

option classes for a brief or sometimes lengthy time period. Thus, CBOE strongly encouraged, and now requires, that members have CBOE's AutoQuote system ready as a back-up should a proprietary system fail. The Exchange also proposes to add subparagraph (g)(10) to CBOE Rule 17.50—Imposition of Fines for Minor Rule Violations, to incorporate in its Minor Rule Violation Plan violations of new Rule 8.85(a)(xi).

### III. Discussion

The Commission finds that the proposed rule change, as amended, is consistent with section 6 of the Act<sup>5</sup> and the rules and regulations thereunder applicable to a national securities exchange. In particular, the Commission finds that the proposed rule change is consistent with section 6(b)(5) of the Act<sup>6</sup> which requires, among other things, that the rules of the 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. The proposed rule change is also consistent with section 6(b)(6) of the Act,<sup>7</sup> which generally requires that the Exchange provide for the appropriate discipline of its members, and Rule 19d-1(c)(2) under the Act,<sup>8</sup> which governs minor rule violation plans.

The proposed rule change removes impediments to and perfects the mechanism of a free and open market because by requiring members of the Exchange to maintain CBOE's AutoQuote system as a back-up, the Exchange provides a mechanism for ensuring the smooth and uninterrupted operation of the Exchange in the event of a failure by a member's proprietary autoquote system. Without CBOE's AutoQuote system in place as a back-up, the Exchange might be unable to open trading for an entire group of listed option classes if a proprietary autoquote system fails. Requiring members to maintain CBOE's AutoQuote system as a back-up would avoid such disruptions, which in turn would benefit investors and the public interest.

The Commission also finds that adding Rule 8.85(a)(xi) to the list of violations included in the Exchange's Minor Rule Violation Plan ("Plan") is consistent with requirements of Section 6(b)(6) of the Act<sup>9</sup> because it provides an additional option for the appropriate

discipline of Exchange members. The Commission notes that while the Plan provides the Exchange with the option of proceeding under the Plan against a member found to be in violation of a rule included in the Plan, the Exchange must continue to conduct surveillance of its members and ensure their compliance with the Exchange's rules, and to proceed with formal disciplinary action if a particular case warrants such action. Finally, the Commission finds that the addition of Rule 8.85(a)(xi) to the list of violations included in the Exchange's Plan is consistent with Rule 19d-1(c)(2) under the Act,<sup>10</sup> which governs minor rule violation plans because the Plan provides an efficient means to punish violations of Exchange rules, consistent with the public interest and the protection of investors.

### IV. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,<sup>11</sup> that the proposed rule change (SR-CBOE-2002-30), as amended, is approved.

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

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

[FR Doc. 02-29315 Filed 11-18-02; 8:45 am]

**BILLING CODE 8010-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46814; File No. SR-ISE-2002-23]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the International Stock Exchange, Inc. To Amend Rule 720 Regarding Options Priced Under \$3.00

November 12, 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 October 16, 2002, the International Stock Exchange, Inc. ("ISE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this

notice to solicit comments on the proposed rule change.

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

The Exchange is proposing to amend Rule 720 (the "Obvious Error Rule") as it pertains to transactions in options priced under \$3.00. The text of the proposed rule change is set forth below. Proposed new language is *italicized*; proposed deletions are in brackets.

\* \* \* \* \*

#### Rule 720. Obvious Errors

The Exchange shall either bust a transaction or adjust the execution price of a transaction that results from an Obvious Error as provided in this Rule.

(a) Definition of Obvious Error. For purposes of this Rule only, an Obvious Error will be deemed to have occurred when:

(1) if the Theoretical Price of the option is less than \$3.00[.];

(i) *during regular market conditions (including rotations)* the execution price of a transaction is higher or lower than the Theoretical Price for the series by an amount of [25] 35 cents or more; or

(ii) *during fast market conditions (i.e., the Exchange has declared a fast market status for the option in question), the execution price of a transaction is higher or lower than the Theoretical Price for the series by an amount of 50 cents or more.*

(2) if the Theoretical Price of the option is \$3.00 or higher:

(i) during regular market conditions (including rotations), the execution price of a transaction is higher or lower than the Theoretical Price for the series by an amount equal to at least two (2) times the maximum bid/ask spread allowed for the option, so long as such amount is 50 cents or more; or

(ii) *during fast market conditions (i.e., the Exchange has declared a fast market status for the option in question), the execution price of a transaction is higher or lower than the Theoretical Price for the series by an amount equal to at least three (3) times the maximum bid/ask spread allowed for the option, so long as such amount is 50 cents or more.*

\* \* \* \* \*

### 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 the proposed rule change and discussed any comments it received on the proposed

<sup>5</sup> 15 U.S.C. 78f.

