

Pilot permitted member organizations to accord offset treatment in accounts carried for such specialists, market makers and SFDs only when their activity is limited to bona fide specialist or market making transactions. The limitations imposed were consistent with the Exchange's belief that market makers bear the primary responsibility and obligation to maintain fair and orderly markets, and provide liquidity to the marketplace.

On January 3, 2003, the Exchange filed a proposed rule change to extend the Pilot for an additional sixty days (from January 6, 2003 until March 6, 2003) to allow the Pilot to continue in effect on an uninterrupted basis and to permit customers to continue trading SFCs in securities accounts while the Exchange considered the comments discussed below that it had received on the Pilot.²¹

Discussion of Comments Received

On December 9, 2002, the Chicago Board Options Exchange, Incorporated ("CBOE") submitted a comment letter with regard to the Exchange's margin rules for SFCs.²² In its letter, the CBOE requested that the Commission not grant permanent approval of the amendments to NYSE Rule 431 as proposed and approved on a pilot basis, unless the Exchange amended the rule to exempt SFCs from its day trading provisions and deleted references to the term "bona fide" in connection with market maker or specialist transactions.

In addition, as proposed, the Exchange's day trading margin requirements would apply to SFCs carried in securities accounts. The CBOE believed that day trading provisions should not apply to such accounts because it would create a disparity that the CFMA was designed to eliminate. In this regard, CBOE's letter stated that the SEC and CFTC did not impose day trading margin requirements to SFCs carried in futures and securities accounts. Since similar margin rules recently approved by the Commission do not impose day trading margin requirements on SFCs carried in futures account, the CBOE stated that permanent approval of the Exchange's proposed rule would lead to a regulatory disparity the CFMA was designed to prevent.

The Exchange is now seeking to adopt, on a permanent basis, margin requirements for SFCs carried in securities accounts, with proposed text

modifications from the Pilot based on the comments received and as discussed below.

In proposing its rule amendment on the application of day trading margin requirements to SFCs carried in securities accounts, the Exchange did not intend to create a regulatory disparity with other SROs' rules. However, the Exchange notes that an SRO's rules can be more stringent than those of the Commission. In proposing rules, the Exchange is guided by Commission rules and has latitude to promulgate more stringent rules, which it believes are necessary for the protection of investors. In this regard, NYSE believes that the application of the day trading margin requirements of NYSE Rule 431 as applied to SFCs carried in a securities account is consistent with the treatment of all securities transacted in a margin account under this rule. Accordingly, the Exchange will propose to apply the day trading margin requirements to SFCs carried in a securities account.

The CBOE also believes that the Exchange should delete the term "bona fide" in connection with market maker or specialist transactions. CBOE commented that the Exchange does not define the term "bona fide" nor does it use the term in relation to the other provisions of its margin rule relating to market maker and specialist transactions.

In response to CBOE's comments, the Exchange is proposing to amend the rule text by deleting the term "bona fide" in connection with specialist or market maker transactions. In proposing such language under the pilot program, it was the Exchange's intent to permit good faith margin treatment for offsetting positions that were effected by specialists or market makers in discharging the primary responsibilities noted above in its original filing, rather than to permit persons other than qualified market makers to act in such a capacity—hence the term "bona fide" in connection with specialist and market making transactions. Upon consideration, and in order to be consistent with similar rules proposed by other SROs,²³ the Exchange will not use the term "bona fide" in connection with specialist and market making transactions and instead the Exchange proposes to incorporate the definition of a SFD in Exchange Act Rule 400(c)(2)(v)²⁴ to clarify what constitutes a SFD for purpose of the rule.

Notwithstanding this amendment, the Exchange reiterates that good faith margin treatment be permitted for transactions effected by SFDs in discharging their responsibilities and obligations to maintain fair and orderly markets, and to provide liquidity to the marketplace.

2. Statutory Basis

The basis under the Exchange Act for this proposed rule change is section 6(b)(5) of the Act,²⁵ which requires, among other things, that an exchange have rules that are 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. The Exchange believes that the proposed rule change is designed to accomplish these goals by permitting customers to trade SFCs in securities accounts.

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

The Exchange 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

The Exchange notes that it received written comments on the original proposed rule change that was filed with the Commission on October 23, 2002, and thereafter amended on November 6, 2002. The Exchange has responded to such comments, and hereby amends its proposed rule change, which was approved by the Commission as a pilot program.

III. 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

²¹ See *supra* note .

²² See letter from Edward J. Joyce, President and Chief Operating Officer, CBOE, to Jonathan G. Katz, Secretary, Commission, dated December 9, 2002.

²³ See e.g., Securities Exchange Act Release No. 46711 (November 5, 2002), 67 FR 68710 (November 12, 2002).

²⁴ 17 CFR 240.400(c)(2)(v).

²⁵ 15 U.S.C. 78f(b)(5).