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BY ELECTRONIC FILING

Nancy M. Morris  
Secretary  
United States Securities and Exchange Commission  
100 F. Street, N.E.  
Washington, D.C. 20549

Re: File No. SR-AMEX-2007-85; Release No. 34-56236

Dear Ms. Morris:

The American Stock Exchange LLC (“Amex” or the “Exchange”) writes to respond to the September 5, 2007 comment letter (the “Letter”) jointly submitted by four of the eight Amex equity specialist firms (the “Specialists”) in response to the above-referenced proposal to create a new class of off-floor market makers in ETFs and equities called Designated Amex Remote Traders (“DARTs”).

The Bulk of the Specialists’ Criticisms Do Not Implicate Regulatory Concerns

The Specialists devote the first eight (8) pages of the Letter to purely business-side critiques of how best to allocate Amex resources to craft a market structure that will best ensure Amex’s future success.<sup>1</sup> The Specialists believe that a pure specialist-based market structure is superior to a more open one including specialists and additional market makers, that adding DARTs to Amex somehow will degrade market quality and injure Amex’s competitive position, and that Amex should devote its scarce resources to different needs the Specialists perceive. However, Amex management believes that, in the post-Regulation NMS world, it is essential that Amex’s existing structure be enhanced by the introduction of additional quoting participants, while preserving those aspects of the specialist system that order flow providers

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<sup>1</sup> The Specialists also claim in the penultimate paragraph of the Letter that they would like to know more about certain business, not regulatory, aspects of the DARTs program. Amex respectfully submits that the rule filing itself evidences that sufficient detail has been disclosed about the proposal. For example, the Specialists want to know “the number of securities in which a DART will be allowed to make a market” even though the proposed rule *explicitly states*: “There is no limitation on the number of such securities in which a DART may make markets.”

still value. Combined with other changes to Amex's market structure, Amex management believes the addition of DARTs will create additional resident liquidity at the Amex needed to better compete with other trading centers for order flow.

In any event, the above-described differences between Amex management's and the Specialists' business judgment do not provide a *regulatory* basis for the Commission to act. Amex should be accorded latitude to exercise the business judgment of its management and board as to market structure changes intended to benefit investors. So long as the requirements of the 1934 Act, and the regulations thereunder, are satisfied, Amex management submits that the Specialists' entreaties for the Commission to wade into Amex non-regulatory business matters should be rejected. Putting this general market-structure debate aside, the discrete regulatory concerns raised in the Letter are addressed below.

#### The DARTs Proposal Was Duly Authorized By the Amex Membership Corporation Board of Directors ("MC Board")

Section 1(j) of Article IV of the Amex Constitution prohibits the Amex Board of Governors ("Amex Board") from authorizing issuance of any new forms of trading privileges without obtaining the consent of the Amex Membership Corporation ("MC") *in accordance with the terms of the MC's certificate of incorporation*. The Specialists claim that the approval of the DARTs proposal without an MC shareholder vote violates this provision. However, such a vote was unnecessary because the MC certificate of incorporation was amended to affirmatively remove such requirement via rule filing approved by the Commission on March 20, 2006.<sup>2</sup> Since then, only the approval of the MC Board is required for issuance of new trading rights.<sup>3</sup> The MC Board in fact unanimously approved the DARTs proposal for both ETFs and equities on June 29, 2007.

#### Net Capital Rule Requirements Will Be Satisfied

Rule 110A—AEMI(a)(viii), addressing the net capital requirements applicable to DARTS, is similar to NYSEArca's rule applicable to Equity Trading Permit Holders<sup>4</sup>, in that both contain a reference to whether an equity trader is subject to Rule 15c3-1 under the Exchange Act (the "Net Capital Rule"). The Specialists argue, because there is no current exemption for equity or ETF market makers from the Net Capital Rule, that Rule 110A—AEMI(a)(viii) is confusing and should be removed. However, the proposed rule text merely leaves open the possibility of a future change to the Net Capital Rule, and should not create any possible misunderstanding among the relatively sophisticated member organizations that are likely to seek DART status as to its current applicability. In any event, prior to receiving Amex approval to operate as a DART, any proposed DART will be subject to a detailed review, including, as appropriate, meetings with the Financial Regulation Department of the FINRA Amex Regulation Division about compliance with the Net Capital Rule, as applicable.

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<sup>2</sup> 71 F.R. 15231 (March 27, 2006)(Release No. 34-53525; File No. SR-Amex-2005-117).

<sup>3</sup> *Id.*

<sup>4</sup> See NYSE Arca Rule 4.1

### Specialist Stabilization Rules Should Not Apply to DARTs

The Specialists suggest that equity (but not ETF) DARTs should be subject to the same stabilization rules that are applicable to equity specialists. However, DARTs do not have the same agency obligations or perceived time and place informational advantages (albeit small) that specialists do, so stabilization obligations equivalent to those of specialists would be inappropriate.<sup>5</sup> Rather, the significant obligations contained in proposed Rule 110A—AEMI(b)(i)-(ii) (similar to the obligations of registered traders on the Amex, and those of other non-specialist market makers in other major markets such as NASDAQ and NYSE Arca) are sufficient for both equity and ETF DARTs. These include the obligations to:

- provide continuous two-sided quotations in all assigned securities;
- have their transactions constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market in each such security;
- make competitive bids and offers as reasonably necessary to contribute to the maintenance of a fair and orderly market; and
- engage, to a reasonable degree under the existing circumstances, in dealings for his/her own account when there exists a lack of price continuity or a temporary disparity in supply and demand for a security.

