

For the Commission, by the Division of Investment Management, under delegated authority.

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Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46507; File No. SR-CBOE-2002-54]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Chicago Board Options Exchange, Inc. Proposing To Allow the Listing of Options on Exchange Traded Funds at \$1 Strike Price Intervals

September 17, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 12, 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. 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

CBOE proposes to list options at \$1 strike price intervals on securities ("Units") that represent interests in registered investment companies (or series thereof) organized as open-ended management investment companies, unit investment trusts, or similar entities that are principally traded on a national securities exchange or through the facilities of a national securities association, and that meet all criteria of Interpretation and Policy .06 to CBOE Rule 5.3., commonly referred to as "Exchange Traded Funds" or "ETFs." The text of the proposed rule change appears below. New text is in italics.

#### CBOE Rule 5.5: Series of Option Contracts Open for Trading

(a)-(c) No Change.

\* \* \* Interpretations and Policies

.01-.07 No change.

.08 *Notwithstanding Interpretation and Policy .01 above, and except for*

*options on Units covered under Interpretation and Policies .06 and .07 above, the interval between strike prices of series of options on Units, as defined under Interpretation and Policy .06 to Rule 5.3, will be \$1 or greater where the strike price is \$200 or less.*

#### 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 proposes to amend CBOE Rule 5.5 by adding Interpretation and Policy .08, which would provide for \$1 strike price intervals for options traded on ETFs. Additionally, the interval of strike prices for options on ETFs can be \$1 only where the strike price is at \$200 or less.

CBOE contends that this proposed amendment is consistent with the strike price intervals established for options on ETFs on the American Stock Exchange LLC ("Amex"), the Philadelphia Stock Exchange, Inc. ("Phlx"), and the International Securities Exchange, Inc. ("ISE").<sup>3</sup> Furthermore, the CBOE currently trades options on certain ETFs at \$1 strike price intervals.<sup>4</sup> Specifically, that proposed rule change allowed for \$1 strike price intervals for options on Nasdaq-100 Index ETFs ("QQQ") and was based on similar Amex rules relating to strike price intervals for options on ETFs.

<sup>3</sup> See Securities Exchange Act Release Nos. 40157 (July 1, 1998), 63 FR 37426 (Amex approval order); 44037 (March 2, 2001), 66 FR 14613 (March 13, 2001) (ISE approval order); and 44055 (March 8, 2001), 66 FR 15310 (March 16, 2001) (Phlx). Although the Phlx proposal granted \$1 strike price intervals for trading on the general term "ETFs," CBOE believes that it would be more accurate, under CBOE rules, to clarify the specific definition of an ETF by granting the \$1 strike price intervals to those Units provided for under Interpretation and Policy .06 to CBOE Rule 5.3.

<sup>4</sup> See Securities Exchange Act Release No. 44147 (April 3, 2001), 66 FR 18676 (April 10, 2001).

Lastly, CBOE affirms that it has the necessary systems capacity to support any additional series of options that may be added pursuant to the proposed rule change. Further, CBOE has been advised by Options Price Reporting Authority ("OPRA") that it has the capacity to support any additional series of options that may be added pursuant to the proposed rule change.<sup>5</sup>

###### (2) Statutory Basis

The CBOE believes that the proposed rule change is consistent with section 6(b) of the Act,<sup>6</sup> in general, and furthers the objectives of section 6(b)(5),<sup>7</sup> in particular, in that it is designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and, in general, 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 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

No written comments were solicited or received with respect to the proposed rule change.

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

The foregoing rule change has become effective pursuant to section 19(b)(3)(A) of the Act<sup>8</sup> and subparagraph (f)(6) of Rule 19b-4<sup>9</sup> thereunder because the Exchange has designated the proposed rule change as one that does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate; and the Exchange has given the Commission written notice of its intention to file the proposed rule change at least five business days prior to filing. At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission

<sup>5</sup> See letter from Joseph P. Corrigan, Executive Director, OPRA, to William Speth, Director of Research, CBOE, dated September 11, 2002.

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

<sup>8</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>9</sup> 17 CFR 240.19b-4(f)(6).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

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.

Under Rule 19b-4(f)(6)(iii) of the Act,<sup>10</sup> the proposal does not become operative for 30 days after the date of its filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest and the Exchange is required to give the Commission written notice of its intention to file the proposed rule change at least five business days prior to filing. The Exchange has requested that the Commission waive the 30-day operative date and the five-day pre-filing notice requirement in order for it to implement the proposed rule change as quickly as possible. The CBOE contends that the proposed rule is substantially similar to comparable rules of the Amex, ISE, and Phlx. The Commission, consistent with the protection of investors and the public interest, has determined to waive the 30-day operative period as well as the five-day pre-filing notice requirement,<sup>11</sup> and, therefore, the proposal is effective and operative upon filing with the Commission.

