

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49747; File No. SR-Amex-2003-89

May 20, 2004

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Amendments No. 1, 2, 3, 4, 5, and 6 Thereto and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 7 to the Proposed Rule Change by the American Stock Exchange LLC to Implement a New Options Trading Platform Known as the Amex New Trading Environment or ANTE

I. Introduction

On October 7, 2003, 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 adopt new rules for the implementation of its new options trading platform known as the Amex New Trading Environment or ANTE. On November 17, 2003, December 17, 2003, February 9, 2004, March 2, 2004, March 18, 2004, and March 24, 2004, the Exchange submitted Amendments No. 1, 2, 3, 4, 5, and 6 to the proposed rule change.³ The proposed rule change and Amendments No. 1, 2, 3, 4, 5, and 6 were published for comment in the Federal Register on March 31, 2004.⁴ The Commission received no comment letters with respect to the proposal, as

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See letters from Claire P. McGrath, Senior Vice President and Deputy General Counsel, Amex, to Nancy Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated November 14, 2003 ("Amendment No. 1"); December 16, 2003 ("Amendment No. 2"); February 5, 2004 ("Amendment No. 3"); March 1, 2004 ("Amendment No. 4"); March 17, 2004 ("Amendment No. 5"); and March 23, 2004, replacing Form 19b-4 in its entirety ("Amendment No. 6").

⁴ See Securities Exchange Act Release No. 49465 (March 24, 2004), 69 FR 16990 ("Notice").

amended. On April 19, 2004, the Amex filed Amendment No. 7 to the proposed rule change.⁵ This order approves the proposed rule change and Amendments No. 1, 2, 3, 4, 5 and 6; grants accelerated approval to Amendment No. 7 to the proposed rule change; and solicits comments from interested persons on Amendment No. 7.

II. Description of the Proposal

The Exchange proposes to implement a new trading environment (referred to hereinafter as “ANTE” or the “ANTE System”) to replace many of its existing floor trading systems. Initially, ANTE would be used for the trading of standardized options on the Exchange, but would be expanded to include all of the Exchange’s current and future product lines—Exchange-Traded Funds, equities and single stock futures.⁶ The ANTE System would replace many of the Exchange’s current systems, including the automated quotation calculation system and specialist “book” functions such as limit order display, automatic order execution, and allocation of trades. Each floor participant would have electronic access to the ANTE System.⁷

A. ANTE Central Book and ANTE Display Book

⁵ See letter from Claire P. McGrath, Senior Vice President and Deputy General Counsel, Amex, to Nancy Sanow, Assistant Director, Division, Commission, dated April 16, 2004, replacing the proposed rule text in its entirety (“Amendment No. 7”). In Amendment No. 7, the Exchange made minor clarifying changes to the text of proposed Amex Rule 951-ANTE, Commentary .01.

⁶ The Exchange seeks the approval of new rules and the amendment of current rules to implement ANTE in options only. Additional filings would be submitted to the Commission when the Exchange seeks to expand ANTE to other product lines.

⁷ Floor brokers would access the ANTE system through the Booth Automated Routing System (“BARS”); specialists would access the ANTE System through the Central and Display Books, described below, which would provide the functions of the existing quote calculation system (known as “XTOPS”) and the Amex Options Display Book (“AODB”) in one integrated system; and registered options traders would access the ANTE System through handheld devices.

The functions currently available in the AODB would be split between the ANTE Central Book and the ANTE Display Book. The Central Book would contain what was formerly known as the “specialist’s limit order book” and would provide for the matching and execution of eligible orders similar to the current Auto Match and Auto-Ex Systems. The Display Book would be similar to the “Acknowledgement Box” currently found in the AODB and would contain orders awaiting manual handling.⁸ Market and marketable limit orders routed to the Exchange would be sent to either the Central Book or the Display Book depending on whether the size of the order is within the size eligible for automatic matching in the Central Book (referred to as the “auto-match size”). As discussed in greater detail below, the Options Trading Committee would establish the auto-match size for each option class.⁹

B. Quote Calculation and Dissemination

Specialists and registered options traders would be able to calculate quotations using either their own proprietary automatic quotation systems or an Exchange-provided automatic quotation system. Both specialists and registered options traders would have the ability to stream quotations for each option series they trade. While specialists would continue to be required to disseminate quotations in all series of the option classes they trade, registered options

⁸ Registered options traders would be able to view both the Display Book and the Central Book on their hand-held devices, giving them a complete view of the limit order book and all pending orders in each option series they trade.