Moreover, the Specialists' point that equities present higher risks of price manipulation is not an issue with the introduction of DARTs, which, as noted above, do not possess any of the perceived informational advantages particular to specialists, and thus are in no better position to manipulate prices than any other non-specialist equity market participant.<sup>6</sup>

### DARTs Will Be Subject to Regulation M and Rule 193—AEMI To the Extent Applicable

The Specialists have requested clarification as to how Regulation M and Amex Rule 193 will apply to DARTs, in light of the language contained in proposed Rule 110A—AEMI(c)(ii) dealing with required information barriers to prevent misuse of material non-public information. When Amex implements the DARTs program, it may choose to issue a member notice clarifying obligations thereunder, but it sees no need to complicate Rule 110A—AEMI itself with lengthy advisory opinions on such matters at this time. However, Amex does point out that:

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<sup>5</sup> For example, specialists currently are the only market participants able to see the cumulative size of reserve orders and existing stop orders on the AEMI Book. As the Exchange's market continues to evolve and the remaining informational advantages of equity specialists are reduced or eliminated, such changes may justify modification or elimination of specialist stabilization requirements. In the interim, however, it would be entirely inappropriate to apply these requirements to a new class of off-floor market participants that do not have such informational advantages.

<sup>6</sup> The specialists also mis-cite Release 34-49087, SR-Amex-2002-116 (January 15, 2004) for the proposition that stabilization rules were, because of the lesser risk of manipulation in ETFs and other derivatively priced securities, eliminated for registered traders. The filing actually only dealt with elimination of stabilization rules for ETF specialists.

- Regulation M applies to DARTs in the same way it applies to any other market participants.
- Amex Rule 193 applies to a DART to the extent the DART is affiliated with a specialist member organization, and no expansion of the application of Amex Rule 193 (including provisions requiring pre-approval of information barriers) beyond current practice is intended.<sup>7</sup>

#### Floor Officials Will Be Able To Interact with DARTs

The Specialists also question how DARTs will interface with Amex's Floor Officials in the case of trade disputes. To clarify, the Exchange intends to handle disputes involving DARTs substantially in accordance with existing procedures used for Supplemental Registered Options Traders ("SROTs"), another off-floor market participant.<sup>8</sup> DARTs accordingly will be required to designate persons on and/or off-floor to be in direct real-time contact with Floor Officials on such matters.

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<sup>7</sup> The language in Rule 110A—AEMI(c)(ii) cross-referencing Amex Rule 193 is substantively identical to language also contained in Amex Rules 993—ANTE(d)(iii) (Supplemental Registered Options Traders) and 994—ANTE(d)(iii) (Remote Registered Options Traders), neither of which have been interpreted to expand the applicability of Amex Rule 193 beyond affiliates of specialists.

<sup>8</sup> The relevant portion of the current Amex service desk written procedures manual provides:

SROTs transmit proprietary option quotation data and send orders from off-floor facilities but have floor representation through their affiliated Member Firm or Clearing entity. The Amex Service Desk (SD) handles SROT order and quote issues similarly to all customers. SD personnel have direct contact to the SROTs through phone and email. An SROT can request a trade review under Obvious Error rules through initial contact with the SD. A SD representative will time stamp the request, notify an Amex Trading Official, inform the Trading Floor Regulatory Liaison Group (TFRLG), inform the floor representative, as applicable, research the orders, and present details to the TFRLG. The SD serves as the liaison between the SROT and floor activity, and in all situations requiring TFRLG and Floor Official involvement. The SD, in a customer service capacity, will present all data and communicate the SROT requests and follow-up detail to the appropriate parties. Documentation associated with corrective actions and/or floor rulings is presented to the SROT's on-floor representation for signature/stamp of approval and relevant documentation is recorded and saved. In situations involving clearly erroneous transactions or other events involving the SROT (although not initiated by the SROT), it is the Amex SD that will contact the SROT (via phone or email) to provide notification of a possible dispute involving one or more SROT trades.

A similar provision relating to DARTs will be added to the manual. However, Amex has recently filed a proposed rule making an on-floor presence to resolve trade disputes optional, with an off-floor presence to resolve disputes mandatory. If this rule change is approved by the Commission, corresponding changes will be made to the manual. See "Proposal to Amend the Process of Resolving Uncompared Transactions," SR-Amex-2007-56, Amendment 1 (filed September 18, 2007).

Surveillance Program Details Will Be Addressed Confidentially By Amex With Responsible SEC and Amex Regulation Staff, Not In Public Filings

Curiously, the Specialists devote an entire page of their Letter to attack a single paragraph in the rule filing dealing with surveillance of DARTs. The Specialists demand more details and accuse Amex of having not thought through its surveillance program by virtue of the absence of particulars in the rule filing. However, Amex included the short discussion to generally explain the nature of its surveillance program for DARTs and to indicate that certain adjustments might be needed, not to provide a point-by-point explanation of same. Nor would any responsible SRO that wanted to maintain the efficacy and integrity of its surveillance programs provide in a public filing (in a response to a comment letter) a roadmap to their construction and operation. When the DARTs program is implemented, regulatory compliance will be achieved by a comprehensive non-public plan approved by appropriate regulatory personnel.

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We trust the foregoing adequately addresses the comments of the Specialists. Should the Staff have further questions, Amex will be happy to address them.

Respectfully submitted,

A handwritten signature in cursive script, reading "Charles P. McKeath". The signature is written in dark ink and is positioned below the typed name "Charles P. McKeath".