

periods will immediately become payable to all participants and will be paid within 30 days after the change in control.

The Committee may, unless the relevant award agreement otherwise specifies, cancel, rescind, or suspend an award in the event that the LTIP participant engages in competitive activity, discloses confidential information, solicits employees, customers, partners or suppliers of Allegheny, or undertakes any other action determined by the Committee to be detrimental to Allegheny.

The LTIP contains provisions intended to ensure that certain restricted share awards and performance awards to "covered employees" under Section 162(m) of the Internal Revenue Code are exempt from the \$1 million deduction limit contained in that section of the code. Those exemptive provisions, by their terms and under the applicable IRS regulations, expired as of May 14, 2003. Any pending, but unvested, awards issued under these provisions are unaffected by the provisions' expiration, but any future restricted stock or performance awards to covered employees will not be eligible for the exemption from the Section 162(m) limit unless the provisions are reapproved by the shareholders. Allegheny may seek stockholder reauthorization of the LTIP with respect to these provisions, but has no present intention to do so. Allegheny may choose alternative methods to compensate covered employees who would have received compensation under the terminated provisions of the LTIP had these provisions not terminated.

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

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48771; File No. SR-CBOE-2003-25]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1, 2, and 3 by the Chicago Board Options Exchange, Inc. Relating to Bid-Ask Differentials

November 12, 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 June 20, 2003, 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 CBOE filed Amendments Nos. 1, 2, and 3 to the proposal on July 3, 2003,³ September 10, 2003,⁴ and October 29, 2003,⁵ respectively. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The CBOE proposes to amend CBOE Rule 8.7, "Obligations of Market Makers," to allow the appropriate Market Performance Committee ("MPC") to establish bid-ask differentials that are no more than \$0.50 wide ("double-width") for options where the bid price is less than \$2 when the primary market for the underlying security: (1) Reports a trade outside of its disseminated quote, including any Liquidity Quote;⁶ or (2) disseminates an

inverted quote. The double-width relief must terminate automatically when the triggering event ceases.

The text of the proposed rule change appears below. Additions are in *italics*.

Rule 8.7 Obligations of Market Makers

- (a) No change.
- (b) No change.
- (i)-(iii) No change.
- (iv) No change.

(A) Without limiting the authority provided to it in Rule 8.7(b)(iv), the appropriate MPC may, with respect to options trading with a bid price less than \$2, establish bid-ask differentials that are no more than \$0.50 wide ("double-width") when the primary market for the underlying security: (a) Reports a trade outside of its disseminated quote (including any Liquidity Quote); or (b) disseminates an inverted quote. The imposition of double-width relief must automatically terminate when the condition that necessitated the double-width relief (i.e., condition (a) or (b)) is no longer present. Market makers that have not automated this process may not avail themselves of the relief provided herein (i.e., they may not manually adjust prices).

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 Rule 8.7(b)(iv) establishes bid-ask differentials and allows the appropriate MPC to establish differences for one or more options series.⁷ The

best bid (in the case of a Liquidity Bid) or at a specific price interval above the best offer (in the case of a Liquidity Offer). See Securities Exchange Act Release No. 47614 (April 2, 2003), 68 FR 17140 (April 8, 2003) (File No. SR-NYSE-2002-55).

⁷ CBOE Rule 8.7(b)(iv) requires market makers to bid and/or offer so as to create differences of no more than \$0.25 between the bid and the offer for each option contract for which the bid is less than \$2; no more than \$0.40 where the bid is at least \$2

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See letter from Steve Youhn, CBOE, to Deborah Flynn, Division of Market Regulation ("Division"), Commission, dated July 2, 2003, and accompanying Form 19b-4 ("Amendment No. 1"). Amendment No. 1 converts the proposal from a filing submitted pursuant to Section 19(b)(3)(A) of the Act to a proposal filed pursuant to Section 19(b)(2) of the Act. In addition, Amendment No. 1 clarifies that the CBOE's autoquote systems automatically will widen quotes to double the applicable bid-ask differential upon the occurrence of one of the triggering events and automatically will return the quotes to the normal bid-ask differential when the triggering event ceases.

