

is consistent with section 6(b) of the Act,<sup>9</sup> and furthers the objectives of section 6(b)(4) of the Act<sup>10</sup> in particular, in that it is designed to provide for the equitable allocation of reasonable dues, fees, and other charges among CBOE members.

#### *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 that is 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*

The CBOE neither solicited nor received written comments with respect to the proposed rule change.

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

Because the foregoing rule change establishes or changes a due, fee, or other charge imposed by the CBOE, it has become effective pursuant to section 19(b)(3)(A) of the Act<sup>11</sup> and subparagraph (f) of Rule 19b-4 thereunder.<sup>12</sup> At any time within 60 days after the filing of the proposed rule change, the Commission may summarily abrogate the 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 proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be

available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the CBOE. All submissions should refer to file number SR-CBOE-2003-19 and should be submitted by June 26, 2003.

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

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 03-14171 Filed 6-4-03; 8:45 am]

BILLING CODE 8010-01-M

## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-47941; File No. SR-CSE-2003-05]

### **Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the Cincinnati Stock Exchange, Inc. Relating to an Extension of an Existing Pilot Amending CSE Rule 12.6, Customer Priority, To Require Designated Dealers to Better Customer Orders at the National Best Bid or Offer by Whole Penny Increments**

May 29, 2003.

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 May 22, 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 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 to grant accelerated approval of the proposed rule change for a pilot period through December 1, 2003.

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

The Exchange proposes to extend the termination date of the pilot that amends CSE Rule 12.6, Customer Priority, by adding new Interpretation .02, which requires a CSE Designated Dealer ("Specialist") to better the price of a customer limit order that is held by that Specialist if that Specialist determines to trade with an incoming

market or marketable limit order.<sup>3</sup> Under the pilot rule, the Specialist is required to better a customer limit order at the national best bid or offer ("NBBO") by at least one penny and at a price outside the current NBBO by at least the nearest penny increment. The Exchange is requesting an extension of the pilot, and the exemption letters associated therewith.<sup>4</sup> The proposed extension of the pilot requires no changes to the Initial Pilot rule text, which is available at the CSE 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 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 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 Exchange proposes to amend Exchange Rule 12.6<sup>5</sup> by adding an

<sup>3</sup> See Securities Exchange Act Release Nos. 46274 (July 29, 2002), 67 FR 50743 (August 5, 2002) ("Initial Pilot"); 46554 (September 25, 2002), 67 FR 6276 (October 4, 2002) ("Pilot Extension"); and 46929 (November 27, 2002), 67 FR 72711 (December 6, 2002) ("Second Extension").

<sup>4</sup> See letter from Robert L.D. Colby, Deputy Director, Division of Market Regulation ("Division"), Commission, to Jeffrey T. Brown, General Counsel, CSE (July 26, 2002) ("Initial Exemption Letter") in response to letter from Jeffrey T. Brown, General Counsel, CSE, to Annette Nazareth, Director, Division, Commission (November 27, 2001) ("Initial Exemption Request"); letter from Robert L.D. Colby, Deputy Director, Division, Commission, to Jeffrey T. Brown, General Counsel, CSE (September 25, 2002) (amending and extending the Initial Exemption Letter) ("Amended Exemption Letter") in response to letter from Jeffrey T. Brown, General Counsel, CSE, to Annette Nazareth, Director, Division, Commission (September 18, 2002) ("Amended Exemption Request"); letter from Alden S. Adkins, Associate Director, Division, Commission, to Jeffrey T. Brown, Senior Vice President & General Counsel, CSE (November 27, 2002) ("Second Exemption Extension Letter") in response to letter from Jeffrey T. Brown, Senior Vice President & General Counsel, CSE, to Annette Nazareth, Director, Division, Commission (November 20, 2002) ("Second Exemption Request").

<sup>5</sup> CSE Rule 12.6 provides, in pertinent part, that no member shall (i) personally buy or initiate the purchase of any security traded on the Exchange for

Continued

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

<sup>10</sup> 15 U.S.C. 78f(b)(4).

<sup>11</sup> 15 U.S.C. 78s(3)(a).

<sup>12</sup> 17 CFR 240.19b-4.

