

Redemption Amount per Unit will equal:

$$\$10 \times \left(\frac{\text{Ending Value}}{\text{Starting Value}} \right)$$

If the Ending Value is greater than the Starting Value, the Redemption Amount per Unit will equal:

$$\$10 + \left(\$30 \times \left(\frac{\text{Ending Value} - \text{Starting Value}}{\text{Starting Value}} \right) \right)$$

provided, however, the Redemption Amount cannot exceed the Capped Value.

The Notes are cash-settled in U.S. dollars and do not give the holder any right to receive a portfolio security, dividend payments or any other ownership right or interest in the portfolio or index of securities comprising the Index. The Notes are designed for investors who want to participate or gain exposure to the Index, subject to a cap, and who are willing to forego market interest payments on the Notes during such term. The Commission has previously approved the listing of options on the Index.⁷ The Commission has also previously approved the listing of securities with a structure identical to that of the Notes.⁸

The Index is currently composed of 17 U.S. companies primarily involved in the design, distribution, manufacture, and sale of semiconductors.⁹ The Index was set to an initial value of 200 on December 1, 1993 and was split two-for-one on July 24, 1995. The Index is maintained by the Philadelphia Stock Exchange ("PHLX"). The PHLX may change the composition of the Index at any time, subject to compliance with the maintenance criteria discussed herein, to reflect the conditions in the

semiconductor industry. If it becomes necessary to replace a security in the Index, the PHLX will replace the security with a stock which the PHLX, in its discretion, believes would be compatible with the intended market character of the Index.¹⁰ In making replacement determinations, the PHLX will also take into account a security's capitalization, liquidity, volatility, and name recognition of the proposed replacement. Further, securities may be replaced in the event of certain corporate events, such as takeovers or mergers that change the nature of the security. If, however, the PHLX determines to increase the number of Index component securities to greater than 21 or reduce the number of Index component securities to fewer than 11, the PHLX will submit a rule filing with the Commission pursuant to section 19(b) of the Act. In addition, in choosing replacement securities for the Index, the PHLX will be required to ensure that at least 90% of the weight of the Index continues to be made up of stocks that are eligible for standardized options trading.

The Index is a price-weighted index and reflects changes in the prices of the component securities relative to the Index's base date of December 1, 1993. Specifically, the Index value is calculated by adding the prices of the component stocks, dividing this summation by a divisor that is equal to the number of the components of the Index to get the average price, and multiplying the resulting number by 100. To maintain the continuity of the Index, the divisor will be adjusted to reflect non-market changes in the prices of the component securities as well as changes in the composition of the Index. Changes that may result in divisor adjustments include, but are not limited to, stock splits and dividends, spin-offs, certain rights issuances, and mergers and acquisitions.

As of March 24, 2003, the market capitalization of the portfolio of securities representing the Index ranged from a high of \$118.1 billion to a low of \$893.9 million. The average daily trading volume for the last six months, as of March 17, 2003, ranged from a high of 53.6 million shares to a low of 2.2 million shares.

Nasdaq states that, the PHLX has represented that the Index value will be updated at least once every 15 seconds during the trading day.¹¹ The updated Index values will be disseminated and displayed by means of primary market prints reported by the Consolidated Tape Association. Merrill Lynch also represented that it will maintain and disseminate the updated Index values every 15 seconds through a third-party provider if PHLX ceases to maintain and disseminate the updated Index values every 15 seconds.¹² If Merrill Lynch, however, fails to maintain and disseminate the updated Index values according to the above representation, Nasdaq represented that it will delist the Notes.¹³

Under NASD rule 4420(f), Nasdaq may approve for listing and trading innovative securities, which cannot be readily categorized under traditional listing guidelines.¹⁴ Nasdaq proposes to list for trading notes based on the Index under NASD rule 4420(f).

Criteria for Initial and Continued Listing

The Notes, which will be registered under section 12 of the Act, will initially be subject to Nasdaq's listing criteria for other securities under NASD rule 4420(f). Specifically, under NASD rule 4420(f)(1):

(A) The issuer shall have assets in excess of \$100 million and stockholders' equity of at least \$10 million.¹⁵ In the case of an issuer which is unable to satisfy the income criteria set forth in

⁷ See Securities Exchange Act Release Nos. 38157 (January 10, 1997), 62 FR 2707 (January 17, 1997) (approving the listing and trading of European-style options on the Index); 34546 (August 4, 1994), 59 FR 43881 (August 18, 1994) (approving the listing and trading of options and long-term options on the Index).

⁸ See Securities Exchange Act Release Nos. 47464 (March 7, 2003), 68 FR 12116 (March 13, 2003) (approving the listing and trading of Market Recovery Notes Linked to the S&P 500 Index); 47009 (December 16, 2002), 67 FR 78540 (December 24, 2002) (approving the listing and trading of Market Recovery Notes linked to the Nasdaq-100 Index); and 46883 (November 21, 2002), 67 FR 71216 (November 29, 2002) (approving the listing and trading of Market Recovery Notes linked to the Dow Jones Industrial Average).

⁹ As of March 24, 2003, the portfolio of securities comprising the Index consisted of: Advanced Micro Devices, Inc.; Altera Corporation; Applied Materials, Inc.; Broadcom Corporation; Intel Corporation; KLA-Tencor Corporation; Lattice Semiconductor Corporation; Linear Technology Corporation; LSI Logic Corporation; Maxim Integrated Products, Inc.; Micron Technology, Inc.; Motorola, Inc.; National Semiconductor Corporation; Novellus Systems, Inc.; Teradyne, Inc.; Texas Instruments, Incorporated; and Xilinx, Inc.

¹⁰ The PHLX has represented that any replacement or additional component securities will be listed and traded on either the New York Stock Exchange, Inc. ("NYSE"), the American Stock Exchange LLC ("Amex") or quoted on and traded through the Nasdaq National Market. See Securities Exchange Act Release No. 34546 (August 18, 1994), 59 FR 43881 (August 25, 1994) (SR-PHLX-94-02).

¹¹ *Id.*

¹² Telephone conversation between John D. Nachmann, Senior Attorney, Nasdaq, and Hong-Ahn Tran, Special Counsel, Division of Market Regulation ("Division"), Commission, on April 18, 2003.

¹³ *Id.*

¹⁴ See Securities Exchange Act Release No. 32988 (September 29, 1993); 58 FR 52124 (October 6, 1993) (order approving File No. SR-NASD-93-15), (the "1993 Order").

¹⁵ Merrill Lynch satisfies this listing criterion.