

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-51337; File No. SR-Amex-2004-109)

March 9, 2005

Self-Regulatory Organizations; American Stock Exchange LLC; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change and Amendment Nos. 1, 2 and 3 thereto Relating to Split Price Priority

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> notice is hereby given that on December 23, 2004, the American Stock Exchange LLC (“Amex” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Amex. On February 4, 2005, the Amex amended the proposed rule change (“Amendment No. 1”).<sup>3</sup> On February 14, 2005, the Amex amended the proposed rule change (“Amendment No. 2”).<sup>4</sup> On March 8, 2005, the Amex amended the proposed rule change (“Amendment No. 3”).<sup>5</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons. In addition, the Commission is granting accelerated approval of the proposed rule change.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Amex seeks to amend Amex Rules 950 and 950 — ANTE to permit a limited

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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> In Amendment No. 1, the Amex restated the proposed rule change in its entirety.

<sup>4</sup> In Amendment No. 2, the Amex corrected a reference to the Options Trading Committee in proposed Commentary .06(b) to Amex Rule 950-ANTE(d).

<sup>5</sup> In Amendment No. 3, the Amex requested accelerated approval of the proposed rule change.

exception to the existing split price priority requirement. The text of the proposed rule change is set forth below. Proposed new language is in *italics*; deletions are in [brackets].

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## **Rule 950**

### **Rules of General Applicability**

(a) – (c) No change.

(d) The provisions of Rule 126, with the exception of subparagraphs (a) and (b) thereof, shall apply to Exchange option transactions and the following additional commentary shall also apply:

Commentary...

.01 - .04 No change.

.05 (a) **Purchase or Sale Priority.** If a member purchases (*sells*) one or more option contracts of a particular series at a particular price or prices such member shall, at the next lower (*higher*) price at which a member other than [an Exchange] a *floor* [B]broker or specialist representing a customer agency order entitled to priority pursuant to Rule 950(c), have priority in purchasing (*selling*) up to the equivalent number [(or a reasonably larger number)] of option contracts of the same series that he purchased (*sold*) at the higher (*lower*) price or prices, but only if his bid (*offer*) is made promptly and the purchase (*sale*) so effected represents the opposite side of a transaction with the same order or offer (*bid*) as the earlier purchase or purchases (*sale or sales*). This paragraph only applies to transactions effected in open outcry.

[Sale Priority. If a member sells one or more option contracts of a particular series at a particular price or prices, he shall, at the next higher price at which a member other than an Exchange Broker or specialist representing a customer agency order entitled to priority pursuant to Rule 950(c), have priority in selling up to the equivalent number (or a reasonable larger number) of option contracts of the same series that he sold at the lower price or prices, but only if

his offer is made promptly and the sale so effected represents the opposite side of a transaction with the same order or bid as the earlier sale or sales.]

**(b) Purchase or sale priority for orders of 100 contracts or more.** If a member purchases (sells) fifty or more options contracts of a particular series at a particular price or prices, such member shall, at the next lower (higher) price have priority in purchasing (selling) up to the equivalent number of option contracts of the same series that he purchased (sold) at the higher (lower) price or prices, but only if his bid (offer) is made promptly and the purchase (sale) so effected represents the opposite side of a transaction with the same order or offer (bid) as the earlier purchase or purchases (sale or sales). The Options Trading Committee may increase the “minimum qualifying order size” above 100 contracts for all products under its jurisdiction. Announcements regarding changes to the minimum qualifying order size shall be made via Regulatory Circular. This paragraph only applies to transactions effected in open outcry.

(c) Two or more members entitled to priority. If the bids or offers of two or more members are both entitled to priority in accordance with paragraph (a) or paragraph (b), it shall be afforded them insofar as practicable, on a pro-rata basis.

