

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-55640; File No. SR-Amex-2007-04)

April 17, 2007

Self-Regulatory Organizations; American Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Its Buy-In Rules

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> notice is hereby given that on January 8, 2007, the American Stock Exchange LLC (“Amex”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II, and III below, which items have been prepared primarily by Amex. Amex filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>2</sup> and Rule 19b-4(f)(6) thereunder<sup>3</sup> so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The purpose of the proposed rule change is to amend Amex Rules 759, 783, 784, and 789 and to adopt new Rule 798 to standardize Amex’s buy-in rules.

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

In its filing with the Commission, Amex included statements concerning the purpose of and basis for the proposed rule change 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 IV

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

<sup>2</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>3</sup> 17 CFR 240.19b-4(f)(6).

below. Amex has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.<sup>4</sup>

(A) Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

Amex is amending its Rules 783, 784, and 789 and is adopting new Rule 798 to permit buyer executed buy-ins,<sup>5</sup> to reduce the waiting period to execute a buy-in from twenty-one (21) days to three (3) days, and to otherwise provide more standardized and consistent industry buy-in rules and procedures. Amex is also making conforming changes to Rules 759, 784, and 789. This proposal seeks to substantially mirror the recent New York Stock Exchange (“NYSE”) amendments to its buy-in rules approved by the Commission, which were made mainly for the purpose of achieving industry uniformity.<sup>6</sup>

Introduction

The Amex buy-in rules apply to transactions that are not subject to the rules of a qualified clearing agency, such as The Depository Trust Company (“DTC”)<sup>7</sup> and the National Securities Clearing Corporation (“NSCC”)<sup>8</sup>, including transactions processed in NSCC’s Continuous Net

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<sup>4</sup> The Commission has modified the text of the summaries prepared by Amex.

<sup>5</sup> A “buy-in” is a transaction between broker-dealers where because the securities are not delivered on time by the broker-dealer on the sell-side, the broker-dealer on the buy-side purchases the securities from another source.

<sup>6</sup> Securities Exchange Act Release No. 52842 (November 28, 2005), 70 FR 72321 (December 2, 2005) [File No. SR-NYSE-2005-50].

<sup>7</sup> DTC is a member of the U.S. Federal Reserve System, a limited-purpose trust company under New York State banking law, and a clearing agency registered with the Commission.

<sup>8</sup> NSCC is a central counterparty that provides centralized clearance, settlement, and information services for virtually all broker-to-broker equity, corporate bond and municipal bond, exchange-traded funds, and unit investment trust trades in the U.S. NSCC provides clearing and settlement, risk management, central counterparty services,

Settlement service (“CNS”)<sup>9</sup> that settle through them.<sup>10</sup> In the event that a buy-in is sent to the Amex floor for execution, then Amex buy-in rules apply.

However, under current Amex rules that place the responsibility for the actual execution of the buy-in on the defaulting member or member organization (“defaulting member” or “seller”), there are disincentives for the defaulting member to execute the buy-in. For example, the defaulting member could potentially manipulate the extent to which it has market exposure by timing its purchase of the necessary securities to benefit itself. Therefore, an initiating member or member organization (“initiating member” or “buyer”) may receive negative customer reaction if the customer learns that its trade has not been settled and that their securities are not available because a buy-in has not been executed or executed in a timely manner by the defaulting member.

Other self-regulatory organizations (“SROs”) have recognized this conflict of interests, and their buy-in rules assign responsibility accordingly by allowing the buyer to execute the buy-in. By allowing buyers to execute their own buy-ins, the defaulting members’ conflicts of interest are avoided, and the process is expedited.

The Securities Industry Association (“SIA”) Securities Operations Division Buy-In Committee (“Committee”)<sup>11</sup> has expressed a strong preference that Amex consider amending its

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and a guarantee of completion for trades. NSCC also nets trades and payments among its members thereby reducing the volume of securities and payments that need to be exchanged each day.

<sup>9</sup> CNS is an automated accounting system that centralizes and nets the settlement of compared security transactions in order to maintain an orderly flow of security and money balances.

