

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55008; File No. SR-Amex-2006-98)

December 22, 2006

Self-Regulatory Organizations; American Stock Exchange LLC; Order Approving Proposed Rule Change Relating to the Codification of Exchange Policy Regarding Specialist Commissions

I. Introduction

On October 4, 2006, 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”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend Amex Rule 154 to codify policies regarding specialist commissions. The proposed rule change was published for comment in the Federal Register on October 25, 2006.³ The Commission received two comment letters regarding the proposal.⁴ On November 28, 2006, the Exchange submitted a response to the comments.⁵ On December 5, 2006, one of the initial commenters

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 54618 (October 18, 2006), 71 FR 62492.

⁴ See letter from Jonathan Q. Frey, Managing Partner, J. Streicher & Co. L.L.C., to Nancy M. Morris, Secretary, Commission, dated November 13, 2006 (“Streicher Letter I”), and web comment from William Silver, Managing Partner, Weiskopf, Silver Co, dated November 6, 2006 (“Weiskopf Letter”).

⁵ See letter from Neal L. Wolkoff, Chairman & Chief Executive Officer, Amex, to Nancy M. Morris, Secretary, Commission, dated November 28, 2006 (“Amex Response”).

submitted a response to the Amex Response.⁶ This order approves the proposed rule change.

II. Description

The Exchange proposes to codify in new subparagraph (b) to Amex Rule 154 its policies regarding situations where specialists may charge a commission for trades that are executed in whole or in part. Specifically, proposed Amex Rule 154(b) would prohibit a specialist from: (i) charging a commission on an off-floor order in equities that is electronically delivered to the specialist unless the order requires special handling by the specialist or the specialist provides a service, and (ii) billing for electronically delivered orders in equities that are executed automatically by the Exchange's order processing facilities upon receipt. In addition, proposed Amex Rule 154(b) would reference Amex Rule 152(c), which prohibits specialists from charging a commission where they act as principal in the execution of an order entrusted to them as agent. Lastly, proposed Amex Rule 154(b) sets forth the types of orders specialists would be allowed to bill a commission. In particular, these orders would include limit orders that remain on the book for more than two minutes, market on close or limit on close orders, tick sensitive orders, orders for non-regular way settlement, stop or stop limit orders, orders stopped at one price and executed at a better price, fill-or-kill, and immediate-or-cancel orders, and orders for the account of a competing market maker.

⁶ See letter from Jonathan Q. Frey, Managing Partner, J. Streicher & Co. L.L.C., to Nancy M. Morris, Secretary, Commission, dated December 5, 2006 ("Streicher Letter II").

III. Summary of Comments

The Commission received three comment letters regarding the proposed rule change from two specialists. Two of these comment letters, submitted by Streicher, opposed the proposed rule change for the three reasons discussed below.⁷ The third comment letter, submitted by Weiskopf, supported the proposed rule change, because “the specialist’s commission charges, if not competitive, have the potential to drive business away from the exchange and eliminate an important competitor from the market place.”⁸ Weiskopf also stated its view that the proposed rule change is “a very constructive step towards fostering greater competition in The National Market System.”⁹

Streicher argued that the proposed rule change would “adversely impact investors by reducing the qualify [sic] of markets offered by the Amex.” In particular, Streicher argued that Amex’s proposed elimination of certain specialist commissions would harm investors by putting pressure on specialists to increase spreads to offset the lost commissions. Streicher stated that “[w]hile an increase in spreads may not be practical in highly competitive markets, many of the securities listed on the Amex are thinly traded with most of their trading volume taking place primarily on the Amex.” According to Streicher, “there is often little effective competition from other markets” for these securities, and, thus, the resulting increased spreads will “have an adverse impact investors....”¹⁰

⁷ See Streicher Letter I and Streicher Letter II.

⁸ See Weiskopf Letter.

⁹ Id.

¹⁰ Streicher Letter I at 2-3.

In its response, the Exchange stated that the purpose of the proposed rule change “is to attract and maintain order flow to Amex specialists by providing transparency, clarity and consistency to the costs of doing business on the Exchange.” The Exchange argued that Streicher’s position that the elimination of certain specialist commissions would lead to specialists seeking higher spreads is flawed, because “it is against each specialist’s own economic interest to widen its spreads and thereby risk losing order flow.” Furthermore, the Exchange disagreed with Streicher’s assertion that “there is often little effective competition from other markets” and noted that “[a]ll Amex listed securities trade in at least one additional market center” and that “[t]he large majority of Amex issues trade on multiple venues.” The Exchange concluded that “[w]idening of the spreads in these securities will likely result in further market share erosion as order flow providers mindful of their best execution responsibilities direct their orders elsewhere.”¹¹

Streicher responded by taking issue with Exchange’s assertion regarding competition from other markets, by stating that many of the other markets for Amex-listed securities “frequently offer little more than a means to internalize order flow using the quote established by the Amex as the dominant marketplace for the security in question.” Streicher also disagreed with Exchange’s statement that “it is against each specialist’s own economic interest to widen its spreads and thereby risk losing order flow,” by stating that there might be circumstances in which “a greater return on fewer orders might very well make sense and be in [the commenter’s] best economic interest.”¹²

Second, Streicher noted that Amex’s purpose for this proposal is to strengthen Amex’s competitive position. However, Streicher asserted that Amex’s concerns

¹¹ Amex Response at 3-4.