⁹ Under the ANTE System, an order greater than the established auto-match size would be routed to the Display Book for an immediate execution by the specialist, at the disseminated price, up to the disseminated size. Market and marketable limit orders less than or equal to the disseminated size and less than or equal to the auto-match size would be sent to the Central Book for automatic matching and execution against the disseminated quote and allocation to the appropriate party. Orders less than or equal to the disseminated size and greater than the auto-match size would be routed to the Display Book. Orders greater than the disseminated size and less than or equal to the auto-match size would be routed to the Central Book for a partial execution up to the disseminated size.

traders would be able to choose whether to stream quotes with size in all or select series of the option classes they trade or join the specialist's quote.

The ANTE System would collect all of the quotes submitted by the specialist and each registered options trader, and would determine the best bid and best offer for dissemination as the Amex Best Bid and Offer ("ABBO").¹⁰ The Exchange's market data system would continue to submit only one quote per series to the Options Price Reporting Authority. Each quote entered would have a specific participant identifier to allow the ANTE System to allocate directly contracts executed at the best bid or best offer to those participants quoting at the ABBO at the time the execution occurs. Furthermore, the ANTE System would allocate to each registered options trader only the amount of executed contracts indicated in their quote size.

C. Trading Outside the ANTE System

The Exchange would continue to maintain its floor-based auction market so that orders of size, complex orders, solicited orders, facilitation orders and other types of orders as determined by the order flow providers could potentially receive price improvement and be exposed to the auction market environment. Orders not eligible for execution through the ANTE System and orders represented by a floor broker at the specialist's post would trade in the same manner and pursuant to the same rules as they do today. Crowd trades or trades that occur outside the ANTE System would be allocated to registered options traders in the same manner as such trades are allocated today.¹¹ Paragraph (l) of Amex Rule 950—ANTE, Commentary .03 would be revised

¹⁰ The ANTE System would never allow a locked or crossed market to occur in the ABBO. Proposed Amex Rule 933-ANTE, (f)(i)(E) provides that orders otherwise eligible for automatic matching and execution may not receive automatic matching during certain market activities, including whenever the ABBO crosses or locks the National best bid or offer ("NBBO") and causes an inversion in the quote, except as provided in Amex Rule 941-ANTE (e) for orders sent through the Options Intermarket Linkage.

¹¹ See Amex Rule 950—ANTE (l), Commentary .03.

to reflect that it remains the specialist's obligation to allocate executed contracts when an execution has occurred outside the ANTE System.¹²

D. Rollout of the ANTE System

The Exchange currently anticipates to begin its rollout of the ANTE System on or about May 24, 2004 and to complete the rollout by the end of the third quarter of 2005.¹³ The Exchange plans to roll out the ANTE System on a specialist's post-by-specialist's post basis. Assuming the ANTE System performs well at the three initial specialist posts, by the end of June 2004, option classes on additional specialist's posts would begin to be rolled-out, and by the end of July 2004, it is anticipated that three additional specialists' posts and another 200 classes would be rolled-out. The Exchange expects that by the end of the January 2005, the 300 most actively traded option classes would be trading on the ANTE System. Additional specific plans for the roll out are being developed by the Exchange with the intention to have all equity and index option classes trading on the ANTE System by the second quarter of 2005. Once rolled out, the new system would be used for all option classes traded on the Exchange.¹⁴

¹² Specialists would be obligated to use best efforts to attempt to ensure that the registered options trader responsible for announcing the best bid or offer during a crowd trade be appropriately allocated executed contracts in accordance with the participation provisions found in Amex Rule 950—ANTE (d), Commentary .07.

¹³ The Exchange has changed its implementation dates and the time frame for the roll out of the ANTE System initially proposed in the Notice from March 1, 2004 to May 24, 2004. Telephone conversation between Claire P. McGrath, Senior Vice President and Deputy General Counsel, Amex, and Jennifer Colihan, Special Counsel, Division, Commission, on May 20, 2004.