(d) Floor brokers are able to achieve split price priority in accordance with paragraphs (a) and (b) above. Provided, however, that a floor broker who bids (offers) on behalf of a non-market-maker Amex member broker-dealer (“Amex member BD”) must ensure that the Amex member BD qualifies for an exemption from Section 11(a)(1) of the Exchange Act or that the transaction satisfies the requirements of Exchange Act Rule 11a2-2(T), otherwise the floor broker must yield priority to orders for the accounts of non-members.

.06 - .07 No change.

(e) – (p) No change.

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**Rule 950—ANTE**

**Rules of General Applicability**

(a) – (c) No change.

(d) The provisions of Rule 126, with the exception of subparagraphs (a) and (b) of such Rule, shall apply to Exchange option transactions as modified by Commentaries .01 and .02 to Rule 950(c), and the following additional commentary shall also apply:

Commentary...

.01 - .05 No change.

.06 (a) **Purchase or Sale Priority** - For trades occurring outside the ANTE System only, if a member purchases (sells) one or more option contracts of a particular series at a particular price or prices such member shall, at the next lower (higher) price at which a member other than [an Exchange] a floor [B]broker or specialist representing a customer agency order entitled to priority pursuant to Rule 950—ANTE(c), have priority in purchasing (selling) up to the equivalent number [(or a reasonably larger number)] of option contracts of the same series that he purchased (sold) at the higher (lower) price or prices, but only if his bid (offer) is made promptly and the purchase (sale) so effected represents the opposite side of a transaction with the same order or offer (bid) as the earlier purchase or purchases (sale or sales). This paragraph only applies to transactions effected in open outcry.

[(b) **Sale Priority**- For trades occurring outside the ANTE System only, if a member sells one or more option contracts of a particular series at a particular price or prices, he shall, at the next higher price at which a member other than an Exchange Broker or specialist representing a

customer agency order entitled to priority pursuant to Rule 950—ANTE(c), have priority in selling up to the equivalent number (or a reasonable larger number) of option contracts of the same series that he sold at the lower price or prices, but only if his offer is made promptly and the sale so effected represents the opposite side of a transaction with the same order or bid as the earlier sale or sales.]

**(b) Purchase or sale priority for orders of 100 contracts or more.** If a member purchases (sells) fifty or more options contracts of a particular series at a particular price or prices, such member shall, at the next lower (higher) price have priority in purchasing (selling) up to the equivalent number of option contracts of the same series that he purchased (sold) at the higher (lower) price or prices, but only if his bid (offer) is made promptly and the purchase (sale) so effected represents the opposite side of a transaction with the same order or offer (bid) as the earlier purchase or purchases (sale or sales). The Options Trading Committee may increase the “minimum qualifying order size” above 100 contracts for all products under its jurisdiction. Announcements regarding changes to the minimum qualifying order size shall be made via Regulatory Circular. This paragraph only applies to transactions effected in open outcry.

(c) Two or more members entitled to priority. If the bids or offers of two or more members are both entitled to priority in accordance with paragraph (a) or paragraph (b), it shall be afforded them insofar as practicable, on a pro-rata basis.

(d) Floor brokers are able to achieve split price priority in accordance with paragraphs (a) and (b) above. Provided, however, that a floor broker who bids (offers) on behalf of a non-market-maker Amex member broker-dealer (“Amex member BD”) must ensure that the Amex member BD qualifies for an exemption from Section 11(a)(1) of the Exchange Act or that the transaction

satisfies the requirements of Exchange Act Rule 11a2-2(T), otherwise the floor broker must yield priority to orders for the accounts of nonmembers.

.07 No change.

(e) – (n) No change.

