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Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Comments Regarding Nasdaq Stock Market LLC's Proposal to Establish Rules Governing the Trading of Options on the Nasdaq Options Market (SR-Nasdaq-2007-004)

Dear Ms. Morris:

The American Stock Exchange, LLC ("Amex" or "Exchange") appreciates this opportunity to comment on the proposal (the "Proposal") of the Nasdaq Stock Market LLC ("Nasdaq") concerning the establishment of rules governing the trading of options on the Nasdaq Options Market ("NOM"). The Exchange believes that the NOM, as proposed, presents several operational issues as well as other market structure issues. Accordingly, we urge the Commission to address the issues noted below.

Proposed Chapter IV, Section 5

The Proposal provides that trading will open in series of options if there is a minimum of one (1) market maker registered for trading that particular series. The Commission in connection with recent options market approvals has typically required a more robust "trading crowd." For example, the Boston Options Exchange (the "BOX") proposal approved in 2004, required at least two (2) market makers in order for an options series to be opened and traded.[1] In addition, the International Securities Exchange, LLC (the "ISE") requires at least one (1) Primary Market Maker and at least two (2) Competitive Market Makers appointed to each options class traded at the ISE.[2] Given the order exposure requirements set forth in Chapter VII, Section 14, the Exchange submits that meaningful order exposure will not be effected with a "trading crowd" of less than two (2) market makers. In addition, the term "trading crowd"

[1] See Securities Exchange Act Release No. 49068 (January 13, 2004), 69 FR 2775 (January 20, 2004).
[2] See ISE Rule 802.

becomes a misnomer when such a "crowd" may potentially consist of a sole market maker. Chapter III, Section 4(f)(ii) in connection with "Crossed Orders" also uses the term "trading crowd" but fails to define it so that a "trading crowd" may potentially consist of one (1) market maker (a number far less than a "crowd"). We urge the Commission to require Nasdaq to amend its filing to require at least two (2) market makers for an options series to be listed and traded. In this manner, adequate depth and liquidity will be available to market participants.

Proposed Chapter VI, Section 5

Paragraph (b) of Section 5 of Chapter VI provides that the minimum trading increment for options traded on NOM will be one (1) cent for all series. Given that Nasdaq defines a "quote" or "quotation" as a bid or offer entered by a market maker as a "firm order" that updates a market maker's previous bid or offer, if any, we submit that quotes and orders are the same. The Amex believes that this Proposal to trade all options series in penny increments is inconsistent with the penny quoting pilot program (the "Penny Pilot") recently adopted by all options exchanges with the Commission's approval.[3] Only in the limited nature of the Penny Pilot, may options series be quoted in pennies. We urge the Commission to require Nasdaq to explain in an amendment how the proposed provision is consistent with existing options market structure.

Nasdaq also has taken the liberty to provide its "Order Imbalance Indicator" in penny increments. The Order Imbalance Indicator is a message disseminated about eligible interest and the prices at which such interest would execute at the time of dissemination. The Exchange believes that the proposed Order Imbalance Indicator in penny increments is inconsistent with the Penny Pilot and would be contrary to the measured manner in which the Commission has introduced options penny quoting. Accordingly, we submit that the Order Imbalance Indicator should be set forth in the appropriate minimum price variations and not penny increments.

Order Types

The Proposal provides that participants may enter limit orders to buy/sell options as attributable, non-attributable or non-displayed. The Exchange questions whether the concept of a "non-displayed" order (including the non-displayed portions of "reserve orders") is permissible in the options markets given the differing regulatory requirements as compared to equities. Given the limit order display requirements and the firm quote obligations required of all options exchanges,[4] we believe that the concept of a "non-displayed" order is inconsistent with these legal requirements and principles as well as the obligations required by the Options Linkage Plan.[5]

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3 See e.g. Securities Exchange Act Release No. 55162 (January 24, 2007), 72 FR 4738 (February 1, 2007)(Amex File No. SR-2006-106).

4 See e.g. Amex Rule 958A—ANTE.

5 See Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000), as subsequently amended. See also Securities Exchange Act Release No. 47297 (January 31, 2003), 68 FR 6526 (February 7, 2003)(Amex File No. SR-2002-84).

The market-on-close order or "MOC" is defined as an order to buy or sell at the market that is to be executed only during the Nasdaq Closing Cross. However, the provision in Chapter VI, Section 9(b)(3) regarding Closing Crosses states that an MOC may be unexecuted. Given that an MOC is a market order, the operation of the Closing Cross would alter the nature of a market order as generally understood by market participants. We believe that Nasdaq should better explain how the MOC will operate.

