

raises collateral issues that the Amex will need to monitor and address. Increasing the maximum order size for particular option classes will make a larger number of option orders eligible for Auto-Ex. These orders may benefit from greater speed of execution, but at the same time create greater risks for market maker participants. Market makers signed on to the Amex's Auto-Ex system will be exposed to the financial risks associated with larger-sized orders being routed through the system for automatic execution at the displayed price; however, these risks are somewhat offset by the fact that the Exchange's Auto-Ex system allocates executed contracts into lots of 10 contracts among the specialist and any ROTs logged onto Auto-Ex.

In addition, when the market for the underlying security changes rapidly, it may take a few moments for the related option's price to reflect that change. In the interim, customers may submit orders that try to capture the price differential between the underlying security and the option. The larger the orders accepted through Auto-Ex, the greater the risk market makers must be willing to accept. The Commission does not believe that, because Amex floor governors or senior floor officials determine to approve orders as large as 500 contracts as eligible for Auto-Ex, Amex floor governors or senior floor officials or Amex staff should disengage Auto-Ex more frequently by, for example, declaring an "unusual market condition." Disengaging Auto-Ex can negatively affect investors by making it slower and less efficient to execute their orders.¹⁶ It is the Commission's view that the Amex, when increasing the maximum size of orders that can be sent through Auto-Ex, should not disadvantage all customers—the vast majority of whom enter orders for less than 500 contracts—by making their automatic execution systems less reliable.

IV. Conclusion

For the foregoing reasons, 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, and, in particular, with section 6(b)(5).¹⁷

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹⁸ that the

¹⁶ See Amex Rule 933(f)(i), specifying the circumstances in which Auto-Ex may be disengaged or operated in a manner other than the normal manner.

¹⁷ 15 U.S.C. 78f(b)(5).

¹⁸ 15 U.S.C. 78s(b)(2).

proposed rule change (SR-Amex-2003-08) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁹

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03-9593 Filed 4-17-03; 8:45 am]

BILLING CODE 8010-01-P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47664; File No. SR-PCX-2003-14]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Pacific Exchange, Inc. and Amendment No. 1 Thereto Regarding the Maximum Permissible Number of Nasdaq-100 Tracking Stock ("QQQ") Option Contracts Executable Through the Exchange's Automatic Execution System ("Auto-Ex")

April 10, 2003.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and rule 19b-4 thereunder,² notice is hereby given that on March 27, 2003, the Pacific Exchange, Inc. ("Exchange" or "PCX") 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 PCX. The proposed rule change has been filed by the PCX as a "non-controversial" rule change under rule 19b-4(f)(6) under the Act.³ On April 7, 2003, the PCX filed Amendment No. 1 to the proposed rule change.⁴ 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 amend its rules to increase to 2,000 contracts in the first two near term expiration months, and to 1,000 contracts for all other expiration months, the maximum permissible number of QQQ option contracts in an

¹⁹ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 17 CFR 240.19b-4(f)(6).

⁴ See letter from Mai Shiver, Senior Attorney, Regulatory Policy, PCX, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated April 4, 2003. In Amendment No. 1, PCX amended the proposed rule text of the proposed rule change to reflect the current rule language of PCX rule 6.87.

order that can be executed through Auto-Ex.

Below is the text of the proposed rule change, as amended. Proposed new language is *italicized*.

* * * * *

Automatic Execution System

Rule 6.87(a)-(b)(5)—No change.

(6) The OFTC or its delegate consisting of two Floor Officials shall determine the size of orders that are eligible to be executed on Auto-Ex. The OFTC or its delegate, two Floor Officials, may approve requests of the Lead Market Makers to execute orders on Auto-Ex in sizes greater than 20 contracts. Although the order size parameter may be changed on an issue-by-issue basis by the OFTC or its delegate, two Floor Officials, the maximum order size for execution through Auto-Ex is as follows:

(A) Equity Options: the maximum order size for execution through Auto-Ex for equity options is 250 contracts *except for options on the Nasdaq-100 Tracking Stock (QQQ) in which case, the maximum order size will be 2,000 contracts in the first two (2) near term expiration months and 1,000 contracts for all other expiration months;*

(B) Index Options: the maximum order size for execution through Auto-Ex is 250 contracts.

(7)—No change.

(c)-(p)—No change.

Commentary .01-.08—No change.