⁴ See letter from Steve Youhn, CBOE, to Deborah Flynn, Division, Commission, dated September 9, 2003 ("Amendment No. 2"). Amendment No. 2 provides examples illustrating the need for the proposed relief, clarifies that CBOE market makers will not be able to widen their quotes when the New York Stock Exchange, Inc. ("NYSE") prints a trade at or within its Liquidity Quote, and states that neither the CBOE's Retail Automated Execution System ("RAES") nor the CBOE's Hybrid System will automatically execute incoming orders at prices inferior to the national best bid or offer ("NBBO").

⁵ See letter from Steve Youhn, CBOE, to Deborah Flynn, Division, Commission, dated October 28, 2003 ("Amendment No. 3"). Amendment No. 3 revises the proposal to limit the application of the quote width relief to options that trade with a bid price of less than \$2 and clarifies that the quote width relief provided in the proposal will be available only to a market maker who has an automated quotation system that will return his or her quotes to the normal bid-ask differential when the triggering event ceases.

⁶ The rules of the NYSE permit the dissemination, in selected securities, of a "Liquidity Bid" and a "Liquidity Offer" which reflect aggregated NYSE trading interest at a specific price interval below the

Exchange proposes to amend this rule to codify two instances when the bid-ask differential for options trading with a bid price of less than \$2 may be wider than the \$0.25 interval expressly required for such options by CBOE Rule 8.7(b)(iv). Specifically, proposed CBOE Rule 8.7(b)(iv)(A) authorizes the appropriate MPC, with respect to options trading with a bid price less than \$2, to establish bid-ask differentials that are no more than \$0.50 wide ("double-width") when the primary market for the underlying security: (a) Reports a trade that occurs outside of its disseminated quote (including any Liquidity Quote); or (b) disseminates an inverted quote (together, the "triggering events"). The proposed quote width relief will apply to options on stocks and options on exchange-traded funds ("ETFs").⁸

The proposed quote width relief will apply only to options that trade with a bid price of less than \$2.⁹ Thus, options trading at a price of \$2 (bid) or higher will not be eligible for the proposed quote width relief. The CBOE notes that options trading at less than \$2 are subject to a \$0.25 bid-ask differential, which generally means that market makers have only \$0.125 of pricing latitude on either side of the theoretical value to widen their quotes to take into account any pricing discrepancy in the underlying security. As described more fully below, the CBOE believes that the grant of double-width relief for low-priced options will provide market makers with more pricing flexibility with which to protect themselves.

Under the proposal, CBOE market makers will not be permitted to widen their quotes when the NYSE prints a trade at or within its Liquidity Quote. Because the NYSE disseminates Liquidity Quotes, which are quotes of substantial size outside of the regular disseminated quote, the CBOE notes that CBOE market makers should not be surprised if the NYSE prints a trade outside of its regular quote but at or within its Liquidity Quote. For this

but does not exceed \$5; no more than \$0.50 where the bid is more than \$5 but does not exceed \$10; no more than \$0.80 where the bid is more than \$10 but does not exceed \$20; and no more than \$1.00 where the bid is more than \$20. The bid/ask differentials do not apply to in-the-money series where the underlying securities market is wider than the differentials set forth in CBOE Rule 8.7(b)(iv). For those series, the bid/ask differential may be as wide as the quotation on the primary market of the underlying security.

⁸ Upon Commission approval of the proposal, the CBOE, prior to the effective date of the rule, will disseminate to members a Regulatory Circular that identifies the specific ETF that will serve as the underlying security for each option class. See Amendment No. 3, *supra* note 5.