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II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change, as amended, and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item III below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Amex Rules 950(d), Commentary .05 and 950—ANTE(d), Commentary .06 establish priority principles for split-price transactions. Generally, a member buying (selling) at a particular price shall have priority over other members in purchasing (selling) up to an equivalent number of contracts of the same order at the next lower (higher) price. Awarding split price priority serves as an inducement to members to bid (offer) more aggressively for an order that may require a split-price execution by giving them priority at the next lower (higher) price point. For example, assume the market is \$1.00 - \$1.20, 300-up when a floor broker (“FB”) receives instructions from a customer that he/she would like to buy 500 options at a price or prices no higher than \$1.20. The FB could attempt to execute the order in open outcry at a

price better than the displayed market of \$1.20. Assume a Specialist is willing to sell 250 contracts at \$1.15 provided he/she can also sell the remaining 250 contracts at \$1.20. Under current rules, that Specialist could offer \$1.15 for 250 contracts and then, by virtue of the split price priority rule, he/she would have priority for the balance of the order (up to 250 contracts) over other crowd members. If executed, the resulting net price of \$1.175 is better than the current displayed market of \$1.20, which results in a better fill for the customers.<sup>6</sup>

One limitation on the ability of crowd participants to use the split price priority rule is the rule's requirement that orders in the limit order book ("book") have priority over the member attempting to fill the balance of the order at the split price. Using the example above, if the \$1.20 price represented orders in the book, those orders would have priority over the Specialist at \$1.20. This means that a Specialist who is willing to trade at \$1.15 and \$1.20 may be completely unwilling to trade at the better price of \$1.15 if he/she cannot trade the balance of the order at \$1.20 because of the requirement to yield to existing customer interest in the book. This jeopardizes the FB's ability to execute the first part of the order at a price of \$1.15, thereby potentially making it difficult to achieve price improvement for the customer on the Amex. Instead, the order may trade at another exchange that has no impediments, e.g., no customer interest at those price levels. Accordingly, the Exchange is proposing to adopt a limited exception to the existing priority requirement.

Under newly-proposed paragraph (b) to Rules 950(d), Commentary .05 and 950—ANTE(d), Commentary .06, a member with an order for at least 100 contracts who buys (sells) at least 50 contracts at a particular price shall have priority over all others in purchasing

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<sup>6</sup> If successful, two trades will be reported (at \$1.15 and \$1.20) and the net price result to the customer will be \$1.175.

(selling) up to an equivalent number of contracts of the same order at the next lower (higher) price.<sup>7</sup>

Using the above example, the Specialist trading at \$1.15 would have priority over members and orders in the book at \$1.20 to trade at \$1.20 with the balance of the order in the trading crowd. The Exchange believes the proposal will lead to more aggressive quoting by Specialists, which in turn could lead to better executions. As indicated above, a Specialist may be willing to trade at a better price for a portion of an order if he/she is assured of trading with the balance of the order at the next pricing increment. As a result, FBs representing orders in the trading crowd may receive better-priced executions. As proposed, the Options Trading Committee (consisting of Floor Governors, Heads of the Specialist Association, FB Association, and the Options Market Maker Association) will have the ability to increase the minimum qualifying order size to a number larger than 100 contracts. Any changes, which must apply to all products under the committee's jurisdiction, will be announced to the membership via Regulatory Circular.

The Amex believes it is reasonable to make a limited exception to the customer priority rule to allow split price trading. In this regard, the proposed exception is similar in operation to the limited priority exception that exists for complex orders (contained in Rules 950(d), Commentary .01 and 950—ANTE(d), Commentary .01). The complex order priority exception generally provides that a member affecting a qualifying complex order may trade ahead of the book on one side of the order provided the other side of the order betters the book. This

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<sup>7</sup> Orders for less than 100 contracts would be unaffected by this proposal. The Exchange also takes the opportunity to consolidate current paragraphs (a) and (b) of each of Commentary .05 to Amex Rule 950(d) and Commentary .06 to Amex Rule 950—ANTE(d) into one paragraph (paragraph (a) in each). This consolidation would not effect the operation of the rule in any way; it simply would make the rule shorter.



exception was intended to facilitate the trading of complex orders, which by virtue of their multi-legged composition could be more difficult to trade without a limited exception to the priority rule for one of the legs. The purpose behind the proposed split-price priority exception is the same – to facilitate the execution of large orders, which by virtue of their size and the need to execute them at multiple prices operate in the same manner as the complex order exception by allowing a member affecting a trade that betters the market to have priority on the balance of that trade at the next pricing increment even if there are orders in the book at the same price.

