for a higher percentage in the form of an LC if circumstances warrant.

rules and regulations thereunder and particularly with the requirements of section 17A(b)(3)(F) of the Act, which requires that the rules of a clearing agency be designed to safeguard securities and funds in its custody or control or for which it is responsible.[8] The Commission finds that by having the ability to require an additional clearing fund deposit or deposits in the form of letters of credit in circumstances as described above, the proposed rule change will help to ensure that GSCC has adequate clearing fund assets available to it in the event that it must liquidate the collateral of an insolvent participant. Additionally, the change to GSCC's insolvency rule to include references to certain insolvency proceedings against foreign members will better equip GSCC to handle the financial difficulties of foreign members and should help GSCC to assure the safeguarding of securities and funds in the its custody or control or for which it is responsible. Therefore, the proposed rule change is consistent with GSCC safeguarding obligations under section 17A(b)(3)(F).

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular with the requirements of section 17A of the Act and the rules and regulations thereunder applicable.

It is therefore ordered, pursuant to section 19(b)(2) of the Act, that the proposed rule change (File No. SR–GSCC–00–12) be, and hereby is, approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.[9]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03–14831 Filed 6–11–03; 8:45 am]

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[8] 15 U.S.C. 78q–1(b)(3)(F).

[9] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–47993; File No. SR–NASD–2003–81]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by National Association of Securities Dealers, Inc. Relating to Quote Decrementation in SuperMontage

June 5, 2003.

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 May 12, 2003, 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 (''SEC'' or ''Commission'') the proposed rule change as described in items I, II, and III below, which items have been prepared by Nasdaq. On May 29, 2003, Nasdaq filed Amendment No. 1 to the proposal.[3] The Commission is publishing this notice, as amended, 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 proposes to modify how the quotes of order-delivery Electronic Communication Networks (''ECNs'') in Nasdaq's National Market Execution System (''NNMS'' or ''SuperMontage'') will be decremented after they decline an order shipped to them, or partially fill an order sent to them, or fail to respond to the delivery within 30 seconds.[4] Under the proposal, order-delivery ECNs that decline an order, partially fill an order, or fail to respond within 30 seconds to orders sent to them (''time-out'') by SuperMontage will no longer have all of their trading interest at or better than the declined price level removed from the system. Instead, the system after a decline, partial fill, or time-out, will remove the entire amount of each individual quote(s)/order(s) to which the orders was delivered to by NNMS. The proposed rule text is as follows:

Proposed new language is *italicized*; proposed deletions are in [brackets].

4710. Participant Obligations in NNMS

(b) Non-Directed Orders

(1) General Provisions—A Quoting Market Participant in an NNMS Security, as well as NNMS Order Entry Firms, shall be subject to the following requirements for Non-Directed Orders:

(A) through (B)—No Change.

(C) Decrementation Procedures—The size of a Quote/Order displayed in the Nasdaq Order Display Facility and/or the Nasdaq Quotation Montage will be decremented upon the delivery of a Liability Order or the delivery of an execution of a Non-Directed Order or Preferenced Order in an amount equal to the system-delivered order or execution.

(i) If an NNMS Auto-Ex ECN has its bid or offer Attributable Quote/Order and Reserve Size decremented to zero without transmission of another Attributable Quote/Order to Nasdaq, the system will zero out the side of the quote that is exhausted. If both the bid and offer are decremented to zero without transmission of a revised Attributable Quote/Order, the ECN will be placed into an excused withdrawal state until the ECN transmits to Nasdaq a revised Attributable Quote/Order.

(ii) If an NNMS Order-Delivery ECN declines or partially fills a Non-Directed Order without immediately transmitting to Nasdaq a revised Attributable Quote/Order that is at a price inferior to the previous price, or if an NNMS Order-Delivery ECN fails to respond in any manner within 30 seconds of order delivery, the system will cancel the delivered order and send the order (or remaining portion thereof) back into the system for immediate delivery to the next [Quoting Market Participant] *eligible Quote/Order* in queue. The system then will zero out [the] *those* ECN['s] Quote/Orders *to which the Non-Directed Order was delivered.* [at that price level on that side of the market,] *If there are no other Quote/Orders at the declined price level*, [and] the ECN's quote on that side of the market will remain at zero until the ECN transmits to Nasdaq a revised Attributable Quote/Order. If both the bid and offer are zeroed out, the ECN will be placed into an excused withdrawal state until the

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

[2] 17 CFR 240.19b–4.

[3] *See* letter from Mary M. Dunbar, Vice President and Deputy General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation (''Division''), Commission, dated May 29, 2003 (''Amendment No. 1''). In Amendment No. 1, Nasdaq replaced the proposed rule change in its entirety.

[4] Nasdaq's original target date for implementation of this proposal, if approved by the Commission, was June 16, 2003. Nasdaq has revised its intended implementation time-frame for mid-July 2003, and will notify the Commission and market participants when a firm date has been set. Telephone conversation between Thomas Moran, Associate General Counsel, Nasdaq, and Marc McKayle, Special Counsel, Division, Commission on June 5, 2003.