⁹ See Amendment No. 3, *supra* note 5.

reason, the CBOE does not propose to allow the MPC to authorize CBOE market makers to widen their quotes when the NYSE prints a trade at or within its Liquidity Quote. However, if the NYSE prints a trade outside of the Liquidity Quote, a CBOE market maker would be able to widen its quotes. The following example illustrates the operation of the proposal with respect to Liquidity Quotes:

- NYSE disseminated quote: \$23.10–\$23.20, 300 × 1000
- NYSE Liquidity Quote: \$22.95–\$23.35, 15,000 × 15,000

With the above quotes, if the NYSE reports a trade between \$22.95 and \$23.35, CBOE market makers would not be permitted to quote double-wide. If the NYSE reports a trade below \$22.95 or above \$23.35 without changing its disseminated quote, CBOE market makers would be permitted to quote double-wide.

The CBOE intends to automate its systems so that the CBOE's autoquote systems automatically will widen the quote to double the bid-ask differential upon the occurrence of either of the two triggering events.¹⁰ The quotes will remain double-width until the triggering event ceases, at which time CBOE systems automatically will return the quote to the normal bid-ask differential. Accordingly, if the primary market's quotes invert and the CBOE quotes double-wide, the CBOE's quotes must return to normal width when the underlying market's quotes no longer are inverted. Similarly, if the primary market prints a trade outside of its disseminated quote, the CBOE may quote double-wide until the print is no longer outside of the disseminated quotes (*i.e.*, until the quotes move to encompass the previous print or the next print is inside of the disseminated quotes).¹¹

The CBOE notes that the automation of this process ensures that double-width relief will take effect only when permissible and, more importantly, will last only as long as the condition that necessitated it occurs. Thus, there will be no sustained dissemination of stale double-wide quotes when one of the triggering events is not present.¹² In addition, the CBOE states that a market maker will be able to utilize the double-width relief only if the market maker has an automated quotation system that returns the market maker's quotes to normal width upon the termination of the triggering event.¹³ Double-width

relief will not be available to market makers who must rely on manual input to restore quote values to normal width.

The CBOE notes that the grant of double-width relief will not result in the automatic execution of customer orders at artificially wide prices.¹⁴ According to the CBOE, neither RAES nor the CBOE Hybrid System will automatically execute incoming orders at prices inferior to the NBBO. Instead, orders received while the CBOE is not the NBBO will route to PAR, where the DPM can expose the order to the crowd or send a linkage order to an away market. Accordingly, the CBOE notes that orders received while the CBOE's quotes are double-wide would receive a measure of price protection.

In addition, the CBOE represents that the purpose of the proposal is not to create a heightened profit opportunity by allowing CBOE market makers to execute trades at widened quotes and, hence, increased profits.¹⁵ Instead, the CBOE believes that the proposal represents a narrowly-tailored protective measure designed to enable CBOE market makers to widen their quotes when a situation occurs in the underlying market that prevents accurate pricing. Under the proposal, market makers will have the ability, if they choose, to widen their quotes to limit the losses that may occur when the underlying market disseminates faulty or delayed information.

Necessity for the Relief Requested

According to the CBOE, the main component of equity option pricing is the value of the underlying security. The CBOE states that accurate option pricing is impossible if the value of the underlying security is unreliable or indiscernible. The following examples provided by the CBOE highlight the difficulties and risks in pricing options when the quote for the underlying security is inverted and/or when the underlying market prints a trade outside of its disseminated quote.

a. Underlying Market Disseminates an Inverted Quote

Assume that the quote for stock ABCD is \$21.06–\$21.16 and that, based on those prices, the quote for the July 20 call option is \$1.15–\$1.25. Now assume that the stock quote changes to \$21.12–\$21.02, creating an inversion. Under these circumstances, it is not clear which price, the bid or the offer, is correct, or whether both prices are incorrect. If the bid is correct, the quote for the underlying stock might be

¹⁰ See Amendment No. 1, *supra* note 3.

¹¹ See Amendment No. 3, *supra* note 5.

¹² See Amendment No. 1, *supra* note 3.

