

as the Commission may designate if consistent with the protection of investors and the public interest. The Exchange has provided the Commission with written notice of its intent to file the proposed rule change, at least five business days prior to the filing date. Therefore, the proposed rule change has become effective pursuant to section 19(b)(3)(A) of the Act<sup>8</sup> and rule 19b-4(f)(6) thereunder.<sup>9</sup>

A proposed rule change filed under rule 19b-4(f)(6)<sup>10</sup> does not become operative prior to 30 days after the date of filing or such shorter time as the Commission may designate if such action is consistent with the protection of investors and the public interest. The CBOE has requested that the Commission accelerate the implementation of the proposed rule change so that it may take effect prior to the 30 days specified in rule 19b-4(f)(6)(iii).<sup>11</sup> The Commission believes that waiving the 30 day operative delay is consistent with the protection of investors and the public interest and, therefore, has determined to allow the proposed rule change to become effective and operative as of the date of filing with the Commission.<sup>12</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission 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.

#### 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 CBOE. All submissions should refer to File No. SR-CBOE-2002-47 and should be submitted by September 27, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 02-22655 Filed 9-5-02; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46436; File No. SR-CHX-2002-20]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 Thereto by The Chicago Stock Exchange, Incorporated Relating to Automatic Execution of Orders and Execution Prices

August 29, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice hereby is given that on July 11, 2002, the Chicago Stock Exchange, Incorporated ("CHX" or "Exchange") filed with the Securities and Exchange Commission (the "Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the self-regulatory organization. On August 12, 2002, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>3</sup> On August 27, 2002, the Exchange filed Amendment No. 2 to the proposed rule change.<sup>4</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

<sup>13</sup> 17 CFR 200.30(a)(12).

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

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

<sup>3</sup> See letter from Kathleen M. Boege, Associate General Counsel, CHX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated August 9, 2002 ("Amendment No. 1").

<sup>4</sup> See letter from Kathleen M. Boege, Assistant General Counsel, CHX, to Nancy J. Sanow, Assistant Director, Division, Commission, dated August 23, 2002 ("Amendment No. 2").

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

The Exchange proposes to amend Article XX, Rule 37 of the CHX Rules, which governs, among other things, automatic execution of market and marketable limit orders. Below is the text of the proposed rule change. Proposed new language is italicized; deletions are bracketed.

#### Article XX

#### Guaranteed Execution System and Midwest Automated Execution System

RULE 37(a). Guaranteed Executions.

\* \* \* \* \*

1. Eligible Orders. Specialists must accept and guarantee execution of all agency *market and marketable limit* orders [in Dual Trading System issues] from 100 *through* [up to and including] 5099 shares in accordance with this rule. [Specialists must accept and guarantee execution of all agency market orders or marketable limit orders in NASDAQ/NM Securities from 100 up to and including 5099 shares in accordance with this rule. Specialists must accept all agency limit orders in NASDAQ/NM Securities from 100 up to and including 10,000 shares for placement in the limit order book.]

2. *Market and Marketable Limit Orders. Any market or marketable limit order executed automatically shall be executed at the BBO price or better. With respect to any market or marketable limit order not executed automatically, a specialist shall be obligated to either (a) manually execute such order at a price and size equal to or better than the NBBO price and size at the time the order was received; or (b) act as agent for such order in seeking to obtain the best available price for such order on a marketplace other than the Exchange, using order routing systems where appropriate.* [Subject to the requirements of the short sale rule and the limitations of Rule 43(d) of this Article, all agency market orders must be filled on the basis of the size and price associated with the best bid among the American, Boston, Cincinnati, Chicago, New York, Pacific, Philadelphia or the Intermarket Trading System/Computer Assisted Execution System ("ITS/CAES") quote ("ITS Best Bid") on a sell order or the size and price associated with the best offer among the American, Boston, Cincinnati, Chicago, New York, Pacific, Philadelphia or the ITS/CAES quote ("ITS Best Offer") on a buy order (the "ITS Best Bid" and "ITS Best Offer" are collectively referred to as the "ITS

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

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

<sup>10</sup> *Id.*

<sup>11</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>12</sup> For purposes of accelerating the implementation of the proposed rule change only, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

BBO"); provided, however, for NASDAQ/NM Securities, all agency market orders must be filled on the basis of the price and size associated with the best bid disseminated pursuant to SEC Rule 11Ac1-1 on a sell order or price and size associated with the best offer disseminated pursuant to SEC Rule 11Ac1-1 on a buy order (collectively, the "NBBO"); or, if the specialist is quoting at the NBBO, based on the size associated with the specialist's bid or offer and the auto-execution threshold designated by the specialist.]

