

Linkage Plan. Autofade will move one side of CBOE's quote to a price that is 1-tick inferior to the NBBO.<sup>5</sup> This will ensure that the Exchange will not immediately receive additional linkage orders in order to allow the member to refresh the quote (either manually or through an autoquote update).

As mentioned above, autofade also would apply anytime an automatic execution of any order via the Exchange's Retail Automatic Execution System ("RAES") has depleted the size of CBOE's quote. On March 29, 2002, the Commission approved a CBOE proposal to implement a "quotes with size" system that would enable the Exchange to disseminate options quotations with a size that reflects previous executions (decrementing quotes).<sup>6</sup> A current feature of this functionality provides that when a quote is exhausted via automatic executions, the Exchange may disseminate a size of "1" for a specified "reroute" period during which time the Exchange's RAES system is disengaged.<sup>7</sup> Autofade would eliminate any need to disengage the RAES system and disseminate a size of 1 contract at the same price. Once a quote is exhausted, autofade would move one side of the quote to a price that is one tick inferior to the NBBO (as described above).

#### *The Reason for this Rule Filing*

CBOE anticipates that there may be limited instances where the autofade functionality moves the quote in a manner that causes the quote width to widen beyond the bid/ask parameters provided pursuant to CBOE Rule 8.7(b)(iv). Accordingly, CBOE seeks to adopt (on a pilot basis) a temporary exception to the requirements of CBOE Rule 8.7(b)(iv) in cases where the Exchange automatically adjusts one side of the disseminated quote to one minimum increment below (above) the NBBO bid (offer) and this cause the quote to exceed the quote width parameters of that rule. The proposed exemption period would last for 30 seconds after any given autofade that caused a wider quote than allowed under CBOE Rule 8.7(b)(iv). Thus, to the extent a quote remained outside of the maximum width after the 30-second time period, the responsible broker or dealer disseminating the quote would be

deemed in violation of CBOE Rule 8.7(b)(iv) for regulatory purposes. CBOE proposes that the pilot run until January 30, 2004.

#### 2. Statutory Basis

The proposed rule change will, among other things, allow the Exchange to comply more easily with the requirements of the Linkage Plan. Accordingly, the Exchange believes the proposed rule change is consistent with Section 6(b) of the Act<sup>8</sup> in general and furthers the objectives of Section 6(b)(5)<sup>9</sup> in particular in that it should promote just and equitable principles of trade, serve to remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

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

This proposed rule change does not 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**

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) As the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### **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 Section. Copies of such filing will also be available for inspection and copying at the principal office of CBOE. All submissions should refer to File No. SR-CBOE-2003-08 and should be submitted by August 25, 2003.

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. 34-48234; File No. SR-NASD-2003-93]**

### **Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change by the National Association of Securities Dealers, Inc., To Increase the Trading Activity Fee**

July 28, 2003.

#### **I. Introduction**

On June 11, 2003, the National Association of Securities Dealers, Inc. ("NASD") 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 increase its Trading Activity Fee ("TAF") by adjusting the rates for covered equity securities. The proposed rule change was published for notice and comment in the **Federal Register** on June 25, 2003.<sup>3</sup> The Commission received one comment letter on the proposal.<sup>4</sup> On July 23, 2003, the NASD

<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> See Securities Exchange Act Release No. 48061 (June 19, 2003), 68 FR 37887.

<sup>4</sup> See July 17, 2003 letter from Jeffrey T. Brown, Senior Vice President and General Counsel, The Cincinnati Stock Exchange ("CSE") to Jonathan G. Katz, Secretary, SEC ("CSE Letter").

<sup>5</sup> The only exception is when CBOE's NBBO quote (or next best quote) is represented by a customer order in the book. In such cases, the Exchange would not fade a booked order (it would have to be traded).

<sup>6</sup> See Securities Exchange Act Release No. 45676, 67 FR 16478 (April 5, 2002).

<sup>7</sup> The reroute period can be set from 0 to 30 seconds.

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

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

filed its response to comments.<sup>5</sup> This order approves the proposed rule change.

