

made pursuant to Section 19(b)(3)(A)(ii) of the Act.<sup>3</sup>

As described above, the proposed marketing fee will be imposed on all of the market makers (including the DPM) in the classes of options that are subject to the fee. The Exchange believes that, because these same persons will be able to participate in the order flow derived from the program, there will be a fair correlation between those members who pay the costs of the marketing program funded by the new fee and those who receive the benefits of the program.

In connection with any program involving payment for order flow that may be funded by the Exchange's proposed marketing fee, the Exchange will issue appropriate regulatory or educational circulars to its members that emphasize the disclosure and best execution obligations of members who may accept such payment.

The Exchange believes that the new marketing fee and the marketing programs it may fund, including any payment for order flow program, will serve to enhance the competitiveness of the Exchange and its members. Accordingly, the Exchange believes that the proposed rate change is consistent with and furthers the objectives of the Act, including specifically Section 6(b)(5)<sup>4</sup> thereof, which requires the rules of exchanges to be designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, and Section 11A(a)(1)(C)<sup>5</sup> thereof, which reflects the finding of Congress that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure fair competition among brokers and dealers and among exchange markets.

#### *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*

No written comments were solicited or received with respect to the proposed rule change.

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

Because the foregoing rule change establishes or changes a due, fee, or other charge imposed by the Exchange, it has become effective pursuant to section 19(b)(3)(A)(ii) of the Act<sup>6</sup> and subparagraph (f)(2) of Rule 19b-1 thereunder.<sup>7</sup> 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.

### **IV. Solicitation of Comments**

The Commission, in the past, has raised serious concerns about payment for order flow and internalization.<sup>8</sup> Payment for order flow is of concern because brokers who are paid to send their customers' orders to one exchange have a conflict of interest that may reduce their commitment to the duty they owe their customers to find the best execution available.<sup>9</sup> While payment for order flow has been a common practice in the equities markets for some time, only recently has payment for order flow developed in the options markets. Despite these concerns, however, the CBOE's proposal involves the imposition of a fee and the Act gives exchanges wide latitude to establish, revise, and collect fees and other charges without prior Commission approval. The Commission invites interested persons to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule is consistent with the Act. In particular, the Commission asks persons who submit comments whether the payment for order flow facilitated by the CBOE's proposal raises greater or different concerns than payment for order flow by specialists on other options exchanges. After receiving comments, and at any time within 60 days from the date the CBOE filed its proposal, the Commission can decide to require the CBOE to stop collecting the fee, refile the proposal, and await

Commission approval before reinstituting the fee.

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 No. SR-CBOE-00-28 and should be submitted August 31, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

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

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-43114; File No. SR-CBOE-00-31]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Chicago Board Options Exchange, Inc., to Amend its Rules to Allow for the Trading of Options on Securities that Represent Interests in Registered Investment Companies Based on Narrow-Based Indices or Portfolios of Securities**

August 3, 2000.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 24, 2000, the Chicago Board Options Exchange Inc. ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The proposed rule change has been filed by the CBOE as a "non-controversial" rule

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

<sup>7</sup> 17 CFR 240.19b-4(f)(2).

<sup>8</sup> See Securities Exchange Act Release No. 42450 (February 23, 2000), 65 FR 10577 (Feb. 28, 2000); Securities Exchange Act Release No. 34902 (October 27, 1994), 59 FR 55006 (Nov. 2, 1994). See also Securities Exchange Act Release No. 43084 (July 28, 2000).

<sup>9</sup> The CBOE has filed with the Commission a proposal to implement the "CBOE Best Execution Assurance Program." See Securities Exchange Act Release No. 43113 (August 3, 2000), File No. SR-CBOE-00-32.

<sup>10</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> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>4</sup> 15 U.S.C. 78f(b)(5).

<sup>5</sup> 15 U.S.C. 78k(a)(1)(C).

change effective upon filing under Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b-4(f)(6)<sup>4</sup> thereunder. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The CBOE proposes to amend its rules to allow for the trading of options on securities that represent interests in registered investment companies based on narrow-based indices or portfolios of securities.