3-7. No change to text.

(b) Automated Executions. The Exchange's Midwest Automated Execution System (the MAX System) may be used to provide an automated delivery and execution facility for orders that are eligible for automatic execution on the Exchange. [under the Exchange's BEST Rule (Article XX, Rule 37(a)) and certain other orders. In the event that an order that is subject to the BEST Rule is sent through MAX, it shall be executed in accordance with the parameters of the BEST Rule and the following. In the event that an order that is not subject to the BEST Rule is sent through MAX, it shall be executed in accordance with the parameters of the following:]

(1) Size. The MAX System has two size parameters which must be designated by the specialist on a stock-by-stock basis. These parameters are the auto-execution threshold and the auto-acceptance threshold. For both Dual Trading System issues and NASDAQ/NM Securities, the auto-execution threshold must be set at 300 shares or greater and the auto-acceptance threshold must be set at 1000 shares or greater. In no event may the auto-acceptance threshold be less than the auto-execution threshold. If the order sending firm sends an agency market order in a Dual Trading System issue through MAX, such order will be executed in accordance with paragraph (b)(6) of this Rule. If the order sending firm sends an agency market order in a Nasdaq/NM Security through MAX, such order shall be executed in accordance with paragraph (b)(7) of this Rule. *Notwithstanding the subsequent provisions of Rule 37(b) regarding automatic execution of orders, a specialist may elect, on an issue-by-issue basis, to limit the specialist's automatic execution exposure during a designated time period to a number of shares aggregated from multiple orders (the "Aggregate Share Threshold"). If a specialist makes this election, the MAX system will automatically execute orders in such issue until the Aggregate Share Threshold is reached and subsequent*

*orders will be directed to the specialist's book for manual execution during the remainder of the designated time period.*

\* \* \* \* \*

#### Interpretations and Policies:

.01—.09 No change in text.

.10 *For purposes of this Rule 37, "BBO price" shall mean the best bid or offer disseminated by a national market participant and reasonably accessible by the Exchange. "NBBO price" shall mean (a) for Dual Trading System issues, the best bid among the American, Boston, Cincinnati, Chicago, New York, Pacific, Philadelphia or the Intermarket Trading System/Computer Assisted Execution System ("ITS/CAES") quote ("ITS Best Bid") on a sell order or the best offer among the American, Boston, Cincinnati, Chicago, New York, Pacific, Philadelphia or the ITS/CAES quote ("ITS Best Offer") on a buy order (the "ITS Best Bid" and "ITS Best Offer" are collectively referred to as the "ITS BBO"); and (b) for NASDAQ/NM Securities, the price associated with the best bid disseminated pursuant to SEC Rule 11Ac1-1 on a sell order or price associated with the best offer disseminated pursuant to SEC Rule 11Ac1-1 on a buy order.*

\* \* \* \* \*

#### RULE 43.

\* \* \* \* \*

#### [(d) Manual Executions.

With respect to MAX System agency market or marketable limit orders in NASDAQ/NM Securities which have a size equal to or less than the auto-execution threshold but which are not auto-executed under the provisions of Rule 37(b)(7) of this article, a specialist shall be obligated to either (i) manually executed such orders at the NBBO in existence when the order is received or better, or (ii) act as agent for such orders in seeking to obtain the best available price for such orders on a marketplace other than the Exchange. A specialist acting as agent pursuant to subparagraph (ii) above shall use order routing systems where appropriate.]

\* \* \* \* \*

#### ARTICLE XXX

##### Specialists

\* \* \* \* \*

#### Precedence to Orders in the Book

##### RULE 2.

\* \* \* \* \*

#### Interpretations and Policies:

.05 Interaction between professional limit orders and agency limit orders that are not professional orders ("Agency Orders").