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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

The Exchange proposes to increase the maximum order size eligibility for Auto-Ex in the first two near term expiration months in QQQ options to 2,000 contracts and to 1,000 contracts

for all other expiration months⁵ to match the size of orders in the same options eligible for automatic execution on another options exchange.⁶ The Exchange notes that the American Stock Exchange LLC ("Amex") and the Philadelphia Stock Exchange, Inc. ("Phlx") allow automatic executions in QQQ options for a size of up to 2,000 contracts in series in the two near term expiration months, and up to 1,000 contracts in all other expiration months.⁷ The Exchange represents that Auto-Ex affords prompt and efficient automatic executions at the disseminated quotation price on the Exchange. Therefore, the Exchange believes that increasing automatic execution levels for eligible orders in QQQ options to 2,000 contracts in the first two near term expiration months, and to 1,000 contracts for all other expiration months should provide the benefits of automatic execution to a larger number of customer orders. Further, the Exchange notes that this increase in automatic execution levels in QQQ options should enable the Exchange to remain competitive for order flow with other exchanges that trade QQQ options.

The Exchange believes that the increase in order size eligibility for Auto-Ex orders in QQQ options should provide customers with quicker executions for a larger number of orders by providing automatic rather than manual executions, thereby reducing the number of orders subject to manual processing. The Exchange also believes that increasing the Auto-Ex maximum order size in QQQ options should not impose a significant burden on the operation or capacity of the Auto-Ex System and will give the Exchange better means of competing with other options exchanges for order flow.

2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is

⁵ Currently, the maximum option order size eligible for automatic execution via Auto-Ex is 250 contracts for all equity options including the QQQs.

⁶ Exchange rule 6.87(b)(7) provides that the Options Floor Trading Committee may, in its discretion, increase the size of orders in one or more classes of multiply-traded equity options eligible for Auto-Ex to the extent necessary to match the size of orders in the same options eligible for entry into the automated execution system of any other options exchange, provided that the effectiveness of any such increase shall be conditioned upon its having been filed with the Commission pursuant to section 19(b)(3)(A) of the Act.

⁷ See Securities Exchange Act Release No. 45828 (April 25, 2002), 67 FR 22140 (May 2, 2002) (File No. SR-Amex-2002-30); see also Securities Exchange Act Release No. 46531 (September 23, 2002), 67 FR 61370 (September 30, 2002) (File No. SR-Phlx-2002-47).

consistent with section 6(b) of the Act⁸ in general, and furthers the objectives of section 6(b)(5) of the Act⁹ in particular, because it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments and perfect the mechanisms of a free and open market and 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 inappropriate burden on competition that is not necessary 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. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing proposed rule change, as amended, has become effective pursuant to section 19(b)(3)(A)¹⁰ of the Act and rule 19b-4(f)(6)¹¹ thereunder because the proposal: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date of filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest; provided that the Exchange has given the Commission written notice of its intent to file the proposed rule change at least five business days prior to the filing date of the proposed rule change.¹² The PCX seeks to have the proposed rule change become operative immediately upon filing because it believes that the proposed rule change, as amended, is consistent with the protection of investors and the public interest, and in order to remain competitive with other exchanges with similar rules in effect.¹³

⁸ 15 U.S.C. 78f(b).

⁹ 15 U.S.C. 78f(b)(5).

¹⁰ 15 U.S.C. 78s(b)(3)(A).

¹¹ 17 CFR 240.19b-4(f)(6).

¹² As required under rule 19b-4(f)(6)(iii), the Exchange 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.

¹³ See *supra* note 7.

The Commission, consistent with the protection of investors and the public interest, has determined to make the proposed rule change, as amended, operative immediately upon filing to allow the PCX to compete with other options exchanges that currently has a maximum automatic execution eligibility limit in QQQ options of 2,000 contracts in the first two near term expiration months.¹⁴ 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.¹⁵

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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 PCX. All submissions should refer to File No. SR-PCX-2003-14 and should be submitted by May 9, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁶

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 03-9594 Filed 4-17-03; 8:45 am]

BILLING CODE 8010-01-P

¹⁴ 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).

¹⁵ For purposes of calculating the 60-day abrogation period, the Commission considers the period to commence on April 7, 2003, the date that the Exchange filed Amendment No. 1.

¹⁶ 17 CFR 200.30-3(a)(12).