<sup>6</sup> 15 U.S.C. 78f(b)(5).

<sup>7</sup> 15 U.S.C. 78f(b)(6).

<sup>8</sup> 17 CFR 240.19d-1(c)(2).

<sup>9</sup> 15 U.S.C. 78f(b)(6).

<sup>10</sup> 17 CFR 240.19d-1(c)(2).

<sup>11</sup> 15 U.S.C. 78s(b)(2).

<sup>12</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.

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

On June 25, 2002, the Commission approved an amendment to the ISE Rule 720 ("June Amendment"),<sup>3</sup> which gives the Exchange authority to bust or adjust trades that result from an obvious error based upon objective standards for determining the circumstances under which a trade should be adjusted or busted. In the June Amendment, the Exchange changed the standard for determining the existence of an obvious error for options series trading under \$3.00. Specifically, the June Amendment provided that an obvious error would be deemed to have occurred if the difference between the execution price and the theoretical price is at least \$.25. The June Amendment did not change ISE Rule 720 with respect to options trading at or above \$3.00, which requires the difference between the execution price and theoretical price of an option be at least twice the allowable spread in normal market conditions and three times the allowable spread in fast market conditions.

The Exchange's experience since the June Amendment indicates that a difference of only \$.25 is too low and may allow trades that are not obviously erroneous to qualify for obvious error treatment. In addition, the June Amendment did not provide for a larger difference between the execution price and the theoretical price during fast market conditions, as is the case for options price at and above \$3.00. Accordingly, the Exchange proposes to increase the amount by which the execution price of an option priced under \$3.00 must differ from the theoretical price from \$.25 to \$.35 in normal market conditions, and to provide that the difference must be at least \$.50 in fast market conditions. This proposal will allow fewer executions to qualify as obvious errors, and therefore fewer situations where a trade may be busted or adjusted under ISE Rule 720.

The ISE developed Rule 720 to address the need to handle errors in a fully electronic market where orders and quotes are executed automatically before an obvious error may be

discovered and corrected by ISE members. In formulating ISE Rule 720, the Exchange has weighed carefully the need to assure that one market participant is not permitted to receive a windfall at the expense of another market participant that made an obvious error, against the need to assure that market participants are not simply being given an opportunity to reconsider poor trading decisions. This proposed rule change reflects the Exchange's constant evaluation of the obvious error rule and its fairness to all market participants.

2. Statutory Basis

The Exchange believes that the proposal is consistent with section 6(b) of the Act<sup>4</sup> in general and furthers the objectives of section 6(b)(5)<sup>5</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, 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 that is not necessary or appropriate in furtherance of the purposes of the Exchange Act.

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

The Exchange has neither solicited nor received comments on 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>6</sup> and Rule 19b-4(f)(6)<sup>7</sup> thereunder because the proposal: (i) Does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) does not become operative prior to 30 days after the date of filing or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest. In addition, the Exchange provided the Commission with written notice of its intent to file the proposed

rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of the filing the proposed rule change as required by Rule 19b-4(f)(6). In addition, the Exchange provided the Commission with written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of the filing the proposed rule change as required by Rule 19b-4(f)(6). 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 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.

The ISE has requested that the Commission waive the 30-day operative delay. The Commission believes waiving the 30-day operative delay is consistent with the protection of investors and the public interest. The Commission believes that it is reasonable for the ISE, based upon its experience in administering the Rule, to amend the Rule to state that the standard for determining the existence of an obvious error for options series trading at less than \$3.00 be whether, in regular market conditions, the difference between the execution price and the theoretical price for the series is at least \$.35, and whether, during fast market conditions, the difference between the execution price and the theoretical price for the series is at least \$.50. The Commission notes that the proposal refines the June Amendment, which itself was noticed for public comment and received no comment. For these reasons, the Commission designates the proposal to be effective and operative as of the date of this order.<sup>8</sup>

**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

<sup>4</sup> 15 U.S.C. 78f(b).

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

<sup>6</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>7</sup> 17 CFR 240.19b-4(f)(6).

<sup>8</sup> For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>3</sup> See Securities Exchange Act Release No. 46110 (June 25, 2002), 67 FR 44487 (July 2, 2002).

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-ISE-2002-23 and should be submitted by December 10, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>9</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 02-29243 Filed 11-18-02; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46819; File No. SR-MSRB-2002-10]

### Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of the Proposed Rule Change Relating to Rule G-14, on Reports of Sales or Purchases

November 12, 2002.