<sup>13</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.

interpretation to the rule covering the trading of securities in subpenny increments.<sup>6</sup> New Interpretation .02 to the Rule will require a Specialist to better the price of a customer limit order held by the Specialist by at least one penny (for those customer limit orders at the NBBO) or by at least the nearest penny increment (for those customer limit orders that are not at the NBBO) if the Specialist determines to trade with an incoming market or marketable limit order.<sup>7</sup>

The purpose of the new Interpretation is to prevent a Specialist from taking unfair advantage of customer limit orders held by that Specialist by trading ahead of such orders with incoming market or marketable limit orders. Notwithstanding the fact that a Specialist may price-improve incoming orders by providing prices superior to that of customer limit orders it holds, customers should have a reasonable expectation to have their orders filled at their limit order prices. This expectation should be reflected in reasonable access to incoming contra-side order flow, unless other customers place better-priced limit orders with the Specialist or the Specialist materially improves upon the customer limit order prices (not the customers' quoted prices) it holds.

its own account or for any account in which it or any associated person of the member is directly or indirectly interested while such a member holds or has knowledge that any person associated with it holds an unexecuted market or limit price order to buy such security in the unit of trading for a customer, or (ii) sell or initiate the sale of any such security for any such account while it personally holds or has knowledge that any person associated with it holds an unexecuted market or limit price order to sell such security in the unit of trading for a customer.

<sup>6</sup> In conjunction with this proposed rule change, the CSE has requested that the Commission extend the relief provided by the Second Exemption Extension Letter pursuant to Rules 11Ac1-1(e) (17 CFR 240.11Ac1-1(e)), 11Ac1-2(g) (17 CFR 240.11Ac1-2(g)) and 11Ac1-4(d) (17 CFR 240.11Ac1-4(d)) to allow subpenny quotations to be rounded down (buy orders) and rounded up (sell orders) to the nearest penny for quote dissemination for Nasdaq and listed securities. See letter from Jeffrey T. Brown, General Counsel, CSE, to Annette Nazareth, Director, Division, Commission (May 19, 2003) ("Third Exemption Request"). Concurrent with the instant accelerated approval, the Commission has granted the Third Exemption Request. See letter from Robert L.D. Colby, Deputy Director, Division, Commission, to Jeffrey T. Brown, Senior Vice President & General Counsel, CSE (May 29, 2003) (extending the Second Exemption Extension Letter) ("Third Exemption Extension Letter").

<sup>7</sup> Interpretation .01 to Rule 12.6 provides that "[i]f a Designated Dealer holds for execution on the Exchange a customer buy order and a customer sell order that can be crossed, the Designated Dealer shall cross them without interpositioning itself as a dealer."

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with the provisions of section 6(b) of the Act,<sup>8</sup> in general, and section 6(b)(5) of the Act,<sup>9</sup> in particular, which requires, among other things, that the rules of an exchange be designed 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, and, in general, to protect investors and the public interest. The Exchange requests that this rule be approved on a pilot basis through December 1, 2003, to be co-extensive with the conditional temporary exemptive relief granted concurrently by the Commission in the Third Exemption Extension Letter.

### 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 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 written comments on 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. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No.

<sup>8</sup> 15 U.S.C. 78f(b).

<sup>9</sup> 15 U.S.C. 78f(b)(5).

SR-CSE-2003-05 and should be submitted by June 26, 2003.

## IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange,<sup>10</sup> and, in particular section 6(b)(5) of the Act.<sup>11</sup> As discussed above, through the Third Exemption Extension Letter, the Division has extended the relief granted by the Second Exemption Extension Letter. The Commission believes that the proposed rule change should provide protection to customer limit orders in the subpenny trading environment by helping to ensure that such orders will continue to have access to market liquidity ahead of Exchange Specialists in appropriate circumstances.

The Commission finds good cause for approving the proposed rule change on a pilot basis prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. The Commission believes that granting accelerated approval to the proposed rule change will allow the Exchange to provide uninterrupted protection to customer limit orders in subpenny increments in Nasdaq securities and listed securities.

## V. Conclusion

*It is therefore ordered*, pursuant to section 19(b)(2) of the Act,<sup>12</sup> that the proposed rule change (SR-CSE-2003-05) is hereby approved on an accelerated basis for a pilot period through December 1, 2003.

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

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 03-14170 Filed 6-4-03; 8:45 am]

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<sup>10</sup> In granting approval of the proposal, the Commission has considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>11</sup> 15 U.S.C. 78f(b)(5).

<sup>12</sup> 15 U.S.C. 78s(b)(2).

<sup>13</sup> 17 CFR 200.30-3(a)(12).