## II. Summary of Comments

The Commission received one comment letter on the NASD's proposal to increase the TAF.<sup>6</sup>

- *The CSE Letter*

The CSE disapproved of the proposed rule change, stating the proposal would "double the ill-defined TAF with no justification" and with "little check or recourse on the part of the non-NASD markets."<sup>7</sup> The CSE suggested that the Commission require the NASD to provide supporting documentation to explain the need for increasing the TAF before allowing the NASD to double the fee.<sup>8</sup> Additionally, the CSE stated that the NASD must delineate its responsibilities covered by the TAF, explain how those responsibilities are unique to the NASD, and provide a cost analysis that establishes a nexus between those responsibilities and the fees.<sup>9</sup>

The CSE also stated that the TAF, along with the NASD's Gross Income Assessment, allows "for the subsidization of NASD regulatory activities through the forced taxing of transactions occurring on other markets."<sup>10</sup> According to the CSE, the NASD is using the TAF and Gross Income Assessment, under the guise of revenue neutrality, to subsidize its regulatory activities with monies generated on other markets.<sup>11</sup>

The CSE asked for an accounting, and an explanation of why the NASD believes it is proper to limit this fee adjustment to the TAF, when the TAF is only one component of a fee structure that also includes the Gross Income Assessment ("GIA") and the Personnel Assessment ("PA").<sup>12</sup>

- *The NASD's Response to Comments*

The NASD filed the instant proposed rule change because revenue generated by the TAF at the original rate was lower than expected.<sup>13</sup> The NASD noted that it originally proposed a TAF rate of .0001 per share, but reduced the rate to 0.00005 "after informal feedback from

the membership about the level of volume meeting the definition of 'covered equity security.'"<sup>14</sup> The NASD filed the instant proposed rule change to remedy a shortfall in revenue.<sup>15</sup>

With regard to the CSE's comments that (i) the NASD has not adequately defined its responsibilities, nor has it established a sufficient nexus between its responsibilities and fees; and (ii) where intermarket fees are being assessed, a higher standard of scrutiny should be applied, the NASD noted that the Commission addressed both of these issues in its order approving the TAF.<sup>16</sup>

Finally, the NASD explained that the TAF does not underwrite "the regulation of Nasdaq and the Alternative Display Facility" and that the TAF, GIA, and PA fund the NASD's member regulatory programs.<sup>17</sup>

## III. Discussion and Commission Findings

The Commission has reviewed carefully the proposed rule change, the comment letter, and the NASD's response to the comments, and finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association<sup>18</sup> and, in particular, the requirements of section 15A(b)(5) of the Act.<sup>19</sup> Section 15A(b)(5) requires, among other things, that the rules of a national securities association provide for the equitable allocation of reasonable dues, fees, and other charges among members and issuers and other persons using any facility or system which the association operates or controls. The Commission finds that the proposed increase in the rate for the TAF as described in the instant proposed rule change is consistent with section 15A(b)(5) of the Act, in that the proposal is reasonably designed to recover NASD costs related to regulation and oversight of its members.

The Commission believes the CSE Letter raises no novel issues that were not addressed in the Commission's original TAF approval order.<sup>20</sup> The Commission also believes that the NASD adequately responded to the issues the CSE raised in its letter.

The Commission expects that the NASD will continue to monitor the revenue generated by the TAF, as well as the revenue generated by the Gross Income Assessment and the Personnel Assessment, and will take whatever steps are necessary to ensure that the fees remain consistent with the mandate established in section 15A(b)(5) of the Act,<sup>21</sup> so that the fees remain equitable, as well as consistent with the NASD's expressed goal.

## IV. Conclusion

It is therefore Ordered, pursuant to section 19(b)(2) of the Act<sup>22</sup>, that the proposed rule change (SR-NASD-2003-93) be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>23</sup>

Margaret H. McFarland,  
Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48239; File No. SR-NASD-2003-98]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by National Association of Securities Dealers, Inc., Regarding Reporting of Transactions Conducted Through Electronic Communications Networks to the Automated Confirmation Transaction Service

July 28, 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 June 19, 2003, National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), 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 Nasdaq. The Exchange submitted an amendment to the proposed rule change on January 27, 2003.<sup>3</sup> The Commission is publishing

<sup>5</sup> See July 23, 2003 letter from Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, NASD, to Katherine A. England, Assistant Director, Division of Market Regulation, SEC ("NASD Response Letter").

<sup>6</sup> See footnote 4, *supra*.

<sup>7</sup> CSE Letter at 1.

<sup>8</sup> *Id.* at 2.

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

<sup>10</sup> *Id.* at 3.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 4.

<sup>13</sup> NASD Response Letter at 1.

<sup>14</sup> *Id.* at 1-2.

<sup>15</sup> *Id.* at 2.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* at 3.

<sup>18</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>19</sup> 15 U.S.C. 78o-3(b)(5).

<sup>20</sup> See Securities Exchange Act Release No. 47946 (May 30, 2003), 68 FR 34021 (June 6, 2003) (SR-NASD-2002-148)(approval order).

<sup>21</sup> 15 U.S.C. 78o-3(b)(5).

<sup>22</sup> 15 U.S.C. 78s(b)(2).

<sup>23</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> See Letter from John Yetter, Associate General Counsel, Nasdaq, to Kathy England, Assistant Director, Division of Market Regulation, Commission, dated July 10, 2003 ("Amendment No.