

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-57400; File No. SR-Amex-2007-109)

February 29, 2008

Self-Regulatory Organizations; American Stock Exchange LLC; Order Granting Approval of a Proposed Rule Change as Modified by Amendment No. 1 Thereto Relating to the Trading of Exchange Traded Notes (ETNs)

I. Introduction

On October 9, 2007, the American Stock Exchange LLC (“Amex” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend Section 107 of the Amex Company Guide (“Company Guide”) to permit certain index-linked securities, commodity-linked securities, and currency-linked securities to trade under the rules applicable to exchange-traded funds (“ETFs”). On January 11, 2008, the Amex submitted Amendment No. 1 to the proposed rule change. The proposed rule change, as amended, was published for comment in the Federal Register on January 30, 2008.<sup>3</sup> The Commission received no comment letters on the proposal. This order approves the proposed rule change, as amended.

II. Description of the Proposed Rule Change

The Exchange proposes to amend Sections 107D, 107E and 107F of the Company Guide to permit certain index-linked securities (“Index-Linked Securities”), commodity-linked securities (“Commodity-Linked Securities”), and currency-linked securities (“Currency-Linked

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Securities Exchange Act Release No. 57187 (January 23, 2008), 73 FR 5604.

Securities”) (collectively, “Exchange-Traded Notes” or “ETNs”) that offer a weekly redemption feature to be traded subject to the AEMI trading rules specific to ETFs.

### Background

Securities listed pursuant to Section 107 of the Company Guide (“Section 107 Securities”) are debt securities of an issuer that typically provide for a cash payment at maturity, or if available, upon earlier redemption (such as a weekly redemption feature) at the holder’s option, based on the performance of an underlying index or asset. Permitted underlying assets for Index-Linked Securities include domestic and international equity indexes. Commodity-Linked Securities may be based on a commodity index, basket of commodities, or single commodity while Currency-Linked Securities may similarly be linked to a currency index, basket of currencies, or single currency.

Section 107 Securities typically have a term of at least one year but not greater than 30 years. The issuer may or may not provide for periodic interest payments to holders. The holder of a Section 107 Security may or may not be fully exposed to the appreciation and/or depreciation of the underlying asset.

A number of Section 107 Securities based on securities indexes that are listed and traded on the Exchange provide for a payment amount in a multiple of the positive index return or performance, subject to a maximum gain or cap. The Exchange’s generic listing standards for Section 107 Securities allow for the multiple performance on the upside but prohibit payment at maturity based on a multiple of the negative performance of an underlying asset. Section 107 Securities may or may not provide for a minimum guaranteed amount to be repaid, i.e., “principal protection.”

Section 107 Securities do not give the holder a right to receive the underlying asset or any other ownership right or interest in the underlying portfolio. The current value of the underlying asset is required to be widely disseminated at least every 15 seconds during the trading day.

Section 107 Securities are “hybrid” securities whose rates of return are largely the result of the performance of an underlying asset. In addition, prior to the listing and trading of Section 107 Securities, the Exchange typically highlights and discloses the special risks and characteristics of such security in an Information Circular.

#### Current Rules

Sections 107D,<sup>4</sup> 107E,<sup>5</sup> and 107F<sup>6</sup> of the Company Guide treat Index-Linked Securities, Commodity-Linked Securities and Currency-Linked Securities as equity instruments subject to the Exchange’s AEMI trading rules for equities. The only exception to this requirement is when a Section 107 Security is listed as a bond or debt (i.e., in \$1,000 denominations). In such a case, the Section 107 Security are be subject to Exchange rules applicable to bond or debt securities.<sup>7</sup>

Because the current Rules deem ETNs and other Section 107 Securities as “equity instruments,” the full range of AEMI trading rules specific to equities apply to all Section 107 Securities regardless of the particular structure of the Section 107 Security.

#### Proposal

With respect to an ETN that is continuously-offered with a weekly redemption option (such as BWV), the Exchange proposes that the AEMI trading rules applicable to ETFs (rather

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<sup>4</sup> See Securities Exchange Act Release No. 51563 (April 15, 2005), 70 FR 21257 (April 25, 2005) (SR-Amex-2005-001).

<sup>5</sup> See Securities Exchange Act Release No. 55794 (May 22, 2007), 72 FR 29558 (May 29, 2007) (SR-Amex-2007-45).

<sup>6</sup> Id.