Nasdaq Closing Cross

The Proposal sets forth a Closing Cross for options that is similar to the Nasdaq's Closing Cross in equities. The proposed rules provide that the Closing Cross will begin processing at 4:00 p.m. Eastern time ("ET") but fails to provide a termination or end time. In addition, will the Closing Cross similarly begin at 4:00 p.m. ET for ETF and index options even though these products may trade until 4:15pm ET?

Order Routing

The Proposal provides that the NOM will ensure that orders designated to only execute within the system will not create a trade-through or locked or crossed market. Nasdaq fails to adequately describe how this will occur. For example, what would happen to an order that locks or crosses the NBBO? Will it remain on the NOM book until it is marketable? What will be the obligation and responsibility of Nasdaq for such order? In addition, if the market is already locked or crossed, what will the NOM do with an order that is delivered?

The Proposal sets forth different order routing attributes for "system" and "non-system" securities, however, a definition of a "non-system" security is not provided. If as described, a system security is all options meeting the criteria for listing, how would a "non-system" security be available? In addition, how are orders identified as system" or "non-system"? The options markets and market participants require greater clarity regarding this order routing mechanism.

In connection with the processing of orders, the Proposal provides that any potential price improvement resulting from execution in the system shall accrue to the taker of liquidity. (see Chapter VI, Section 10) It is unclear how this will occur? In addition, a "taker of liquidity" is not defined in the Proposal. We believe that a fuller description of this process is required in order for a reasoned review to properly occur.

One Point and 2 ½ Point Strike Price Pilot Programs

The Proposal identifies both the One-Point and 2 ½ Point Strike Price Pilot Programs (collectively, the "Pilot Programs") that the options exchanges have implemented. However, no details were provided on how the Pilot Programs will be administered once NOM is effective. For example, in the One-Point Strike Price Pilot Program, each options exchange is provided 5 options classes to designate. Each options exchange is then able to trade all the options classes designated by each exchange. In connection with the 2 ½ Point Strike Price Pilot Program, Nasdaq is not currently part of the program so that any change in options class allocations would require a proposed rule change with the Commission. In the absence of any details, we assume that Nasdaq expects to list and trade only those options classes in one-point and 2 ½ point strike intervals that are currently available under the Pilot Programs. In connection with the launch of the ISE and BOX, those exchanges did not change the 2 ½ Point Strike Price Pilot Program, but instead, traded only those options classes in 2 ½ point strike price intervals that were part of the existing program.

Position Limits

Nasdaq seeks to reduce the burden and costs of analyzing, updating and providing expertise regarding position limits by deferring to the rules of the Chicago Board Options Exchange, Inc. and/or the other options exchanges. We believe that each options exchange should be required to develop their own expertise and provide specific requirements in their own rules. This is essential for proper disclosure to members and in furtherance of the compliance and surveillance function of an exchange.

Further, in the section entitled "Self-Regulatory Organization's Statement on Burden on Competition," Nasdaq states that "Market participants that disagree and do not view these developments as pro-competitive, will have the flexibility to use only those functions that improve their trading or to not use the system at all; participation in the system in whole or in part is completely voluntary. " We disagree that the use of the system is completely voluntary. Based on broker-dealer duties of best execution and the Options Linkage responsibilities, market participants are required to take into account every options exchange/market. As such, market participants may be required by law to use the system or submit orders to the NOM.

What is an Index?

The Proposal provides a definition of an "index option" as either an options contract that is an option on an index of equity securities prices or a contract on a tradable instrument which tracks such prices. If by "tradable" instrument, Nasdaq means an exchange-traded fund ("ETF") or the like it should state so. However, an ETF is not itself an "index," but instead is a registered equity security under the Securities Act of 1933 that typically tracks the performance of an underlying benchmark index. Accordingly, the Exchange believes that an option on an ETF should not be characterized as an "index option." In addition, the hours of trading for index options set forth in Article VI, Section 2 permits trading until 4:15 p.m. Currently, the ability to extend index options trading to 4:15 p.m. is premised on whether the index is "broad-based." The Commission should confirm with Nasdaq whether this was an oversight.

In conclusion, the Amex believes that the Commission should require Nasdaq to revise the Proposal as set forth in this letter.

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If you have any questions, please contact me at (212) 306-2500 or Jeffrey P. Burns at (212) 306-1822.

Sincerely,

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cc: Erik Sirri, Director, Division of Market Regulation
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