In the event that a professional order "has the post," i.e., is the highest priority order in the specialist's book at a given price, the professional order is not required to yield precedence to an Agency Order at the same price that has not established time priority over the professional order. [Notwithstanding anything in the previous sentence to the contrary, in the event that such Agency Order is due a fill under the Exchange's Best Rule, that Agency Order shall be filled even though the professional order which had a higher priority on the book is not filled.]

\* \* \* \* \*

#### 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 regarding 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

The Exchange proposes to amend Article XX, Rule 37 and Rule 43 of the CHX Rules, which governs, among other things, automatic execution of market and marketable limit orders and execution prices due orders. The proposed amendments to Rules 37 and 43 are intended to modify a CHX specialist's order execution obligations to address post-decimalization market conditions, specifically the significant reduction in liquidity at each price point, including the national best bid and offer ("NBBO"). The CHX requests the Commission's approval of the proposed rule change on a pilot basis, for six months from the date of the Commission's approval order.

###### Background

New York Stock Exchange, American Stock Exchange and Nasdaq issues are traded on the CHX; each issue traded is assigned to a single specialist. The vast

majority of orders received by a CHX specialist are routed from order-sending firms via the Exchange's MAX® system, which provides for the electronic routing and automatic execution of orders.

To provide order-sending firms with an incentive to route orders to our market, the CHX, like most regional exchanges, has what is referred to at the CHX as the "BEST Rule." The BEST Rule provides that if a specialist accepts an order (or in actuality the MAX system accepts the order for the specialist), the specialist generally must execute the order at the NBBO price up to the NBBO displayed quantity, *i.e.*, the best price and liquidity available in the national market system.

In addition to the BEST Rule that governs execution prices, the CHX rules also provide for automatic execution of orders, *i.e.*, without manual intervention by the CHX specialist, if certain conditions are met.<sup>5</sup> In order to manage his position and prudently limit his auto-execution exposure, each CHX specialist designates an "auto-execution threshold" for each issue.<sup>6</sup> The auto-execution threshold is a number of shares, greater than 99 shares that the specialist is willing to execute automatically.

Although a specialist can set his auto execution threshold in a variety of ways, a fairly typical setting would be to automatically execute all orders, in a particular issue, of 599 shares or less regardless of the quantity offered at the BBO and automatically execute orders up to 1099 shares provided that order size does not exceed the BBO displayed quantity. If an order exceeds the specialist's auto-execution threshold, the order is automatically directed into the specialist's book for manual execution, unless the order-sending firm has elected to receive partial automatic executions, in which case a portion of the order will automatically execute, up to the size of the auto-execution threshold, and the balance of the order will be placed in the specialist's book for manual execution.<sup>7</sup> Significantly, under the current version of the CHX rules, manual execution generally does not excuse a specialist from his or her BEST Rule obligations; an order executed manually must be executed at the NBBO price up to the NBBO displayed quantity unless the specialist

can demonstrate the existence of unusual trading conditions.<sup>8</sup>

#### Issue

Under the current version of the CHX rules, a CHX specialist has unlimited (and the CHX believes unwarranted) auto-execution exposure, because a rapid succession of orders entered into the MAX system at or below the specialist's auto-execution threshold are due an automatic fill at the prevailing NBBO price. For example, if a specialist set the auto-execution threshold as described in the preceding paragraph, and the NBBO was 600 shares offered at \$30.00, the specialist would be obligated to automatically execute 10 500-share market orders to buy at \$30.00 if those orders were rapidly sent by one or more customers while the NBBO remained unchanged. The specialist, who intended to offer price and liquidity equivalent to the best market, instead provided 4400 additional shares of liquidity.

The problem of providing more than the intended amount of liquidity through automatic executions has grown more acute since the conversion to decimal trading. The availability of liquidity at a price point has become a more significant factor in order routing decisions. While the quantity offered at the NBBO has generally declined since the conversion to decimals, this consequence can be easily avoided by rapidly submitting a succession of small orders eligible for automatic execution at the NBBO price to a CHX specialist. The specialist, if he chooses to offset the position in another market, however, will encounter the limited liquidity that drove the order sender to take advantage of the specialist's auto execution of orders and the liquidity it provides.