¹⁴ During the roll-out period, while the Exchange has option classes trading on both systems, current rules (as they are amended from time to time) would apply to those option classes continuing to trade on its current system, while the ANTE rules (as they are amended from time to time) would apply to those option classes trading on the new trading system. Once the roll-out of ANTE is complete, the amendments to the Exchange's options rules reflecting the implementation of ANTE would replace, where applicable, the corresponding provisions in Amex Rules 900 through 958A. Once the roll-out period has ended and all option classes are trading on the ANTE System, the

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 7, including whether Amendment No. 7 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. Please include File Number SR-Amex-2003-89 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-2003-89. 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

Exchange would submit a filing pursuant to Rule 19b-4 under the Act, which would delete rules that would not be applicable to the Exchange's then current trading environment.

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-2003-89 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Discussion

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the Act and the rules and regulations promulgated thereunder applicable to a national securities exchange and, in particular, with the requirements of Section 6(b) of the Act.¹⁵ Specifically, the Commission finds that approval of the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act¹⁶ in that it is designed to facilitate transactions in securities; 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 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.

A. Quoting Function for ANTE Participants and Firm Quotations

Under the proposal, specialists and registered options traders would be able to calculate quotations using either their own proprietary automatic quotation systems or an Exchange

¹⁵ 15 U.S.C. 78f(b). 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).

¹⁶ 15 U.S.C. 78f(b)(5).

provided automatic quotation system and have the ability to stream quotations for each option series in which they trade. While specialists would be required to disseminate quotations in all series of the option classes they trade, registered options traders would be able to either stream their own quotes or join the specialist's disseminated quotation in some or all of his assigned classes or series. If registered options traders join the specialist's quote, they would have the ability to manually improve a quote on a series by series basis. The Commission believes that allowing registered options traders to automatically generate their own quotes across all series in a class should enhance intramarket competition on the Exchange.

Furthermore, whether entering their own quotes or joining the specialist's quote, registered options traders using the ANTE hand held devices would be required to specify the size of each quote they submit or join. As executed contracts are allocated to registered options traders at the ABBO, their quote size would decrement so that they would never be allocated more than their indicated quote size. Once the indicated quote size is depleted, the registered options trader would need to replenish the quote size before being allocated additional executed contracts. The Commission believes that this ability to indicate their size for quotes in each option series should allow registered options traders to manage their exposure to the market and compete more effectively. Registered options traders also would have to be physically present at the specialist's post on the floor of the Exchange whenever they use the ANTE System to enter quotes, join the specialist's quote, or enter an order in an option class through the ANTE System.

In addition, proposed Rule 958A-ANTE would provide: (i) that the registered options traders inputting their own quotes, either manually on a series by series basis or through the use of an Exchange-provided or proprietary automated quote calculation system, would be considered the responsible broker or dealer for the purposes of the rule; and (ii) while the responsible broker or dealer would continue to be required to quote a minimum of ten contracts,

customer limit orders representing the best bid or offer may be disseminated at less than ten contracts. The Commission believes that the proposed provisions are consistent with the obligations imposed upon responsible brokers or dealers under the requirements of the Commission's Quote Rule.¹⁷

As noted above, the ANTE System would never allow a locked or crossed market to occur at the ABBO. The Exchange proposes under Amex Rule 951-ANTE, Commentary .01 that if a quote is submitted that would lock or cross the ABBO, the ANTE System would either: (i) revise the bid or the offer by the minimum price variant(s) so that the ABBO is not locked or crossed; or (ii) if the ABBO represents an off-floor limit order, the ANTE System would execute the order and allocate the trade pursuant to the post trade allocation process.¹⁸ The Commission believes that providing for the execution of off-floor limit orders against a quote that would lock or cross the ABBO should contribute to a fair and orderly market because such orders would receive executions as soon as there is interest available at the limit order price or better.

B. Obligations of Registered Options Traders

Under proposed Amex Rule 958-ANTE, the Exchange would review registered options traders' written applications to trade option classes on the ANTE System and assign classes to each registered options traders based upon the following factors: (i) the preference of applicants; (ii) assuring that financial resources available to a registered options trader enable him to satisfy the obligations set forth in Amex Rule 958—ANTE with respect to each class of option contracts to which he is assigned; (iii) the applicant's expertise in option trading; (iv) the applicant's prior

¹⁷ Rule 11Ac1-1 under the Act, 17 CFR 240.11Ac1-1 ("Quote Rule").