On September 24, 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> the Municipal Securities Rulemaking Board ("Board" or "MSRB") filed with the Securities and Exchange Commission ("Commission" or "SEC") a proposed rule change (File No. SR-MSRB-2002-10). The proposed rule change relates to MSRB Rule G-14, on reports on sales or purchases, by lowering the trade per day threshold for frequently traded municipal securities.

The Commission published the proposed rule change for comment in the **Federal Register**, October 18, 2002.<sup>3</sup> The Commission did not receive any comment letters relating to the forgoing proposed rule change.

### I. Description of the Proposed Rule Change

The MSRB filed with the Commission the proposed rule change relating to Rule G-14, on reports of sales or purchases, to increase transparency in the municipal securities market. The Board has a long-standing policy to increase price transparency in the municipal securities market, with the ultimate goal of disseminating comprehensive and contemporaneous pricing data. One product of the Board's Transaction Reporting Program is its Daily Transaction Report, which has been provided to subscribers each day since January 2000. The report is made available each morning by 7 am and includes details of transactions in municipal securities which were "frequently traded" the previous business day. From the beginning of the Transaction Reporting Program in 1994 through the spring of 2002, "frequently traded" securities were defined as those that were traded four or more times on a given business day. In May 2002, the Board defined "frequently traded" securities as those that were traded three or more times on a given day.<sup>4</sup>

When transparency was initially being introduced into the municipal securities market, the Board was concerned that an observer unfamiliar with the market might mistake an isolated reported transaction or pair of transactions as providing a reliable indicator of "market price." Because of this concern, the Board adopted the "frequently traded" threshold of four trades. At the same time, the Board has made a commitment to review the use of these reports as experience is obtained and eventually to move to transparency reporting on a more contemporaneous and comprehensive basis.<sup>5</sup>

Since 1994, the Board has made ongoing efforts to increase price transparency in the municipal securities market in measured steps, culminating in comprehensive, real-time price transparency. The first price transparency report, begun in 1995, was a report, published the day after trading

("T+1"), that summarized inter-dealer trades in frequently traded municipal securities. In 1998, the Board added customer trades to the T+1 summary reports, and in January 2000 began, as well, to publish individual transaction data on frequently traded securities. The Board has also introduced "comprehensive" transaction reports for this market, which list all municipal securities transactions (regardless of frequency of trading), but which are available no less than one week after trade date.<sup>6</sup>

At this time, the Board believes that the next appropriate step in this process is to change the threshold for determining that information about a municipal security is to be disseminated in the T+1 Daily Transaction Report. The proposed rule change would lower the threshold from three to two trades per day.

### Impact of Proposed Report on Transparency

The proposed threshold would increase substantially the proportion of municipal securities market activity that is reported on the day after trading. On a typical day, there are approximately 26,000 transactions in about 10,000 issues, with a total par value traded of about \$9.5 billion. The present Daily Transaction Report, with a threshold of three or more trades per day, includes an average of 14,400 trades in 2,600 different issues, with a total par value of about \$5.2 billion. Under the proposed threshold, the report is expected to include an average of 19,760 trades in 5,600 issues, with a total par value of about \$7.7 billion. This represents a 37 percent increase in the number of trades reported, a more-than-twofold increase in the number of issues reported, and a 48 percent increase in par value reported.<sup>7</sup>

### Description of Service

The enhanced Daily Transaction Report with the two-trade threshold will replace the current report and will be made available each day to subscribers via the Internet. Subscribers to the current Service receive the report free of charge, and their subscriptions will continue should the proposed Service be implemented. New subscriptions will be available free to parties who sign a subscription agreement. In addition,

<sup>6</sup> The first comprehensive report was introduced in October 2000 and listed all trades after a one-month delay. The latest comprehensive report began operation in August 2002 and has a one-week delay. See Release No. 34-46380 (August 19, 2002) 67 FR 54831-54832.

<sup>7</sup> Data is based upon market activity from April 1, 2001 through July 31, 2001.

<sup>9</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.

<sup>3</sup> See Release No. 34-46636 (October 10, 2002) 67 FR 64435.

<sup>4</sup> See Release No. 34-45861 (May 1, 2002) 67 FR 30989-30990.

<sup>5</sup> See, e.g., "Board to Proceed with Pilot Program to Disseminate Inter-Dealer Transaction Information," *MSRB Reports*, Vol. 14, No. 1 (January 1994). In its approval order for the Inter-Dealer Daily Report, the Securities and Exchange Commission noted that the Board, in proceeding to subsequent levels of transparency, "should continue to work toward publicly disseminating the maximum level of useful information to the public while ensuring that the information and manner in which it is presented is not misleading." See Release No. 34-34955 (November 9, 1994) 59 FR 59810.