

filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change that would establish an allocation plan for market maker appointments and accompanying deposit requirements related to the Exchange's proposed options trading facility, Boston Options Exchange ("BOX").³ On August 7, 2003, the Exchange's rule proposal was published for comment in the **Federal Register**.⁴ No comment letters were received on the proposal. On October 2, 2003, BSE submitted Amendment No. 1 to the proposed rule change.⁵ This order approves the proposal, publishes notice of Amendment No. 1, and approves Amendment No. 1 on an accelerated basis.

II. Description of Proposal

The BSE proposes that it would ultimately not restrict the number of market makers assigned per class in its proposed BOX market model. Nevertheless, BSE proposes a six-month plan to allocate assignments to a limited number of firms to make markets in the initial 250 classes traded on BOX.⁶ Specifically, BOX would phase in trading for the top 250 classes by limiting the number of market maker assignments to 1,911, during the first three months of trading. All remaining assignments requested prior to the commencement of trading on BOX would be assigned by BSE to prospective market making firms on a class-by-class basis during the following three months. In this regard, the Exchange proposes to add to its rules new Chapter XXXVII, which sets forth the initial allocation process for BOX

market maker appointments and accompanying deposit requirements.

Under the proposal, BSE would request that prospective market maker firms declare their interest for the initial market making assignments, and provide information regarding their prior experience as a market maker on an automated market and their capital commitment to options activities. In addition, prospective market maker firms would deposit funds with BSE based on their requested assignments.

To begin the initial allocation, BSE would allocate 889 assignments to experienced firms.⁷ BSE would assign firms to a class based on the firms' requests unless the number of requests for a particular class exceeds the number of assignments available. In that case, the BSE would use a random lottery whereby names would be drawn from a pool of all experienced firms requesting a class until the assignments available in that class are allocated. BSE represents that the random lottery would be externally audited to verify its integrity, neutrality, and fairness.

Following the allocation to experienced firms, BSE would allocate 1,022 assignments to all other prospective market making firms, including any experienced firms that did not receive assignments for all of their requested classes in the lottery. BSE would also allocate these 1,022 assignments by request unless the demand for a particular class exceeds the number of assignments available, in which case BSE would allocate assignments using a random lottery. Any prospective market making firms that do not receive a requested allocation in the 1911 assignments allocated for the first three months of trading would be placed on a waiting list and would be allocated their requested assignments within six months of the launch of the BOX market.⁸

All assignments to prospective market making firms would be subject to such an applicant's approval as an Options Participant⁹ and a market maker on BOX. In addition, any applicant denied any privilege under the allocation process, including denial of acceptance

as an "experienced" market maker, could appeal such decision according to the procedures set forth in BSE Chapter XXX, Disciplining of Members, Denial of Membership.

At the time a market maker's assignments become available to trade on BOX, deposits for those assignments would be released to BOX and would be nonrefundable, and considered as pre-paid fees credited against such market maker's BOX account to offset trading, technology and other related fees and charges.¹⁰ Before any class becomes available for trading for a particular market maker, if the applicant notifies BSE that it wishes to drop certain allocated classes, BSE would refund fifty percent of the related deposit.

The proposed allocation plan would apply on a pilot basis set to expire no later than six months beyond the initial launch date of the BOX market. Following the pilot period, the BSE would no longer limit the number of market makers assigned per class.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 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 Room. Copies of such filings will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-BSE-2003-13 and should be submitted by November 12, 2003.

IV. Discussion

After careful review, the Commission 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 exchange¹¹ and, in particular, the requirements of Section 6 of the Act.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release Nos. 47186 (January 14, 2003), 68 FR 3062 (January 22, 2003) and 48355 (August 15, 2003), 68 FR 50813 (August 22, 2003) (SR-BSE-2002-15).

⁴ See Securities Exchange Act Release No. 48271 (August 1, 2003), 68 FR 47113.

⁵ See letter from George W. Mann, Jr., Executive Vice President and General Counsel, BSE, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated October 1, 2003 ("Amendment No. 1"). In Amendment No. 1, the Exchange clarified that it would use Options Clearing Corporation volume statistics from January 2003 through June 2003 for the initial allocation. The Exchange made several technical modifications to the rule text to reflect this clarification. In addition, the Exchange amended the proposal to clarify that all applicants would receive their requested assignments within six months of the launch of the BOX market.

⁶ The top 250 classes would be determined based on Options Clearing Corporation volume statistics from January 2003 through June 2003. See Amendment No. 1, *supra* note 5.

⁷ A prospective market making firm would qualify as experienced if it has been a market maker or specialist on an organized fully automated market for a minimum of fifty classes for at least six months and has sufficient capital committed to its options activities to effectively support an automated market in BOX, as determined by the BSE. See proposed BSE Chapter XXXVII, Section 1(b).

⁸ See Amendment No. 1, *supra* note 5.

⁹ See proposed BOX Rules, Chapter I, General Provisions, Section 1(a)(39) (definition of "Options Participant").

¹⁰ See Amendment No. 1, *supra* note 5.

¹¹ The Commission has considered the proposed rules' impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).