¹³ See Amendment No. 3, *supra* note 5.

¹⁴ See Amendment No. 2, *supra* note 4.

¹⁵ See Amendment No. 2, *supra* note 4.

\$21.12–\$21.22, which might drive the options quote to \$1.25–\$1.35. If the offer is correct, the quote for the underlying stock might be \$20.92–\$21.02, which might drive the options quote to \$1.05–\$1.15. If both the bid and the offer for the underlying stock are incorrect, it is difficult to know what the price of the underlying stock might be. Assuming that either the bid or the offer is correct, but not both, the stock price probably ranges somewhere between \$20.92–\$21.22, which is three times wider than the original non-inverted quote.

If a CBOE market maker believes that the bid for the underlying stock is correct and has a quote size of 25-up at \$1.25–\$1.35, assume he executes an incoming market order to sell at \$1.25. Now assume that the price of the underlying stock corrects to \$20.92–\$21.02, sending the market maker's quote to \$1.05–\$1.15, and that the market maker receives an incoming market order to buy, which he executes at \$1.15. Under these circumstances, the market maker has purchased the options (*i.e.*, the market maker was on the contra side of the first market order to sell) at \$1.25 and sold the options (*i.e.*, the market maker was on the contra side of the second market order to buy) at \$1.15, locking in a loss of \$0.10, 25 times.

b. Underlying Market Reports a Trade Outside of the Disseminated Quote

According to the CBOE, it is not uncommon for the primary market for an underlying security, in its haste to report trades to the tape, to report trades before changing the disseminated quote, resulting in a transaction that falls outside of the disseminated quote. For example, assume that the disseminated quote for a stock is \$22.10–\$22.25 and that the last sale was \$22.15. Without a change in the quote the next sale is reported at \$22. In this instance, the market for the underlying security could come out in any direction, *i.e.*, it could be \$21.75–\$22, it could be unchanged, or it could be \$22.00–\$22.25. As in the previous example, the CBOE market maker must attempt to guess where the market for the underlying security will come out. If the market maker guesses incorrectly, he has exposure. Allowing the market maker to widen his quote allows him a measure of protection until the market for the underlying security again reports trades within the disseminated quote.

2. Statutory Basis

The Exchange believes 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.¹⁶ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁷ requirements that the rules of an exchange be 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 CBOE 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.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

(A) By order approve such proposed rule change, or,

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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 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–CBOE–2003–25 and should be submitted by December 10, 2003.

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

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 03–28850 Filed 11–18–03; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–48774; File No. SR–CSE–2003–12]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by The Cincinnati Stock Exchange, Inc. and Amendment No. 1 To Change Its Name to National Stock Exchange

November 12, 2003.

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 5, 2003, The Cincinnati Stock Exchange, Inc. ("CSE" 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 CSE. On November 12, 2003, the Exchange filed an amendment to the proposed rule change.³ The Exchange filed the proposal pursuant to Section 19(b)(3)(A)(iii) of the Act⁴ and has designated the proposed rule change as one being concerned solely with the administration of the Exchange under Rule 19b–4(f)(3) of the Act,⁵ which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comment on the proposed rule

¹⁸ 17 CFR 200.30–3(a)(12).

¹ 15 U.S.C. 781(b)(1).

² 17 CFR 240.19b–4.

³ See November 12, 2003 letter from Jennifer M. Lamie, Assistant General Counsel and Secretary, CSE, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission ("Amendment No. 1"). In Amendment No. 1, the CSE replaces "involves a member due, fee or other charge" with "is concerned solely with the administration of the Exchange" in Item III below, to bring it into conformity with Rule 19b–4(f)(3) under the Act. 17 CFR 240.19b–4(f)(3).

⁴ 15 U.S.C. 781(b)(3)(A)(iii).

⁵ 17 CFR 240.19b–4(f)(3).

¹⁶ 15 U.S.C. 78(f).

¹⁷ 15 U.S.C. 78(f)(b)(5).