

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

**Jill M. Peterson,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49146; File No. 4-429]

### Joint Industry Plan; Order Approving Joint Amendment No. 8 to the Options Intermarket Linkage Plan Relating to Satisfaction Orders and Trade-Throughs

January 29, 2004.

#### I. Introduction

On December 18, 2003, December 22, 2003, December 29, 2003, and December 30, 2003, the International Securities Exchange, Inc. ("ISE"), the Pacific Exchange, Inc. ("PCX"), the American Stock Exchange LLC ("Amex"), the Philadelphia Stock Exchange, Inc. ("Phlx"), and the Chicago Board Options Exchange, Inc. ("CBOE") (collectively, the "Participants"), respectively submitted to the Securities and Exchange Commission ("SEC" or "Commission") in accordance with section 11A of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 11Aa3-2 thereunder,<sup>2</sup> a proposed amendment to the Options Intermarket Linkage Plan (the "Plan").<sup>3</sup> The amendment proposes to extend the pilot provision limiting trade-through liability to 10 contracts per satisfaction order at the end of the day for an additional five months, until June 30, 2004.

The proposed amendment to the Plan was published in the **Federal Register** on January 6, 2004.<sup>4</sup> No comments were received on the proposed amendment. This order approves the proposed amendment to the Plan.

#### II. Description of the Proposed Amendment

In Joint Amendment No. 8, the Participants propose to extend the pilot provision contained in section 8(c)(ii)(B)(2)(c) of the Plan that limits trade-through liability to 10 contracts per satisfaction order at the end of the day for an additional five months, until June 30, 2004, in order to gain more experience with the limitation on trade-through liability. Pursuant to the pilot, an exchange member's trade-through liability is limited to 10 contracts per Satisfaction Order for the period between five minutes prior to the close of trading in the underlying security and the close of trading in the options class.

#### III. Discussion

When this pilot was originally proposed in Joint Amendment No. 4 to the Plan,<sup>5</sup> the Participants represented to the Commission that their members had expressed concerns regarding their obligations to fill Satisfaction Orders (which arise after a trade-through<sup>6</sup>) at the close of trading in the underlying security. Specifically, the Participants represented that their members were concerned that they may not have sufficient time to hedge the positions they acquire.<sup>7</sup> The Participants stated that they believed that their proposal to limit liability for trade-throughs for the last five minutes of trading in the underlying security to the filling of 10 contracts per exchange, per transaction would protect small customer orders, but still establish a reasonable limit for their members' liability. The Participants further represented that the proposal should not affect a member's potential liability under an exchange disciplinary rule for engaging in a pattern or practice of trading through other markets under section 8(c)(i)(C) of the Plan.

The Commission approved the proposal for a one-year pilot<sup>8</sup> to give the Participants and the Commission an opportunity to evaluate: (1) The need for the limitation on liability for trade-

throughs near the end of the trading day; (2) whether 10 contracts per Satisfaction Order is the appropriate limitation; and (3) whether the opportunity to limit liability for trade-throughs near the end of the trading day leads to an increase in trade-throughs. In its approval order, the Commission requested that the Participants provide a report to the Commission at least sixty days prior to seeking permanent approval of the pilot program. The Commission specified that the report should include information about the number and size of trade-throughs that occur during the last seven minutes of the trading day, the number and size of Satisfaction Orders that Participants might be required to fill without the limitation on liability and how those amounts are affected by the limitation on liability, and the extent to which the Participants use the underlying market to hedge their options positions.<sup>9</sup>

In connection with the request in Joint Amendment No. 8 to extend the pilot for an additional five months until June 30, 2004, the Commission notes that the Participants represent that if they seek to make the limitations on trade-throughs permanent, they will submit the above-referenced report to the Commission no later than March 31, 2004. The Participants further represent in Joint Amendment No. 8 that each exchange plans to submit individual reports regarding the requested data and that these reports will detail the number of trade-throughs in the last seven minutes of options trading and the rest of the day, as well as the number and size of Satisfaction Orders that would have been filled absent the current exemption. In addition, the Participants represent that the reports will provide information on the extent to which the exchange's members hedge their options trading during the day as part of their overall risk management. Finally, the Participants represent that they will make every effort to provide specific information regarding their members' hedging at the end of the trading day.

After careful consideration, the Commission finds that the proposed amendment to the Plan seeking to extend the current pilot is consistent with the requirements of the Act and the rules and regulations thereunder. Specifically, the Commission finds that the proposed amendment to the Plan is consistent with section 11A of the Act<sup>10</sup> and Rule 11Aa3-2 thereunder,<sup>11</sup> in that extending the pilot, while the Participants gather and evaluate data

<sup>1</sup> 15 U.S.C. 78k-1.

<sup>2</sup> 17 CFR 240.11Aa3-2.

<sup>3</sup> On July 28, 2000, the Commission approved a national market system plan for the purpose of creating and operating an intermarket options market linkage proposed by the Amex, CBOE, and ISE. See Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000). Subsequently, upon request by the Phlx and PCX, the Commission issued orders to permit these exchanges to participate in the Plan. See Securities Exchange Act Release Nos. 43573 (November 16, 2000), 65 FR 70850 (November 28, 2000) and 43574 (November 16, 2000), 65 FR 70851 (November 28, 2000).

<sup>4</sup> See Securities Exchange Act Release No. 49010 (December 30, 2003), 69 FR 706.