#### Proposal

After careful consideration of the issue by the leaders of the CHX Listed Specialist Product Subcommittee, OTC Specialist Product Subcommittee, Rules Subcommittee and Committee on Floor Procedure, the CHX proposes amendment of Article XX, Rule 37 to address the foregoing issue. Specifically, the CHX believes that in today's decimal trading environment, where it is very difficult to find liquidity at the NBBO

price point and the NBBO price is constantly "flickering," it is appropriate for a specialist to limit his or her aggregate auto-execution and BEST Rule liability to the then-current and accessible NBBO price and size. In other words, the specialist's auto-execution threshold would no longer constitute a guarantee of automatic execution of an unlimited number of orders at the NBBO price. CHX proposes below two principal changes to CHX Article XX, Rule 37, which CHX seeks to incorporate into its rules and which a specialist could elect to enable.

#### 1. Changes to BEST Rule and Calculation of BBO

Under the proposed revision to CHX Article XX, Rule 37(a), a CHX specialist would no longer be obligated to provide the NBBO price for every order accepted by the specialist. Instead, the proposed rule change incorporates revised standards for handling orders; these standards are taken directly from the Commission's order-handling rules.<sup>9</sup> Under these revised standards, automatically executed orders must be executed at the "BBO price" or better.<sup>10</sup> "BBO price" is defined in proposed Interpretation and Policy .10 to CHX Rule 37 as the best bid or offer disseminated by a national market participant reasonably accessible by the CHX. Specialists will continue to be obligated to manually execute all orders not eligible for automatic execution at a price equal to or better than the NBBO price at the time the order was received, or act as agent for the order in seeking the best-available price in the marketplace.<sup>11</sup>

Significantly, the revised order-handling standards will continue to be subject to surveillance by the CHX Department of Market Regulation and

<sup>9</sup> See Order Execution Obligations Release, Securities Exchange Act Release No. 37619A (September 6, 1996), 61 FR 48290 (September 12, 1996), which notes, among other things, that " \* \* \* the duty of best execution requires a broker-dealer to seek the most favorable terms reasonably available under the circumstances for a customer's transaction." Order Execution Obligations Release at 48322.

<sup>10</sup> The Exchange represents that this proposal, like the proposed change to the BEST Rule guarantee, is taken from the Commission's Order Handling Release. See Order Execution Obligations Release at 48323 (noting that quotations must be taken into account by broker-dealers if reasonably available).

<sup>11</sup> See Amendment No. 2, *supra* note 4. Importantly, the Commission has already approved this execution standard for the Exchange's rules that apply to the execution of orders in Nasdaq/NM securities. See CHX Article XX, Rule 43(d); Securities Exchange Act Release No. 37369 (June 25, 1996), 61 FR 34462 (July 2, 1996). This proposal, then, simply would extend this standard to the handling of orders in listed securities.

<sup>5</sup> See CHX Article XX, Rule 37(b)(6)(automatic execution of orders in listed securities); CHX Article XX, Rule 37(b)(7)(automatic execution of orders in OTC securities).

<sup>6</sup> See CHX Article XX, Rule 37(b)(1).

<sup>7</sup> See CHX Article XX, Rule 37(b)(6) and (7).

<sup>8</sup> The other exception to this rule occurs in the trading of Nasdaq/NM securities. CHX Article XX, Rule 43(d) provides that, when an order that is of a size less than or equal to the specialist's auto-execution threshold is not automatically executed, the specialist must either "(1) manually execute such orders at the NBBO in existence when the order is received or better, or (2) act as agent for such orders in seeking to obtain the best available price for such orders on a marketplace other than the Exchange."

members will remain subject to discipline for violations of CHX Article XX, Rule 37(a). But the Exchange believes that the rule revision, particularly with a more realistic definition of BBO price, will permit specialists to meet their order handling obligations without being subject to BEST Rule guarantees that, according to the Exchange, are sometimes impossible to satisfy in today's post-decimalization environment.