<sup>10</sup> See Securities Exchange Act Release No. 53528 (March 21, 2006), 71 FR 15506 (March 28, 2006) [File No. SR-NSCC-2005-15] (approving NSCC’s CNS buy-in rules).

buy-in rules to eliminate is buy-in notice procedures and to change who executes the buy-in to the buyer from the seller. The purpose of the Committee's recommendation is to identify and to standardize various buy-in rules and procedures regarding the buy-in process related to non-CNS transactions and to help formulate uniformity among industry rules. The Committee requested that Amex conform its rules to those of the other exchanges that allow the initiating member to execute buy-ins to close out a contract.

#### Current Requirements

Amex Rule 784 sets forth the "mandatory closing of fails" process by which a buyer is required to close-out a contract that has not been completed by the seller for a period of twenty-one (21) business days. A mandatory closing of fails requires that a notice of intention be delivered in quadruplicate and on the twenty-first (21<sup>st</sup>) business day after the original due date of the contract by the initiating member to the seller. The member organization receiving the notice of intention must indicate its position with respect to the resolution of the failed trade (e.g., doesn't know the trade, knows the trade but cannot deliver, will deliver) and return the notice of intention to the initiating member no later than three business days after the notice was sent. If the notice of intention is not returned when due or is returned with the indication that the contract is not known, the initiating member shall itself close the contract by buying or selling the securities involved through its own floor representative. If the notice of intention is returned when due with an indication that the contract is known but that delivery cannot be made and if the contract is one which has been designated as acceptable for clearance as a fail item by a registered clearing agency of which both parties are clearing members, it shall be submitted for clearance by the defaulting member. If the notice of intention is returned when due with an

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<sup>11</sup> The Committee is made up of representatives from a broad cross-section of broker-dealers and industry groups.

indication that the contract is known but that delivery cannot be made and the contract is one which has not been designated as acceptable for clearance as a fail item by a registered clearing agency of which both parties are clearing members, the initiating member shall close the contract according to the procedures in Amex Rule 783. Therefore, the rule currently provides that more than three weeks may lapse before the contract is closed.

Amex Rule 783 sets forth a permissive procedure by which an initiating member may close-out a contract that has not been executed by the defaulting member. The initiating member must provide notice of its intention to make a closing. Pursuant to Amex Rule 783, Amex determines the times for the delivery of such notices of intention to close and orders to close and the time for the closing of contracts. If the times within which securities may be delivered are extended or shortened, the time limits established by Amex may be similarly extended or shortened.<sup>12</sup> Once the initiating member sends the notice to the defaulting member, the defaulting member shall be given a copy of the order to close for execution on that day. If the order is not executed, the defaulting member shall return the original order within fifteen minutes of the close of trading indicating why it cannot be executed, and the buy-in desk will deliver a copy of the floor report to the initiating member. The initiating member may then close the contract and must notify the defaulting party with respect to any money differences that it will claim as damages. If the order is executed by the defaulting member, it shall furnish a copy of the order to close and a copy of the floor report to the buy-in desk on the floor.

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<sup>12</sup> Contracts made for cash within one and one-half hour before the close of trading are given different treatment with respect to timing. When a contract made for cash within one and one-half hour before the close of trading is to be closed on the same day, the time of the transaction shall be stated on the order and notice, which shall be delivered within thirty minutes after the time of the transaction, and the contract shall not be closed until thirty-five minutes after the time of the transaction.

Amex Rule 789 requires an initiating member to accept physical delivery of some or all of the securities that are the subject of a buy-in thereby halting the buy-in execution for those securities if the defaulting member tenders the securities prior to the buy-in. The defaulting member must promptly tender the securities, and if they are not promptly delivered, such member or member organization is liable for any resulting damages.

#### Proposal

Amex is amending Rule 784 to allow the member or member organization failing to receive the securities to execute the buy-in and to reduce the waiting period to execute a buy-in from twenty-one (21) days to three (3) days after delivery on the contract was due. The elimination of Commentary .01 through .06 to Rule 784 is intended to facilitate the amendments to the buy-in procedures. The amendments to these procedures are largely proposed in the text of Rule 784. Amex believes that once the responsibility is shifted to the buy-side of the transaction, the buy-in process will work more efficiently.