¹⁸ If the Ante System revises the quote as discussed in (i), a notification would be sent to the ANTE Participant (specialist or registered options trader) submitting the quote.

market performance; and (v) the impact of the number of registered options traders assigned in an option class or classes on the Exchange's quotation system capacity.¹⁹

Although the Exchange could suspend or terminate any assignment of a registered options trader under this Rule and make additional assignments, the Exchange has clarified and the Commission notes that, pursuant to Article II, Section 3 of the Amex Constitution, registered options traders would have the right to appeal any Exchange determination made in accordance with this Rule.²⁰

In addition to the trading activity requirements in their assigned classes, registered options traders would have an electronic quoting requirement. Any registered options trader who transacts electronically more than 20% of its contract volume in an assigned option class and not through open outcry measured over a calendar quarter would be obligated to maintain continuous two-sided quotations for at least ten contracts in a percentage of series in that option class commencing the next calendar quarter as specified in the rules.

Registered options traders whose electronically transacted contract volume is less than 20% in a given option class would not have an electronic quoting obligation in any specific number of series in that option class. Moreover, for the first 90 days after an option class begins

¹⁹ In addition, with respect to the factor relating to the potential impact on the Exchange's quotation system capacity, the Commission notes that Amex represents that to the extent that the Exchange places limitations on registered options traders' assignments based on concerns about capacity restraints, such limits must be objectively determined and submitted as a proposed rule change to the Commission for approval pursuant to Section 19(b) of the Act. 15 U.S.C. 78s(b). See letter from Claire McGrath, Senior Vice President and Deputy General Counsel, Amex, to Kelly Riley, Division, Commission, dated May 20, 2004.

²⁰ During the first six months that an option class is on the ANTE System, a registered options trader applying for an assignment in that option class should be guaranteed an assignment in such class, provided for at least the immediately preceding calendar year the registered options trader: (i) has been a member of the Exchange; (ii) has maintained a continuous presence as a registered options trader in such option class; and (iii) has met the requirements of Amex Rule 958—ANTE.

trading on the ANTE System, registered options traders would not have to comply with the electronic quoting requirement set forth in Amex Rule 958-ANTE (h)(iii)(A).

In summary, registered options traders would, pursuant to Amex Rule 958—ANTE, be obligated to: (i) apply for an assignment of options classes to trade on the ANTE System; (ii) continue to have 50% of their trading activity each quarter in their assigned classes; (iii) make competitive bids and offers as reasonably necessary to contribute to the maintenance of a fair and orderly market; (iv) maintain a continuous two-sided market in a specified percentage of series in those classes in which the registered options trader has electronically transacted more than 20% of his contract volume; (v) disseminate a size of at least 10 contracts with each quote; and (vi) be physically present at the specialist's post on the floor of the Exchange where the option class is traded in order to quote (either by joining the specialist's quote or streaming his own quotes) or submit orders in that option class.

Because registered options traders receive certain benefits for carrying out their duties, the Commission believes that they should have an affirmative obligation to hold themselves out as willing to buy and sell options for their own account on a regular or continuous basis to justify this favorable treatment. In this regard, the Commission believes that Amex's proposed Rule 958-ANTE would impose such affirmative obligations on ANTE registered options traders.

C. Limit Order Display Feature

The Exchange proposes to develop on a one-year pilot program basis a quote assist feature in ANTE to help the specialist display limit orders immediately upon receipt. The ANTE System would automatically display eligible limit orders within a configurable time that could be set on a class-by-class basis. In proposed Amex Rule 950(g)—ANTE, Commentary .01, Amex proposes to require a specialist to maintain and keep active the ANTE limit order quote assist feature. The Exchange would establish the time frame within which the quote assist feature

would display eligible customer limit orders. The specialist could deactivate the quote assist feature provided Floor Official approval is obtained. Such approval would be required to be obtained no later than three minutes after deactivation. If the specialist does not receive approval within three minutes after deactivation, the Exchange would review the matter as a regulatory issue.²¹ The Exchange commits to documenting all instances where a Floor Official has granted approval. Moreover, the Exchange commits to conducting surveillance designed to detect whether specialists as a matter of course rely on the ANTE quote-assist feature to display all eligible limit orders.

The Commission believes that the quote assist feature should help to ensure that eligible customer limit orders are displayed within the required time period then in effect. The Commission notes that the specialist could be violating his due diligence obligation if he excessively relies on the quote assist feature to display eligible limit orders without attempting to address the orders immediately. Accordingly, during this pilot program, the Commission expects the Exchange to document all instances where a Floor Official has granted approval and to conduct surveillance designed to detect whether specialists as a matter of course rely on the ANTE quote-assist feature to display all eligible limit orders.