## 2. Incorporation of Aggregate Share Threshold Into Automatic Execution Rules

This second proposal would amend CHX Article XX, Rule 37(b) to limit a specialist's unintended automatic execution liability by incorporating an Aggregate Share Threshold into the specialist's designated auto-execution parameters. The Aggregate Share Threshold could be enabled by a specialist on an issue-by-issue basis. This functionality would be entirely optional, however, and a specialist could still elect to provide additional liquidity guarantees. Under this voluntary systems enhancement, the specialist would agree to auto-execution (at the BBO price) of an aggregate number of shares (the "Aggregate Share Threshold"). Once an aggregate number of shares equal to the Aggregate Share Threshold was automatically executed, whether as a result of one order or numerous orders, subsequent orders would be directed into the specialist's book for manual execution. Under the proposed rule change, these subsequent orders would not necessarily be due a fill at the BBO price, but would be subject to the specialist's best execution obligation under revised Rule 37(a). The specialist could act as agent to obtain the best available price on a marketplace other than the Exchange or could voluntarily elect to fill the order at the BBO price. The Aggregate Share Threshold would reset after a prescribed amount of time designated by a specialist<sup>12</sup> and could never be set at a level less than the shares included in the specialist's own bid or offer.

The following examples illustrate how the automatic executions would work. They assume that the specialist has set his or her Aggregate Share Threshold at a level equal to the size at the prevailing NBBO.

*Example 1:* NBBO is 2000 shares offered at 30.

<sup>12</sup> A specialist choosing to enable the Aggregate Share Threshold functionality would be required to provide CHX staff with the designated time increment for each issue. The time increment would commence (and restart) upon any change in the NBBO.

Specialist has designated Aggregate Share Threshold of 2000 shares.

MAX accepts 5 500-share buy market orders.

*Outcome:* 4 orders executed automatically upon receipt at 30. 1 order is directed into the specialist's book for manual execution.

*Example 2:* NBBO is 2000 shares offered at 30 at 12:00:00.

Specialist has designated Aggregate Share Threshold of 2000 shares.

The Aggregate Share Threshold is calibrated to reset after 15 seconds. MAX accepts 5 500 share buy market orders between 12:00 and 12:00:15. NBBO remains at 2000 shares offered at 30 at 12:00:15.

MAX accepts 1 500-share buy market order at 12:00:17.

NBBO remains at 2000 shares offered at 30 at 12:00:17.

*Outcome:* 4 orders received between 12:00:00 and 12:00:15 execute automatically upon receipt. 5th order received between 12:00:00 and 12:00:15 is directed into the specialist's book for manual execution.

The 500-share buy market order received at 12:00:17 executes automatically upon receipt.

*Example 3:* NBBO is 2000 shares offered at 30 at 12:00:00.

Specialist has designated Aggregate Share Threshold of 2000 shares.

The Aggregate Share Threshold is calibrated to reset upon a change in the NBBO.

MAX accepts 5 500-share buy market orders between 12:00:00 and 12:00:10.

NBBO remains at 2000 shares offered at 30 at 12:00:10.

NBBO changes to 1000 shares offered at 30 at 12:00:11.

MAX accepts 2 500-share market buy orders at 12:00:12.

NBBO remains 1000 shares offered at 30 at 12:00:12.

*Outcome:* 4 orders received between 12:00:00 and 12:00:10 execute automatically upon receipt. 5th order received between 12:00:00 and 12:00:10 is directed into the specialist's book for manual execution.

2 500-share market buy orders received at 12:00:12 execute automatically upon receipt.

The CHX believes that these two proposed rule changes would be sufficient to address the unintended adverse consequences of current CHX rules relating to auto-execution liquidity and price guarantees. It is important to note that neither of the proposed changes would operate to discriminate

against order-sending firms in any way; operation of these changes to the MAX system would be enabled on an issue-by-issue basis and would apply equally to all order-sending firms. Similarly, the Exchange believes that the intended outcome of the MAX changes would not have a disparate impact on any order-sending firm or class of firm.

The CHX would further note that in today's market environment, where specialists are required to make public their quality-of-execution statistics and broker-dealers are bound as fiduciaries to make order-routing decisions in accordance with best execution practices, there exist sufficient market-based incentives for specialists to continue to provide execution prices and liquidity akin to the best available in the national market. These incentives render a rule-based requirement largely obsolete, and amply support the rule changes proposed herein.

