

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50561; File No. 4-429)

October 19, 2004

Joint Industry Plan; Order Approving Joint Amendment No. 13 to the Options Intermarket Linkage Plan Regarding Natural Size

I. Introduction

On May 10, 2004, May 11, 2004, June 22, 2004, July 21, 2004, August 12, 2004, and August 16, 2004, the International Securities Exchange, Inc. (“ISE”), the Chicago Board Options Exchange, Inc. (“CBOE”), the American Stock Exchange LLC (“Amex”), the Pacific Exchange, Inc. (“PCX”), the Philadelphia Stock Exchange, Inc. (“Phlx”), and the Boston Stock Exchange, Inc. (“BSE”) (collectively, the “Participants”), respectively, filed with the Securities and Exchange Commission (“Commission”) an amendment (“Joint Amendment No. 13”) to the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (the “Linkage Plan”).¹ In Joint Amendment No. 13, the Participants propose to modify the definitions of Firm Customer Quote Size (“FCQS”) and Firm Principal Quote Size (“FPQS”) to accommodate the “natural size” of quotations. The Linkage Plan currently requires that the Participants be firm for both Principal Acting as Agent and Principal Orders for at least 10 contracts. The proposed Amendment would permit exchanges to be firm for the actual size of their quotation, even if this amount is less than 10 contracts.

¹ On July 28, 2000, the Commission approved a national market system plan for the purpose of creating and operating an intermarket options market linkage proposed by Amex, CBOE, and ISE. See Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000). Subsequently, Phlx, PCX, and BSE joined the Linkage Plan. See Securities Exchange Act Release Nos. 43573 (November 16, 2000), 65 FR 70850 (November 28, 2000); 43574 (November 16, 2000), 65 FR 70851 (November 28, 2000); and 49198 (February 5, 2004), 69 FR 7029 (February 12, 2004).

The proposed amendment to the Linkage Plan was published in the Federal Register on August 24, 2004.² No comments were received on the proposed amendment. This order approves the proposed amendment to the Linkage Plan.

II. Description of the Proposed Amendment

Proposed Joint Amendment No. 13 seeks to change the definitions of both FCQS and FPQS. While the proposed Amendment would maintain a general requirement that the FCQS and FPQS be at least 10 contracts, that requirement would not apply if a Participant were disseminating a quotation of fewer than 10 contracts. In that case, the Participant may establish a FCQS or FPQS equal to its disseminated size, or “natural size.”

Under the proposed amendment, as with Linkage orders today, if the order is of a size eligible for automatic execution, the receiving exchange must provide automatic execution of the Linkage order. If this is not the case (for example, the receiving exchange's automatic execution system is not engaged), the receiving exchange may allow the order to drop to manual handling. However, the receiving exchange still must provide a manual execution for at least the FCQS or FPQS, as appropriate (in this case, the size of its disseminated quotation of less than 10 contracts).

III. Discussion

After careful consideration, the Commission finds that the proposed amendment to the Linkage Plan is consistent with the requirements of the Act and the rules and regulations thereunder. Specifically, the Commission finds that the proposed amendment to the Linkage Plan is consistent with Section 11A of the Act³ and Rule 11Aa3-2 thereunder,⁴ in that it is

² See Securities Exchange Act Release No. 50211 (August 18, 2004), 69 FR 52050.

³ 15 U.S.C. 78k-1.

⁴ 17 CFR 240.11Aa3-2.

appropriate in the public interest, for the protection of investors and the maintenance of fair and orderly markets.

The Commission notes that the Participants adopted the current definitions of FCQS and FPQS, which impose a "10-up" requirement, at a time when all the Participants had rules requiring that their minimum quotation size be for at least 10 contracts. Consequently, an exchange receiving a customer limit order for fewer than 10 contracts would disseminate the price of the customer limit order with a size of 10 contracts and the specialist or the trading crowd would be responsible to make up the difference. Since implementation of the Linkage Plan, several of the Participants have modified their rules to permit them to disseminate the "natural size" of customer limit orders that are of a size less than 10 contracts.⁵ Proposed Joint Amendment No. 13 should conform the minimum quotation requirements contained in the Linkage Plan to be consistent with the Participants' rules regarding the dissemination of the size associated with customer limit orders. The Commission believes that conforming the requirements of the Linkage Plan to the requirements adopted by the Participants, which permit them to disseminate an order's "natural size," should provide greater transparency to investors and the marketplace and better reflect the true state of liquidity in the marketplace.

⁵ See Securities Exchange Act Release Nos. 46325 (August 8, 2002), 67 FR 53376 (August 15, 2002) (SR-Phlx-2002-15); 46029 (June 4, 2002), 67 FR 40363 (June 12, 2002) (SR-PCX-2002-30); 45067 (November 16, 2001), 66 FR 58766 (November 23, 2001) (SR-CBOE-2001-56); 47959 (May 30, 2003), 68 FR 34441 (June 9, 2003) (SR-CBOE-2002-05); and 48957 (December 18, 2003), 68 FR 75294 (December 30, 2003) (SR-Amex-2003-24).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 11A of the Act⁶ and Rule 11Aa3-2 thereunder,⁷ that the proposed Joint Amendment No. 13 is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁸

Margaret H. McFarland
Deputy Secretary

⁶ 15 U.S.C. 78k-1.

⁷ 17 CFR 240.11Aa3-2.

⁸ 17 CFR 200.30-3(a)(29).