Since, according to the Exchange, the ANTE System initially would not be able to produce data that would identify for surveillance purposes when the specialist has relied upon the quote assist feature to display a customer limit order versus when the specialist displayed the customer limit order prior to the quote assist time frame,²² the Commission expects the Exchange

²¹ The Exchange represents that Floor Officials could grant approval only in instances when there is an unusual influx of orders or movement of the underlying that would result in gap pricing or other unusual circumstances.

²² The Exchange represents that this information would be available by the end of the second quarter of 2004.

to run its limit order display exception report to detect any impermissible reliance on the quote assist feature, and to report to the Commission every three months the statistical data it uses to make this determination. The Commission notes that the pilot program for the quote assist feature would expire on the first anniversary of Commission approval of the ANTE System.

D. Automatic Matching and Execution in the Central Book

The Exchange proposes that the ANTE Central Book provide for the automatic matching and execution of eligible market and marketable limit orders at the ABBO, provided that there is no better market at another options exchange and the order is less than the auto-match size. Orders for the accounts of public customers would be eligible for automatic matching and execution in all option classes trading on the ANTE System, provided such order sizes are within the auto-match size. However, as currently provided, the Options Trading Committee would determine on a class-by-class basis whether orders for the accounts of broker-dealers and competing market makers would be eligible for automatic matching and execution. The Options Trading Committee would also continue to determine the maximum order size eligibility for broker-dealer and competing market maker accounts.

The Exchange also proposes under Amex Rule 933-ANTE (c)(2) that non-broker-dealer customer orders would be eligible for automatic matching and execution at the current best bid or offer displayed by another options exchange (automatic price matching) and automatic price improvement pursuant to Commentary .01, while broker-dealer orders would not be so eligible. The Commission believes that excluding broker-dealer orders from the automatic price-matching feature of ANTE is consistent with the Act. Nevertheless, the Commission notes that the Linkage Plan requires Amex members to avoid trading through better prices on other markets, including when executing orders on behalf of broker-dealers.

Under the proposal, orders greater than the disseminated size and less than or equal to the auto-match size would be routed to the Central Book for a partial execution up to the disseminated size. Any contracts remaining in a partially executed order would be handled by the specialist. Orders greater than the disseminated size and greater than the auto-match size would be routed to the Display Book. Furthermore, if the ABBO is not at the NBBO and the order is not eligible for automatic price matching at the NBBO as set forth in Amex Rule 933—ANTE, Commentary .01(b), the order would be routed to the specialist for handling through the Options Intermarket Linkage.

The Commission believes that the various types of executions available through the ANTE System, whether via the Central Book or Display Book, should allow ANTE Participants to provide more efficient and immediate executions, subject to priority and allocation principles.

E. Specialist's Emergency Quote

Since at all times during the trading day a quote with size would be required to be disseminated for each option series, the Exchange proposes in Amex Rule 933-ANTE, Commentary .03 for a Specialist's Emergency Quote process in the ANTE System. The Specialist's Emergency Quote would be calculated continuously and would be disseminated whenever an execution results in the disseminated bid or offer size decrementing to zero, and would continue to be disseminated until the specialist refreshes his bid or offer with size, a registered options trader disseminates a better bid or offer, or a limit order is received that betters the Specialist's Emergency Quote. However, the Specialist's Emergency Quote would not be disseminated if there is a better bid or offer already being disseminated by a registered options

trader or represented by a limit order. Furthermore, the specialist could establish the Specialist's Emergency Quote parameters as often as the start of every trading day.²³

Since the Specialist's Emergency Quote would not represent a bid or offer created using the theoretical value calculated by the specialist's automated quote calculation system, the Exchange believes that the specialist would have an incentive to refresh his previous quote size or update his quote as quickly as possible, and expects that the Specialist's Emergency Quote would be disseminated only for short periods of time before it is replaced by the specialist or other market participants. The Commission notes that the Specialist's Emergency Quote would be consistent with the specialist's obligation under exchange rules to continuously quote.