The text of the proposed rule change is available at the Office of the Secretary, CBOE 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 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 July 2, 1998, the Commission approved a proposed rule change to permit the trading of options on exchange-listed securities representing interest in open-end investment companies that hold securities comprising or based on stock indices or portfolios of securities ("Fund Shares").<sup>5</sup> However, that rule change was limited to trading options on Fund Shares comprising or based on broad-based indices or portfolios. Accordingly, the Exchange now proposes to amend its rules to allow for the trading of options on exchange-listed securities representing interest in open-end investment companies that hold securities comprising or based on non-broad-based, or narrow-based, stock indices or portfolios of securities. The Exchange believes that the ability to

trade options on Fund Shares based on narrow-based indices or portfolios is consistent with the options listing criteria for Fund Shares currently used by the American Stock Exchange, LLC ("Amex").<sup>6</sup>

Fund shares are issued in exchange for an "in-kind" deposit of a specified portfolio of securities, together with a cash payment, in minimum size aggregations or multiples thereof ("Creation Units"). The size of the applicable Creation Unit size aggregation is set forth in the fund's prospectus, and varies from one series of Fund Shares to another, but generally is substantial. A fund generally will issue and sell Fund Shares in Creation Unit size through a principal underwriter on a continuous basis at the net asset value per share next determined after an order to purchase Fund Shares and the appropriate securities are received. Following issuance, Fund Shares are traded on an exchange like other equity securities, and equity trading rules apply. Likewise, redemption of Fund Shares is made in Creation Unit size and "in-kind," with a portfolio of securities and cash exchanged for Fund Shares that have been tendered for redemption.

The CBOE trades options on Fund Shares pursuant to the same rules and procedures that apply generally to trading in options on equity securities, except that some special listing criteria are, under certain circumstances, applied to this category of options. The listing and maintenance standards for options on Fund Shares are set forth in Interpretation and Policy .06 under CBOE Rule 5.3 and in Interpretation and Policy .08 under CBOE Rule. 5.4, respectively. CBOE only lists options on Fund Shares that are principally traded on a national securities exchange or through the facilities of a national securities association and reported as national market securities. In addition, the initial listing standards require that either: (1) The Fund Shares meet the uniform options listing standards in Interpretation and Policy .01 under CBOE Rule 5.3, which include minimum public float, trading volume, and share price of the underlying security in order to list the option; or (2) the Fund Shares must be available for creation or redemption each business day in cash or in kind from the fund at a price related to the net asset value. In this event the Exchange will require that the fund is obligated to issue Fund

Shares in a specified aggregate number even though some or all of the securities needed to be deposited have not been received by the fund, subject to the fund, subject to the condition that the person obligated to deposit the securities has undertaken to deliver the securities as soon as possible and such undertaking is secured by the delivery and maintenance of collateral consisting of cash or cash equivalents satisfactory to the fund, all as described in the fund prospectus.

In addition, the initial listing standards require that: (1) Any Fund Share with non-U.S. stocks in the underlying index or portfolio that are not subject to comprehensive surveillance agreements do not in the aggregate represent more than 50% of the weight of the index or portfolio; (2) stocks for which the primary market is in any one country that is not subject to a comprehensive surveillance agreement do not represent 20% or more of the weight of the index; and (3) stocks for which the primary market is in any two countries that are not subject to comprehensive surveillance agreements do not represent 33% or more of the weight of the index.

The Exchange's maintenance standards provide that if a particular series of Fund Shares should cease to trade on an exchange or as national market securities in the over-the-counter market, there will be no opening transactions in the options on the Fund Shares, and all such options will trade on a liquidation-only basis. In addition, the CBOE will consider the suspension of opening transactions in any series of options of the class covering Fund Shares if: (1) The options fail to meet the uniform equity option maintenance standards in paragraphs (a), (b), (c), and (d) of Interpretation and Policy .01 under CBOE Rule 5.4, when the options were listed pursuant to the equity option listing standards of Interpretation and Policy .01 under CBOE Rule 5.3; (2) following the initial twelve-month period beginning upon the commencement of trading of the Fund Shares on a national securities exchange or as national market securities through the facilities of a national securities association there are fewer than 50 record and/or beneficial holders of Fund Shares for 30 or more consecutive trading days, when options on Fund Shares were listed pursuant to clause D(y) under Interpretation and Policy .06, under CBOE Rule 5.3; or (3) the value of the index or portfolio of securities on which the Fund Shares are based is no longer calculated or available.

