

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 Nasdaq. All submissions should refer to File No. SR-NASD-2003-116 and should be submitted by September 5, 2003.

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

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

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48307; File No. SR-NYSE-2002-63]

### Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 Relating to Amendments to Rules 98, 104A.50, 105, and 900 To Permit Single Stock Futures Hedging by Specialists

August 8, 2003.

#### I. Introduction

On November 21, 2002, the New York Stock Exchange ("NYSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission"), 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> a proposed rule change to amend certain Exchange rules to permit single stock futures hedging by specialists. On January 10, 2003, the rule proposal was published for comment in the **Federal Register**.<sup>3</sup> On July 23, 2003 the NYSE filed Amendment No. 1 to the proposed rule

change.<sup>4</sup> The Commission received no comments on the proposed rule change. This order approves the proposed rule change, as amended, grants accelerated approval of Amendment No. 1 and solicits comments from interested persons on Amendment No. 1.

#### II. Description of the Rule Change

Under the rule change, the Exchange will permit specialists to use security futures overlying single securities (hereinafter referred to as "single stock futures") to hedge specialty stock positions. Rule 105 currently permits specialists to use options to hedge their specialty stock positions. Specifically, the Exchange is amending Rules 105, 98, 104A.50, and 900(d)(v).

##### *Amendments to Rule 105*

The Exchange is amending paragraph (d) of the Guidelines to Rule 105 (the "Guidelines") to explain the conditions under which single stock futures may be used to hedge an existing specialty stock. Under the rule change, anticipatory hedging is not permitted. As is the case under Rule 105 with options, only existing specialty stock positions may be hedged.

As amended, Rule 105 will provide three conditions (similar to those applicable to options) that single stock futures transactions must meet:

- (i) The transaction must result in a net futures position on the opposite side of the market from the underlying specialty stock position;
- (ii) The transaction must be effected solely to offset the risk of making a market in the underlying specialty stock; and
- (iii) The resulting net futures position must not exceed the number of shares of the specialty stock position that the specialist is offsetting.

Any single stock futures transaction that does not meet all three of the above conditions would be deemed to be in violation of Rule 105.

Under the rule change, a specialist would be able to use one single stock futures contract to hedge each 100

shares of the existing specialty stock position. A hedge that subsequently exceeds the specialty stock position being hedged as a result of 25% or more in the specialist's stock position or which becomes on the same side of the market as the specialty stock position must be liquidated, unless the equivalent share position is 5000 shares or less.

Similarly, Rule 105 will be amended to specify that, as with options, specialists may also not front-run blocks and must record futures positions in a separate "memo" account. Additionally, specialists must report to the Exchange: (i) accounts in which single stock futures positions are held and (ii) their positions in single stock futures.

Rule 105 permits an approved person of a specialist to act as a primary market maker or specialist with respect to an option on a specialty stock, provided all the requirements of the Rule 98 exemptive program are met. This provision will be amended to incorporate references to market makers in single stock futures so that an approved person of an equity specialist may act as a primary market maker or specialist with respect to a stock futures contract, provided all the requirements of the Rule 98 exemptive program are met.

In addition, Rule 105 prohibits an approved person of an equity specialist from acting as a market maker in any equity security in which the associated specialist is registered as such and which underlies an option as to which the approved person acts as an options market maker. Under the rule change, the same prohibition will apply with respect to market makers in single stock futures contracts.

The Exchange is adding a provision to Rule 105 to explain the combined use of both options and single stock futures to hedge specialty stock positions. Under the rule change, if a specialist chooses to hedge a specialty stock position with positions in both options and single stock futures, the resulting total market position, when established, may not exceed the size of the existing specialty stock position being hedged. Any excess or same side of the market equivalent position must be liquidated in accordance with the provisions of Rule 105.

##### *Other Proposed Amendments*

In addition to the amendments to Rule 105, the Exchange is amending Rules 98, 104A.50, and 900(d)(v) to incorporate appropriate references to single stock futures.

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> See Securities Exchange Act Release No. 47160 (January 10, 2003), 68 FR 02064 (January 17, 2003).

<sup>4</sup> In Amendment No. 1, the Exchange amended the definition of "security future" in Rule 105(b) to conform it to the definition of that term in section 3(a)(55) of the Act for uniformity. The Exchange also made certain technical changes to the proposed rule text and added an example that describes the way a combination of options and single stock futures contracts may be used to hedge a specialty stock position. In addition, the Exchange acknowledged that the prohibition in section 6(h)(1) of the Act on effecting transactions in security futures products that are not listed on a national securities exchange would apply to the transactions permitted under the proposed rule change. The Exchange stated further that it will remind its members of this prohibition when it announces the approval of the proposed rule change.

### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>5</sup> Specifically, the Commission believes the proposed rule change, as amended, 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 prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to perfect the mechanism of a free and open market, and in general to protect investors and the public interest.

The Commission believes that the rule change should provide specialists with greater flexibility in their ability to use hedging transactions to offset market-making risk. By permitting specialists to use single stock futures to hedge their specialty stock positions, the Commission believes that the rule change should enable specialists to add to overall stock market liquidity by taking specialty stock positions they might not otherwise assume or by reducing risks on positions they are required to assume.

The Commission is accelerating approval of Amendment No. 1 to the proposed rule change. Amendment No. 1 made technical corrections and certain other minor changes to the proposed rule change. The Commission believes that the changes included in Amendment No. 1 should not affect the substance of the rule change. Accordingly, pursuant to Section 19(b)(2) of the Act,<sup>7</sup> the Commission finds good cause to approve Amendment No. 1 prior to the thirtieth day after notice of the Amendment is published in the **Federal Register**.

### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 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

<sup>5</sup> In approving the proposed rule change, the Commission has considered its impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

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

<sup>7</sup> 15 U.S.C. 78s(b)(2).

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 also will be available for inspection and copying at the principal office of the NYSE. All submissions should refer to File No. SR-NYSE-2002-63 and should be submitted by September 5, 2003.

### V. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>8</sup> that the proposed rule change (SR-NYSE-2002-63) is approved, and Amendment No. 1 is approved on an accelerated basis.

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

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48310; File No. SR-Phlx-2002-85]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change, and Amendment No. 1 Thereto, by the Philadelphia Stock Exchange, Inc. Relating to the Definition of a Wheel Assignment Area

August 8, 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 December 20, 2002, the Philadelphia Stock Exchange, Inc. ("Phlx" 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 Phlx submitted Amendment No. 1 to the proposed rule change on July 28, 2003.<sup>3</sup> The Commission is publishing

<sup>8</sup> Id.

<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> Letter from Richard S. Rudolph, Director and Counsel, Phlx, to Nancy Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated July 25, 2003 ("Amendment No. 1"). In Amendment No. 1, the Phlx amended the

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 Phlx proposes to amend Option Floor Procedure Advice ("OFPA") F-24, AUTO-X Contra-Party Participation (The Wheel), to redefine a "Wheel Assignment Area," based on the current configuration of the Exchange Options Floor. The text of the proposed rule change is set forth below. Proposed new language is in italics. Proposed deletions are in brackets.

\* \* \* \* \*

F-24 AUTO-X Contra-Party Participation (The Wheel)

(a)-(b) No change.

(c) Participation Requirements and Sign-on/off—Specialists on the Options Floor are required to participate on the Wheel in assigned issues in accordance with paragraph (e) of this Advice.

(i) An ROT[s] may elect to participate on the Wheel for any or all [issues] *options* which *such ROT* [they] maintains an ROT assignment, as long as *such* [those listed] *options* are located *within the Wheel Assignment Area (as defined below) for the crowd in which such ROT participates*, [within two contiguous quarter turrets of each other] and the ROT is actively making markets in the specific [issues] *options traded within such Wheel Assignment Area*.

(ii) No two associated or dually affiliated ROTs may be on the Wheel for the same option at the same time. Regardless of [an ROT's] *the total number of options assigned to an ROT* [issues], an ROT may only sign-on the Wheel in one Wheel [a]Assignment [a]Area at any given time.

(iii) For [the] purposes of this Advice, a Wheel [a]Assignment [a]Area is [each area on the trading floor constituted by two contiguous quarter turrets] *a location on the trading floor where an ROT: (1) Is actively making markets by quoting continuous, 2-sided markets in compliance with Advice B-1 and Rule 1014; (2) can hear and ascertain the markets that are being made by the specialist and crowd; (3) is deemed to be quoting the disseminated markets being made by the specialist in accordance*

proposed rule change by clarifying the proposed definition of a "Wheel Assignment Area" set forth in paragraph (c)(iii) of OFPA F-24, AUTO-X Contra-Party Participation (The Wheel). The substance of Amendment No. 1 is incorporated into the description of the proposed rule change in Section II.A. below, and the proposed rule text set forth herein reflects the changes made in Amendment No. 1.