To address potential concerns regarding Section 11(a) of the Act,<sup>8</sup> the Amex proposes to adopt new subparagraph (d) to Rules 950(d), Commentary .05 and 950—ANTE(d), Commentary .06. Section 11(a) generally prohibits members of national securities exchanges from effecting transactions for the member’s own account, absent an exemption. With respect to the proposal, there could be situations where because of the limited exception to customer priority, orders on behalf of members could trade ahead of orders of nonmembers in violation of Section 11(a). The proposed rule text makes clear that FBs may avail themselves of the split-price priority rule, but that they will be obligated to ensure compliance with Section 11(a). In this regard, a FB that bids (offers) on behalf of a non-market-maker Amex member broker-dealer (“Amex member BD”) must ensure that the Amex member BD qualifies for an exemption from Section 11(a)(1) of the Act or that the transaction satisfies the requirements of Rule 11a2-2(T) under the Act. Otherwise, the FB must yield priority to orders for the accounts of non-members.

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<sup>8</sup> 15 U.S.C. 78k(a).

The Exchange further proposes to amend Amex Rule 905(d), Commentary .05(b) and Amex Rule 905—ANTE(d), Commentary .06(b) to remove the parenthetical “(or a reasonably larger number)”.<sup>9</sup>

## 2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is consistent with Section 6(b)<sup>10</sup> of the Act in general and furthers the objectives of Section 6(b)(5)<sup>11</sup> in particular in that it is designed to perfect the mechanisms of a free and open market and the national market system, protect investors and the public interest and promote just and equitable principles of trade.

### B. Self-Regulatory Organization's Statement on Burden on Competition

The proposed rule change, as amended, will impose no burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

No written comments were solicited or received by the Exchange on this proposal.

## III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

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<sup>9</sup> See Amendment No. 1. The Exchange believes this language to be unnecessary to achieve the intent of the rule, which is to allow FBs to have priority for up to an equivalent number of contracts purchased or sold at the preceding price, as specified in the rule. Telephone conference on March 8, 2005, between Laura Clare, Assistant General Counsel, Amex and Ira Brandriss, Assistant Director, Division of Market Regulation, Commission.

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

<sup>11</sup> 15 U.S.C. 78(f)(b)(5).

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>);  
or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-Amex-2004-109 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-Amex-2004-109. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the Amex. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-Amex-2004-109 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change.

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>12</sup> In particular, the Commission believes that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>13</sup> which requires, among other things, that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade and, in general, to protect investors and the public interest. The Commission believes that the proposed rule change should encourage more aggressive quoting by market makers in competition for large-sized orders, and, in turn, lead to better-priced executions. The Commission notes that the proposed rule change includes interpretive language that clarifies that floor brokers who avail themselves of the split priority rule are obligated to ensure compliance with Section 11(a) of the Act.

The Amex has requested that the Commission approve the proposed rule change prior to the thirtieth day after publication of notice thereof in the Federal Register. The Commission notes that granting accelerated approval of the proposal will allow the Amex to immediately implement a rule that is similar to rules already in place at other exchanges.<sup>14</sup> Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>15</sup> for approving the

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<sup>12</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> See Securities Exchange Act Release Nos. 51148 (February 8, 2005), 70 FR 7783 (February 15, 2005) (SR-CBOE-2004-67) and 51318 (March 4, 2005) (SR-PCX-2005-25).

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

proposed rule change prior to the thirtieth day after the date of publication of notice thereof in the Federal Register.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>16</sup> that the proposed rule change (SR-Amex-2004-109), as amended, is hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>17</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>16</sup> 15 U.S.C. 78s(b)(2).

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