<sup>5</sup> See Securities Exchange Act Release No. 47028 (December 18, 2002), 67 FR 79171 (December 27, 2002) (Notice of Proposed Joint Amendment No. 4).

<sup>6</sup> Trade-throughs occur when a broker-dealer executes its customer's order on one exchange at a price inferior to another exchange's disseminated quote.

<sup>7</sup> See letter from Michael Simon, Senior Vice President and General Counsel, ISE, to Annette Nazareth, Director, Division of Market Regulation, Commission, dated November 19, 2002.

<sup>8</sup> See Securities Exchange Act Release No. 47298 (January 31, 2003), 68 FR 6524 (February 7, 2003) (approval of pilot program on a 120-day basis); see also Securities Exchange Act Release No. 48055 (June 18, 2003), 68 FR 37869 (June 25, 2003) (approval of pilot program).

<sup>9</sup> *Id.*

<sup>10</sup> 15 U.S.C. 78k-1.

<sup>11</sup> 17 CFR 240.11Aa3-2.

relating to the effect of the operation of the pilot, is appropriate in the public interest, for the protection of investors and the maintenance of fair and orderly markets. Therefore, the Commission is extending the effectiveness of section 8(c)(ii)(B)(2)(c) of the Plan for an additional five months, until June 30, 2004.

#### IV. Conclusion

It is therefore ordered, pursuant to section 11A of the Act<sup>12</sup> and Rule 11Aa3-2 thereunder,<sup>13</sup> that the proposed Plan Amendment No. 8 is approved on a pilot basis until June 30, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

Jill M. Peterson,

Assistant Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49145; File No. SR-Amex-2004-03]

### Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the American Stock Exchange LLC Relating to the Extension of a Linkage Fee Pilot Program

January 29, 2004.

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 January 14, 2004, the American Stock Exchange LLC ("Exchange" or "Amex") filed with the Securities and Exchange Commission ("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 from interested persons and is approving the proposed rule change on an accelerated basis.

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

The Exchange proposes to extend for six (6) months, until July 31, 2004, the current pilot program regarding

transaction fees for trades executed through the intermarket options linkage (the "Linkage") on the Exchange.

The proposed fee schedule is available at the Exchange and at the Commission.

#### 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 Amex 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 III 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 Amex is proposing to extend for six (6) months, until July 31, 2004, the current pilot program establishing Exchange fees for Principal Orders ("P Orders") and Principal Acting As Agent Orders ("P/A Orders") executed through the Linkage. The fees in connection with the pilot program are scheduled to expire on January 31, 2004.<sup>3</sup> The fees charged by the Amex under the pilot program consist of a \$0.26 per contract transaction fee, a \$0.05 comparison fee, and a \$0.05 floor brokerage fee. In addition to the previously approved fees, Amex is proposing to subject incoming P and P/A orders for certain licensed index products to a licensing fee<sup>4</sup> as part of the pilot.<sup>5</sup> These are the same fees charged to specialists and Registered Options Traders ("ROTs") for transactions executed on the Exchange. Consistent with the Linkage Plan, the Amex does not charge for the execution of Satisfaction Orders sent through the Linkage.<sup>6</sup>

<sup>3</sup> See Securities Exchange Act Release No. 47822 (May 9, 2003), 68 FR 27115 (May 19, 2003) (SR-Amex-2003-14).

<sup>4</sup> For example, specialists and registered options traders on the Exchange are subject to a \$.10 per contract fee for transactions in QQQ options.

<sup>5</sup> Telephone conversation between Jeffrey Burns, Associate General Counsel, Amex, and Jennifer Colihan, Special Counsel, Division of Market Regulation, Commission on January 23, 2004 clarifying that the previous approval of fees for Linkage Orders (see note 3, *supra*) did not include the Options Licensing Fee.

<sup>6</sup> See Securities Exchange Act Release No. 47298 (January 31, 2003), 68 FR 6524 (February 7, 2003) (File No. 4-429).

As was the case in its filing for the original pilot program, the Exchange believes that the existing fee amount for equity options that currently is charged to Exchange specialists and ROTs should apply to executions resulting from Linkage Orders. Market makers from other option exchanges accessing the liquidity of the Exchange by sending P or P/A Orders accordingly pay the same fees applicable to Amex specialists and ROTs for such executions.

Based on the limited experience operating the Linkage, the Exchange believes that an extension of the pilot program for six (6) months until July 31, 2004 is appropriate. During this time, the Exchange intends to study the effect of Linkage fees and prepare to file a permanent Linkage fee proposal.

###### 2. Statutory Basis

The Amex believes the proposed rule change is consistent with Section 6(b)(4) of the Act<sup>7</sup> regarding the equitable allocation of reasonable dues, fees and other charges among exchange members and other persons using exchange facilities.

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

The Exchange believes that the proposed rule change will impose no burden on competition.

##### 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. 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. Comments may also be submitted electronically at the following e-mail address: [rule-comments@sec.gov](mailto:rule-comments@sec.gov). All comment letters should refer to File No. SR-Amex-2004-03. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. Copies of the submission, all subsequent

<sup>7</sup> 15 U.S.C. 78f(b)(4).

<sup>12</sup> 15 U.S.C. 78k-1.

<sup>13</sup> 17 CFR 240.11Aa3-2.

<sup>14</sup> 17 CFR 200.30-3(a)(29).

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

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