<sup>7</sup> Id.

than equities) should equally apply to such ETN. In order to qualify, the ETN would be required to offer a weekly redemption option to holders (“Eligible ETNs”). The following rules specifically applicable to ETF trading would apply to the trading of Eligible ETNs:

- Rule 108—AEMI(c). The execution of Eligible ETN orders at the opening would be effected in the same manner as ETFs so that orders in Eligible ETNs would be executed before any broker-dealer bids or offers.
- Rule 110—AEMI(p). A Registered Trader in ETFs (including Eligible ETNs) would only actively quote ETFs traded on the same or contiguous panels for a maximum of three contiguous panels. A Registered Trader would also not actively quote more than a maximum of 15 ETFs (including Eligible ETNs). A Senior Floor Official of the Exchange may modify this restriction if a Registered Trader is able to appropriately fulfill his obligations to the market due to the level of activity in the ETFs and their proximity.
- Rule 128A—AEMI(d)(iv). Any quotation in an ETF entered into the AEMI platform by the specialist or Registered Trader while Auto-Ex is enabled that would cause the Amex Published Quote (APQ) to be locked or crossed would be automatically executed. In the case of a non-ETF Amex-listed security or a non-Nasdaq UTP equity security, quotations that are entered into the AEMI platform by the specialist while Auto-Ex is enabled that would cause the APQ to cross would be rejected. Therefore, Eligible ETNs would be automatically executed, rather than rejected, when a specialist or Registered Trader quotation causes the APQ to be locked/crossed when Auto-Ex is enabled.

- Rule 128A—AEMI(f)(iv). AEMI does not automatically execute non-ETF orders when the automatic execution of an order exceeds the price change parameters of the “1%, 2, 1, ½ point” rule. This rule does not apply to ETFs and would accordingly not apply to the trading of Eligible ETNs.
- Rule 131—AEMI(o). AEMI rejects “too marketable” non-ETF stop and stop limit orders. “Too marketable” is defined as a buy stop order received during the regular trading session with a stop price equal to the bid or lower, or a sell stop order received during the regular trading session with a stop price equal to the offer or higher. ETF stop orders that are “too marketable” are executed by AEMI under this Rule, and accordingly, Eligible ETN stop orders would similarly be executed.
- Rule 131—AEMI(r). AEMI does not accept electronic cross orders for non-ETFs and non-Nasdaq UTP securities. As a result, electronic cross orders are acceptable only for ETFs. As proposed, electronic cross orders for Eligible ETNs would be acceptable in AEMI.
- Rule 154—AEMI(c)(i). The Stop Order Rule requires floor official approval prior to the specialist electing a stop order by selling to the bid/buying on the offer. Prior floor official approval is not required for ETFs and would similarly not apply to Eligible ETNs.
- Rule 154—AEMI(c)(ii). Stop and stop limit orders in ETFs are elected by a quotation, although such orders in non-ETFs are not. Accordingly, stop and stop limit orders in Eligible ETNs would similarly be elected by quotation, pursuant to this rule.

- Rule 154—AEMI(e). Maximum price variation requirements are set forth in Rule 154—AEMI(e) (also known as the “1%-2, 1, .5 Point Rule). This Rule specifically provides that it does not apply to the trading of ETFs. Accordingly, Rule 154—AEMI(e) would similarly not apply to Eligible ETNs.
- Commentary .03 to Rule 170-AEMI. A specialist quotation, made for his own account, should be such that a transaction effected at his quoted price or within the quoted spread, whether having the effect of reducing or increasing the specialist’s position, would bear a proper relation, in the case of ETFs or other derivatively-based securities, to the value of underlying or related securities. Eligible ETNs would similarly be subject to this requirement.
- Commentary .11 to Rule 170—AEMI. Commentary .11 to Rule 170—AEMI specifically exempts ETFs from the stabilization requirements. Accordingly, Eligible ETNs would similarly be exempt.
- Rule 206—AEMI. This Rule prohibits a specialist from crossing the market for the purpose of electing odd-lots and requires floor official approval in various circumstances for non-ETFs. The exemption for ETFs would similarly apply to Eligible ETNs.

Eligible ETNs would also be subject to the same parity allocation as currently exists for ETFs and other equity-traded products that are not listed stocks, UTP stocks, or closed-end funds.

### III. Discussion

After careful consideration, 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 exchange<sup>8</sup> and, in particular, the requirements of Section 6(b) of the Act<sup>9</sup> and the rules and regulations thereunder. Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>10</sup> in that the proposal is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transaction in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest.

The Commission believes that the market price of Eligible ETNs should exhibit a strong correlation to the performance of the relevant underlying asset, since holders of such securities will be unlikely to sell them for less than their redemption value if they have a weekly right to be redeemed for their full value. This weekly redemption feature is similar to the daily redemption feature available in ETFs. In addition, Eligible ETNs are typically continuously offered, on a daily basis, so that the issuer would have the ability to issue new securities from time to time at market prices. This process is similar to the manner in which ETFs are continuously offered via the creation/redemption process in Creation Unit aggregations (*i.e.*, 50,000 shares).

Accordingly, the Commission believes the proposed rule change is consistent with the Act in permitting Eligible ETNs to trade subject to the Exchange's AEMI trading rules for ETFs.

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<sup>8</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>9</sup> 15 U.S.C. 78f(b).

<sup>10</sup> 15 U.S.C. 78f(b)(5).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>11</sup> that the proposed rule change (SR-Amex-2007-109), as modified, is hereby approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>12</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>11</sup> 15 U.S.C. 78s(b)(2).

<sup>12</sup> 17 CFR 200.30-3(a)(12).