The amendments to Rule 784 provide that the initiating member may close a contract no sooner than three business days after the original due date for delivery (“Effective Date”). The initiating member must deliver a written notice to the defaulting member at least two days before the proposed buy-in. After receipt of the buy-in notice, the defaulting member must then send a signed, written response to the initiating member stating its position. If the response is not received by 5 p.m. ET on the day of receipt of the buy-in notice or it is returned with an indication that the contract is not known or that it is known but that delivery cannot be made, the buy-in may be executed on the Effective Date. The initiating member shall be required to accept any portion of the securities called for by the contract from the defaulting member that the defaulting member submits prior to the execution of the buy-in, but the initiating member shall not be required to accept any securities from the defaulting member if the buy-in has already

been executed and if the buy-in could not have been reasonably cancelled by the initiating member. Once the buy-in has been executed, the initiating member shall notify the defaulting member confirming the purchase along with a bill or payment.

Amex is also eliminating the requirements for quadruplicate paper notices and will permit electronic notices, including notices from a computerized network facility, or the electronic functionality of a Qualified Clearing Agency, such as DTC and NSCC. The amendments also change the existing time deadlines for delivering notices, securities, and executions and adopt those used by other self-regulatory organizations.

Amex is also adopting new Commentary .01 to Rule 784 to help ensure that members and member organizations comply with the requirements of Regulation SHO<sup>13</sup>. Members and member organizations are obligated to comply with the marking, locate, and delivery requirements of Regulation SHO for short sales of equity securities. As a result, members and member organizations should have policies and procedures in place to comply with these requirements, including close-out procedures.<sup>14</sup>

Amex is rescinding Rule 783 and has incorporated the permissive buy-in procedures of Rule 783 into Rule 784. Amex is also amending Rule 789 to conform it to this proposal to permit buyer executed buy-ins and to create a Rule 798 to clarify the requirements and time frames upon which a defaulting member may deliver against a buy-in notice. Finally, Amex is

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<sup>13</sup> 17 CFR 242.200 through 242.203. Securities Exchange Act Release No. 50103 (July 28, 2004), 69 FR 48008 (August 6, 2004), [File No. S7-23-03] (adoption of Regulation SHO).

<sup>14</sup> At the same time the changes noted above were being developed, the SEC implemented Regulation SHO, Regulation of Short Sales, which shares a similar purpose, the reduction of fails to deliver, with the buy-in rules. Rule 203 to Regulation SHO imposes locate and borrowing/ delivery requirements on broker-dealers that sell equity securities, including close-out requirements on certain open fail to deliver positions.

making technical amendments to Rules 759, 784 and 789 to better coordinate the rules with industry practice.

Amex believes that the revisions to its buy-in rules will help standardize Amex's procedure and practice by allowing members and member organizations to clean-up fails and efficiently deliver Amex-listed securities. Amex believes that the proposed rule change is consistent with Section 6 of the Act in general and furthers the objectives of Section 6(b)(5) in particular in that it 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 transactions in securities, to remove impediments to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. By amending the Amex buy-in rules to permit buyers to execute buy-ins, firms are expected to find it easier to execute buy-ins of Amex-listed securities. In addition, the amendments seek to remove inefficient requirements and amend time deadlines to conform to current industry practice.

(B) Self-Regulatory Organization's Statement on Burden on Competition

Amex does not believe that the proposed rule change will impose any burden on competition.

(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 with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change (1) does not significantly affect the protection of investors or the public interest, (2) does not impose any significant burden on



competition, and (3) does not become operative for 30 days from the date of filing or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>15</sup> and Rule 19b-4(f)(6) thereunder.<sup>16</sup> As required by Rule 19b-4(f)(6)(iii), Amex provided the Commission with written notice of its intent to file the proposed rule change at least five business days prior to filing the proposal with the Commission or within such shorter period as designated by the Commission.

At any time within sixty (60) days of the filing of the proposed rule change, the Commission could have summarily abrogated such rule change if it appeared to the Commission that such action was necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### IV. Solicitation of Comments

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

##### 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-2007-04 on the subject line.

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<sup>15</sup> 17 U.S.C. Section 78s(b)(3)(A)(iii).

<sup>16</sup> 17 CFR 240.19b-4(f)(6).

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-Amex-2007-04. 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, 100 F Street, NE, Washington, DC 20549. The text of the proposed rule change is available at Amex, the Commission's Public Reference Room, and [http://www.amex.com/atamex/ruleFilings/at\\_rulefilings.html](http://www.amex.com/atamex/ruleFilings/at_rulefilings.html). 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-2007-04 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

Florence E. Harmon  
Deputy Secretary

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