¹² Streicher Letter II at 3.

regarding its competitive position would be better addressed by current Amex Rules 26 and 27.¹³ The Exchange, however, disagreed with Streicher, arguing that, while Amex Rules 26 and 27 are “useful to the Exchange in its efforts to be competitive,” the two rules do not create the “transparency and clarity” that the current proposal would provide.¹⁴

Third, Streicher expressed concerns that the rule change would “result in significant implementation costs” that are “difficult to justify” given the proposed rule change’s temporary nature.¹⁵ The Exchange, however, disputed Streicher’s argument, indicating that the implementation costs would be minimal since “most if not all specialist units” have already complied with the proposed limitations on specialist commissions.¹⁶ The Exchange also noted that it does not intend for the proposed rule to remain in effect for a short period; rather, the Exchange intends to expand the rule to apply to equities and ETFs traded on the Exchange’s Auction and Electronic Market Integration Platform (“AEMI”) system.¹⁷ In response, Streicher suggested that implementation costs would be saved if the Exchange defers this proposed rule change

¹³ Streicher Letter I at 3. Amex Rules 26 and 27 provide the Exchange with the ability to: (1) limit or prohibit the awarding of new allocations to specialists who fail to respond to competition by offering competitive markets and competitively priced services, and (2) remove allocations from specialists who fail to meet certain levels of performance in handling of those securities.

¹⁴ Amex Response at 4.

¹⁵ Streicher Letter I at 3.

¹⁶ Amex Response at 4.

¹⁷ Id.

and has one proposed rule change when the Exchange “is ready to finalize and allowable commission schedule under AEMI.”¹⁸

IV. Discussion

The Commission has carefully reviewed the proposed rule change, the comment letters received, and Amex's response, and the Commission finds that the proposed rule change is consistent with the requirements of Section 6 of the Act¹⁹ and the rules and regulations thereunder applicable to a national securities exchange.²⁰ In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,²¹ because it is designed to promote just and equitable principles of trade, 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 also believes that the proposed rule change is consistent with Section 11(A)(a)(1)(C) of the Act²² which states that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure,

¹⁸ Streicher Letter II at 3.

¹⁹ 15 U.S.C. 78f.

²⁰ 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). The Commission notes that it previously approved a similar proposed rule change relating to commissions on options orders, filed by the Chicago Board Options Exchange, Inc. See Securities Exchange Act Release No. 51235 (February 22, 2005), 70 FR 9687 (February 28, 2005) (Approval of CBOE Rule 8.85(b)(iv)). In addition, the New York Stock Exchange, Inc. (“NYSE”) recently adopted a rule prohibiting specialists from charging commissions on orders in their speciality securities. See Securities Exchange Act Release No. 54850 (November 30, 2006), 71 FR 71217 (December 8, 2006) (Notice of Filing and Immediate Effectiveness of Amendments to NYSE Rule 123B and Adoption of NYSE Rule 104B).

²¹ 15 U.S.C. 78f(b)(5).

²² 15 U.S.C. 78k-1(a)(1)(C).

among other things, economically efficient execution of securities transactions, and fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets.

The Commission notes that the Exchange’s proposed rule change codifies the Exchange’s policy regarding specialist commissions by specifying the particular types of orders in which a specialist may charge a commission and the types of orders in which a specialist may not charge a commission. The Commission notes that the Streicher Letters’ concern expressed about the possibility of specialists attempting to widen spreads to compensate for lost commissions. In this regard, the Commission believes that competition for order flow among competing markets should continue to provide an incentive for specialists not to widen spreads.

In addition, the Commission finds that the proposal is consistent with Section 6(e)(1) of the Act,²³ because it is not designed to permit unfair discrimination between customers, issuers, brokers and dealers, or to impose any schedule or fix rates of commissions, allowances, discounts, or other fees to be charged by its members. Section 6(e) of the Act²⁴ was adopted by Congress in 1975 to statutorily prohibit the fixed minimum commission rate system. As noted on a report of the House of Representatives one of the purposes of the legislation was to “reverse the industry practice of charging fixed rates of commission for transaction on the securities exchanges.”²⁵ The fixed minimum commission rate system allowed exchanges to set minimum commission rates that their members had to charge their customers, but allowed members to charge more.

²³ 15 U.S.C. 78f(e)(1).

²⁴ 15 U.S.C. 78f(e).

²⁵ H.R. Rep. No. 94-123, 94th Cong., 1st Sess. 42 (1975).

Amex's proposal, by contrast, does not establish a minimum commission rate, but instead prohibits the Exchange's specialists from charging a commission for handling an order in equities that is executed on an opening or reopening or an order in equities (or portion thereof) that is executed against the specialist as principal, or for the execution of an off-floor equities order delivered to the specialist through the Exchange's electronic order routing systems, subject to certain exceptions. Accordingly, the Commission does not believe that the Amex's proposal constitutes fixing commissions, allowances, discounts, or other fees for purposes of Section 6(e)(1) of the Act.²⁶ The Commission also notes that Amex's limits on fees that specialists may charge applies only to members who choose to be specialists on Amex. By limiting fees, the Amex is merely imposing a condition, which is consistent with the Act, on a member's appointment as a specialist.

V. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with Sections 6(b)(5) and 6(e)(1) of the Act.²⁷

²⁶ 15 U.S.C. 78f(e)(1).

²⁷ 15 U.S.C. 78f(b)(5) and 78f(e)(1).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²⁸ that the proposed rule change (SR-Amex-2006-98) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁹

Florence E. Harmon
Deputy Secretary

²⁸ 15 U.S.C. 78s(b)(2).

²⁹ 17 CFR 200.30-3(a)(12).