

discussion of the risks that may be associated with the Notes in addition to details on the composition of the Index and how the rates of return will be computed. In particular, Nasdaq will advise members recommending a transaction in the Notes to: (1) Determine that such transaction is suitable for the customer; and (2) have a reasonable basis for believing that the customer can evaluate the special characteristics of, and is able to bear the financial risks of, such a transaction. Based on these factors, the Commission finds that the proposal to trade the Notes is consistent with section 15(b)(6) of the Act.<sup>23</sup> The Commission also notes that Merrill Lynch will deliver a prospectus in connection with the initial purchase of the Notes.

The Commission notes that the Notes are dependent upon the individual credit of the issuer, Merrill Lynch. To some extent this credit risk is minimized by Nasdaq's listing standards in Rule 4420(f), which provide the only issuers satisfying substantial asset and equity requirements may issue securities such as the Notes. In addition, Nasdaq's "other securities" listing standards further require that the Notes have at least \$4 million in market value.<sup>24</sup> In any event, financial information regarding Merrill Lynch, in addition to the information on the Underlying Index, will be publicly available.<sup>25</sup>

The Commission also has a systemic concern, however, that a broker-dealer, such as Merrill Lynch, or a subsidiary providing a hedge for the issuer will incur position exposure. However, as the Commission has concluded in previous approval orders for other hybrid instruments issued by broker-dealers,<sup>26</sup> the Commission believes that this concern is minimal given the size of the Notes issuance in relation to the net worth of Merrill Lynch.

The Commission also believes that the listing and trading of the Notes should

not unduly impact the market for the component securities of the Underlying Index or raise manipulative concerns. The Commission notes that Amex maintains the Select Ten Index and states that it has sole discretion in determining, calculating, and maintaining the Index. The Commission notes that Nasdaq is relying on Amex to calculate continuously and disseminate the Index value every fifteen seconds over the Consolidated Tape Association's Network B. The Commission considers the dissemination of this Index value important to this product's approval and expects Nasdaq to be ultimately responsible for such dissemination.<sup>27</sup> The Commission also notes that Amex could discontinue publication of the Select Ten Index and Amex or another entity could publish a successor or substitute index that the calculation agent,<sup>28</sup> in its sole discretion, could deem a comparable successor index. Also, Amex could discontinue publication of the Select Ten Index and the calculation agent could not select a successor index. In such a case, the calculation agent will compute a substitute value for the Select Ten Index in accordance with the procedures last used to calculate the Select Ten Index before any discontinuance. If Amex discontinues publication of the Select Ten Index before the period during which the Redemption Amount is to be determined and the calculation agent determines that no successor index is available at that time, then on each business day until the earlier to occur of (1) the determination of the Ending Value or (2) a determination by the calculation agent that a successor index is available, the calculation agent will determine the value that would be used in computing the Redemption Amount as if that day were a calculation day. The Commission notes that these risks should be disclosed in the circular that Nasdaq provides to its members.

The Commission also notes that, at the outset, securities in the Select Ten Index will represent approximately an equal percentage of the starting value of the Index, but the Index will only be

rebalanced on an annual basis. The Commission notes that the Select Ten Index is composed of stocks with significant market capitalization and average daily trading volume. The portfolio of securities underlying the Index will be rebalanced annually so as to include the ten highest dividend yielding stocks in the DJIA.

In addition, Nasdaq's equity margin rules and debt trading rules will apply to the Notes. The Commission believes that the application of these rules should strengthen the integrity of the Notes. The Commission also believes that Nasdaq has appropriate surveillance procedures in place to detect and deter potential manipulation for similar index-linked products. By applying these procedures to the Notes, the Commission believes that the potential for manipulation of the Notes is minimal, thereby protecting investors and the public interest. The Commission further notes that the underlying measure on which the Select Ten Index is based (the DJIA), is broad-based and independent of both Nasdaq and the Issuer, factors that the Commission believes should act to minimize the possibility of manipulation.

Nasdaq has requested that the Commission find good cause for approving the proposed rule change, as amended, prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. Nasdaq has requested accelerated approval because this product is similar to several other instruments currently traded on Nasdaq. In determining to grant the accelerated approval for good cause, the Commission notes that it has previously approved the listing of securities and options on securities the performance of which has been linked to or based on an index of the top dividend yielding stocks of the DJIA. Additionally, the Notes will be listed pursuant to existing hybrid security listing standards as described above. Based on the above, the Commission finds good cause to accelerate approval of the proposed rule change, as amended, prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**.

It is therefore Ordered, pursuant to section 19(b)(2) of the Act,<sup>29</sup> that the proposed rule change, as amended (SR-NASD-2003-20) is hereby approved on an accelerated basis.

<sup>23</sup> 15 U.S.C. 78o-3(b)(6).

<sup>24</sup> See NASD Rule 4420(f)(1).

<sup>25</sup> The companies that comprise the Select Ten Index are reporting companies under the Act, and the Notes will be registered under section 12 of the Act.

<sup>26</sup> See, e.g., Securities Exchange Act Release Nos. 44913 (October 9, 2001), 66 FR 52469 (October 15, 2001) (order approving the listing and trading of notes whose return is based on the performance of the Nasdaq-100 Index) (File No. SR-NASD-2001-73); 44483 (June 27, 2001), 66 FR 35677 (July 6, 2001) (order approving the listing and trading of notes whose return is based on a portfolio of 20 securities selected from the Amex Institutional Index) (File No. SR-Amex-2001-40); and 37744 (September 27, 1996), 61 FR 52480 (October 7, 1996) (order approving the listing and trading of notes whose return is based on a weighted portfolio of healthcare/biotechnology industry securities) (File No. SR-Amex-96-27).

<sup>27</sup> Nasdaq represents that, in the event that Amex discontinues the publication of the Select Ten Index, Nasdaq will facilitate the calculation and dissemination every 15 seconds of a value of a successor index either through the facilities of Nasdaq or those of an outside provider that is an independent calculation agent (e.g., not Merrill Lynch), unless otherwise approved by the Commission. See Amendment No. 1, *supra* n. 3.

<sup>28</sup> The Commission notes that in approving this product any such calculation agent that calculates and disseminates the value of a comparable successor index should be independent of the issuer of the Notes.

<sup>29</sup> 15 U.S.C. 78s(b)(2).