Margin requirements for Fund Shares are comparable to margin requirements

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

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

<sup>5</sup> See Securities Exchange Act Release No. 40166 (July 2, 1998), 63 FR 37430 (July 10, 1998) (File No. SR-CBOE-97-03).

<sup>6</sup> The Amex listing criteria were approved by the Commission on July 1, 1998. See Securities Exchange Act Release No. 40157 (July 1, 1998) 63 FR 37426 (July 10, 1998) (File No. SR-Amex-96-44).

that apply to index options under CBOE Chapter 12. Thus, the margin requirements for options on Fund Shares that represent interest in funds that hold securities based upon a narrow-based index or portfolio must have options margin that equals at least 100 percent of the current market value of the contract plus 20 percent of the market value of equivalent units of the underlying security value.

Lastly, the CBOE believes it has the necessary systems capacity to support the additional series of options that would result from the introduction of Fund Shares representing narrow-based indices or portfolios, and it has been advised that the Options Price Reporting Authority ("OPRA") also has the capacity to support these additional series.<sup>7</sup>

## 2. Statutory Basis

By providing investors with a better means to hedge their positions in the underlying units within the framework of CBOE's regulated market place and providing investors with an alternative market center in which to trade these products, thereby increasing competition, the Exchange believes the proposed rule change is consistent with Section 6(b)(5) of the Act<sup>8</sup> in that it is 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.

### *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*

No written comments were solicited or received with respect to the proposed rule change.

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

The foregoing proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>9</sup> and Rule 19(b)-4(f)(6) thereunder because the

proposed rule change has been properly designated by the CBOE as effecting a change that: (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 that the Commission may designate if consistent with the protection of investors and the public interest.<sup>10</sup> 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 the furtherance of the purposes of the Act.<sup>11</sup>

The Exchange has requested that the rule change be accelerated to become operative immediately upon filing of the proposal to expeditiously provide investors with the a better means to hedge their positions in the underlying Fund Shares based on narrow-based indexes or portfolios, as well as an alternative market center in which to trade these products, thereby increasing competition.<sup>12</sup> In addition, the Exchange noted that options on narrow-based indexes are currently trading on the Amex.<sup>13</sup> The Commission finds that accelerating the operative date of the rule change is consistent with the protection of investors and the public interest, and thus designates July 24, 2000 as the operative date of this filing.<sup>14</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 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-CBOE-00-31 and should be submitted by August 31, 2000.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

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

[FR Doc. 00-20261 Filed 8-9-00; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43105; File No. SR-NYSE-00-24]

### **Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Approving Proposed Rule Change Relating to Revising the Exchange's FORM AP-1 Application**

August 2, 2000.

## I. Introduction

On May 25, 2000, the New York Stock Exchange, Inc., ("NYSE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "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 revise the Exchange's FORM AP-1 (the "Form") Application. The proposed rule change was published for comment in the **Federal Register** on June 27, 2000.<sup>3</sup> No comments were received on the proposal. This order approves the NYSE's proposal.

## II. Description of the Proposal

NYSE Rule 304(h) requires that "[a]ny person who controls a member or member organization, or who engages in a securities or kindred business and is controlled by or under common control with a member or member organization but is not a member or allied member

<sup>10</sup> As required under Rule 19b-4(f)(6)(iii), the CBOE 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.

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

<sup>12</sup> Telephone conversation between Angelo Evangelou, Attorney, Legal Division, CBOE, and Heather Traeger, Attorney, Division of Market Regulation, SEC, on July 28, 2000.

<sup>13</sup> See *supra* note 6.

<sup>14</sup> 17 CFR 240.19b-4(f)(6). 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>15</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> Securities Exchange Act Release No. 42971 (June 21, 2000), 65 FR 39644.

<sup>7</sup> See Letter from Joe Corrigan, Executive Director, OPRA, to William Speth, Director of Research, CBOE, dated July 14, 2000.

<sup>8</sup> 15 U.S.C. 78f(b)(5).

<sup>9</sup> 15 U.S.C. 78s(b)(3)(A).