#### 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 Exchange. All submissions should refer to File No.

SR-CBOE-2002-54 and should be submitted by October 16, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46514; File No. SR-ISE-2001-19]

### Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 to the Proposed Rule Change by the International Securities Exchange LLC Relating to Facilitation of Customer Orders

September 18, 2002.

#### I. Introduction

On May 30, 2001, the International Securities Exchange LLC ("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")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to reduce the exposure time required for the facilitation of customer orders through the Exchange's Facilitation Mechanism from 30 seconds to five seconds. Notice of the proposed rule change was published for comment in the **Federal Register** on August 6, 2001.<sup>3</sup> The Commission received thirteen comment letters regarding the proposal<sup>4</sup>

<sup>12</sup> 17 CFR 200.30-3(a)(12).

<sup>15</sup> U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 44612 (July 27, 2001), 66 FR 41074 ("Notice").

<sup>4</sup> See letters to Jonathan G. Katz, Secretary, Commission, from: Joel Greenberg, Managing Director, Susquehanna International Group, LLP, dated August 16, 2001 ("Susquehanna Letter I"); Arthur Duquette, Senior Managing Director, Bear, Stearns & Co. Inc., dated August 24, 2001 (Bear Stearns Letter); Edward J. Joyce, President and Chief Operating Officer, Chicago Board Options Exchange, Incorporated ("CBOE"), dated August 27, 2001 ("CBOE Letter I"); Thomas N. McManus, Executive Director and Counsel, Morgan Stanley & Co. Incorporated, dated August 27, 2001 ("Morgan Stanley Letter"); Juan Carlos Pinilla, Managing Director, Equity Derivatives Group, J.P. Morgan Securities Inc., dated August 27, 2001 ("J.P. Morgan Letter"); Arthur S. Margulis, Jr., Managing Principal, Hull Trading Company, LLC, dated August 30, 2001 ("Hull Letter"); Michael J. Ryan, Executive Vice President and General Counsel, American Stock Exchange LLC ("Amex"), dated August 29, 2001 ("Amex Letter I"); Matthew D. Wayne, Chief Legal Officer, Knight Financial

and two letters from the ISE responding to the assertions of commenters who opposed its proposal.<sup>5</sup> On January 3, 2002, the ISE filed Amendment No. 1 to the proposed rule change, amending the proposal to provide for an exposure period of 10 seconds.<sup>6</sup> This order approves the proposed rule change, as amended, grants accelerated approval of Amendment No. 1, and solicits comments from interested persons on that amendment.

#### II. Description of the Proposal

ISE rules provide that an Electronic Access Member ("EAM") generally may not trade as principal against an order of a customer that it is representing as an agent unless the EAM: (1) Enters the customer order into the market and waits at least 30 seconds before entering its counter proprietary order; (2) has been bidding or offering on the Exchange on behalf of its proprietary account at least 30 seconds prior to receiving the customer order; or (3) makes use of the Exchange's "Facilitation Mechanism."<sup>7</sup>

When an EAM enters a customer order into this Facilitation Mechanism, a broadcast message alerts members of the Exchange's electronic "crowd"—market makers and other members with proprietary orders in the relevant series at the inside bid or offer on the ISE trading system—to the size and price of the proposed facilitation. Crowd participants may indicate within a given time period (currently 30 seconds) whether they want to participate in the facilitation of the customer order at the proposed facilitation price. Crowd participants may also indicate that they are willing to participate in the facilitation of the customer order at a price better than the proposed facilitation price. If, however, this better

Products, LLC, dated September 14, 2001 ("Knight Letter"); Thomas A. Bond, Chief Operating Officer, Lee E. Tenzer Trading Company, dated November 9, 2001 ("Letco Letter"); Edward J. Joyce, President and Chief Operating Officer, CBOE, dated November 14, 2001 ("CBOE Letter II"); Edward J. Joyce, President and Chief Operating Officer, CBOE, dated February 25, 2002 ("CBOE Letter III"); Gerald D. O'Connell, Associate Director, Susquehanna International Group, LLP, dated March 6, 2002 ("Susquehanna Letter II"); and Michael J. Ryan, Executive Vice President and General Counsel, Amex, dated April 17, 2002 ("Amex Letter II").

<sup>5</sup> See letters from Michael Simon, Senior Vice President and Secretary, ISE, to Jonathan G. Katz, Secretary, Commission, dated September 25, 2001, and October 5, 2001 ("ISE Letter I" and "ISE Letter II," respectively).

<sup>6</sup> See letter from Michael Simon, Senior Vice President and General Counsel, ISE, to Nancy Sanow, Assistant Director, Commission, dated January 2, 2002.

<sup>7</sup> ISE Rule 717(d). To use the Facilitation Mechanism, an EAM must be willing to facilitate the entire size of the customer order. See ISE Rule 716(d).

<sup>10</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>11</sup> For purposes only of waiving the five-day pre-filing notice requirement and the 30-day operative period for this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).