## 2. Statutory Basis

The proposed rule is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of section 6(b) of the Act.<sup>13</sup> In particular, the proposed rule is consistent with section 6(b)(5)<sup>14</sup> in that it is designed to promote just and equitable principles of trade, to remove impediments and to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

### B. Self-Regulatory Organization's Statement of Burden on Competition

The Exchange does not believe that the proposed rule change will impose any inappropriate burden on competition.

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

No written comments were either 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 other 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

<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

(ii) as to which he self-regulatory organization consents, the Commission will:

(A) By order approve the 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 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-CHX-2002-20 and should be submitted by September 27, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

**Margaret H. McFarland,**  
Deputy Secretary.

[FR Doc. 02-22654 Filed 9-5-02; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46430; File No. SR-PCX-2002-52]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment Nos. 1 and 2 Thereto by the Pacific Exchange, Inc. Relating to Changes in Its Marketing Fee Program

August 29, 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 August 5,

2002, the Pacific Exchange, Inc. ("PCX" or "Exchange") 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 the PCX. PCX filed Amendment No. 1 to the proposed rule change on August 23, 2002.<sup>3</sup> PCX filed Amendment No. 2 to the proposed rule change on August 28, 2002.<sup>4</sup> 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

PCX proposes to limit the number of equity option issues to which marketing fees may apply to only those that are ranked in the 250 most actively traded equity options. The Exchange is also proposing to require that PCX Lead Market Makers who make payments to order flow providers as part of the Exchange's marketing fee program make, keep current, and preserve records relating to marketing fee arrangements and make those records available to the PCX upon request for inspection and review. The text of the proposed rule change is below; new language is italicized.

\* \* \* \* \*

#### Schedule of Fees and Charges for Exchange Services

PCX Options: Trade-Related Charges

\* \* \* \* \*

<sup>3</sup> Amendment No. 1 replaces the original filing in its entirety. In Amendment No. 1, the Exchange revised the description of the proposed rule change to conform to the proposed rule text and to provide greater detail, referenced the Exchange's pre-filing with the Commission, requested that the Commission waive the 30 day operative period so that the proposal may become operative on August 29, 2002, clarified how the top 250 most actively traded equity options will be selected, and added proposed rule text as exhibits.

<sup>4</sup> In Amendment No. 2, the Exchange revised the proposed rule text to delete the requirement that the required records include records pertaining to the "origin, use, transfer, distribution and amounts of all payments to order flow providers" and added the requirement that the required records be maintained in such a fashion to permit the Exchange to track payments to order flow providers "on the basis of payment (whether on a per contract or flat fee basis)." Because the Form 19b-4 submitted on August 5, 2002 was not complete, the proposed rule change was not considered filed. The proposed rule change became effective on August 28, 2002, the date on which Amendment No. 2 was filed with the Commission.

Marketing Charge Eligible Issues	Rates Variable—See separate schedule Top 250 most active nationally traded issues
Cap on Marketing .....	\$200 per trade Charge

\* \* \* \* \*

**Pacific Exchange, Inc**  
**Rules of the Board of Governors**

#### Market Maker Marketing Reports and Record Keeping

Rule 6.41(a) No Change.  
(b) *Marketing Charges Record Keeping—Lead Market Makers who make payments to order flow providers as part of the Exchange's marketing charges program, must make, keep current and preserve all books and records relating to marketing charges arrangements, including but not limited to all records pertaining to the identity of the order flow providers. Such records must be maintained in such a fashion as to permit the Exchange to track payments to order flow providers on the basis of payment (whether on a per contract or flat fee basis). Such books and records must be made available to the Exchange upon request.*

#### 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 PCX 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 PCX 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

On August 31, 2000, the PCX began collecting a marketing fee of \$0.40 per contract on all equity options traded at the PCX.<sup>5</sup> On August 31, 2001, the Exchange modified its marketing fee program in order to collect marketing fees ranging from \$0 to \$1.00 per contract on a per-issue basis.<sup>6</sup> The

<sup>5</sup> See Securities Exchange Act Release No. 43290 (September 13, 2000), 65 FR 57213 (September 21, 2000).

<sup>6</sup> See Securities Exchange Act Release No. 44830 (September 21, 2001), 66 FR 49728 (September 28, 2001).

<sup>15</sup> 17 CFR 200.30-3(a)(12).

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

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