F. Priority and Allocation

The Exchange also proposes in Amex Rule 935-ANTE the manner in which the ANTE System would allocate executed contracts to non-broker-dealer customers, broker-dealers, competing market makers, specialists and registered options traders.²⁴ Under the proposal, non-broker-dealer customer orders at the ABBO would always have priority over all other market participants in the ANTE System. Multiple public customer orders in ANTE at the ABBO would be ranked for allocation purposes based on time priority. An ANTE Participant quoting alone at the ABBO would be allocated all contracts executed at his disseminated bid or offer up to the disseminated size. When more than one ANTE Participant is quoting or has orders at the ABBO, executed contracts would be automatically allocated as follows: (i) all non-broker-dealer

²³ Under proposed Amex Rule 933-ANTE, Commentary .03, the specialist would be required to establish for each option series emergency quote parameters, which shall be retained by the ANTE System.

²⁴ In addition, Quick Trade, an allocation system in place today to aid in allocating executed contracts, would continue to exist in the ANTE System to assist in the allocation of executed contracts resulting from transactions occurring outside the ANTE System in the trading crowd.

customer orders would be allocated first; (ii) specialist participating in the quote would be allocated executed contracts in accordance with the specialist participation schedule set forth in Amex Rule 935—ANTE; and (iii) remaining executed contracts would be allocated to broker-dealers and competing market makers as one ANTE Participant, and registered options traders as individual ANTE Participants in accordance with provisions also set forth in Amex Rule 935—ANTE.

The Exchange also proposes in Amex Rule 935-ANTE (b) that ANTE Participants and floor brokers representing customer orders be able to trade with orders in the Central Book. Under the proposal, executed contracts would be allocated to single or multiple ANTE Participants provided they have submitted their orders within five seconds of the initial ANTE Participant's submission. The ANTE Participant that first submits the order to trade with the order in the Central Book would be allocated executed contracts up to a size established on a class-by-class basis by the Options Trading Committee and referred to as the "Take Size."²⁵ The Options Trading Committee would review and in some cases revise the assigned "Take Sizes" on a periodic basis, but would not change a "Take Size" during the course of a trading day.

Since the ANTE System initially would not be able to provide floor brokers representing a customer order in the trading crowd with the ability to participate in the post allocation of orders taken off the Central Book,²⁶ the Amex would require: (i) the specialist to disengage the

²⁵ The Options Trading Committee would consider the option's liquidity and the size of the trading crowd in determining the appropriate "Take Size" for each option class. The Exchange represents that the Options Trading Committee's authority to establish the Take Size for a given options class will not be used in a discriminatory manner.

²⁶ Proposed Commentary .01 to Amex Rule 935(b) – ANTE sets forth that the ANTE System would provide floor broker's with greater functionality accessing the Central Book by March 31, 2005 or such later date as established by the Exchange and submitted to the Commission pursuant to Section 19(b) of the Act.

post trade allocation feature in the options series represented by the floor broker's customer order, provided the floor broker has alerted the specialist that he is working a customer order in a specified series; (ii) once the floor broker's customer order has been executed or the floor broker leaves the trading crowd, the specialist to re-engage the post trade allocation feature; (iii) the floor broker to alert the specialist within the five-second timeframe whenever he wants to participate on behalf of his customer in the post trade allocation of orders taken off the specialist's book; (iv) floor brokers to keep a written record of when they have alerted a specialist that they want to participate in the post trade allocation; and (v) the specialist to add the customer's interest being represented by the floor broker in the post trade allocation whenever appropriate.²⁷ While the specialist would be required to keep track of the floor broker's allocation, the Commission expects the Exchange to ensure that the ANTE System is providing an auditable record of which ANTE Participants successfully submitted orders during the five-second period and were therefore entitled to participate in post trade allocation of executed contracts. The Commission finds Amex's proposal to allow the specialist to represent the floor broker's customer interest to be a reasonable, temporary solution.

G. Automated Opening, Re-Opening and Closing Rotations

The Exchange proposes under Amex Rule 918-ANTE for an automated and orderly process for the opening, re-opening after a trading halt, and closing of all option classes. The automated opening, re-opening, and closing rotations would be held in the same manner. The Exchange would require that the specialist always submit a two-sided quote for each option series to be used in the opening and closing sessions. Registered options traders would be able to

²⁷ To accomplish an allocation to the floor broker's order, the specialist could, on a series-by-series basis, shut off the automated post trade allocation feature and manually allocate the executed contracts.

view the same information as the specialist in the opening and closing session windows and participate in the rotations. To participate at the opening and the closing rotations, registered options traders could either: (i) submit quotes for use during the automated opening and closing rotations; (ii) join the specialist's quote; or (iii) submit limit orders on a series by series basis.²⁸

Prior to the opening rotation, the ANTE System would receive all pre-opening orders, orders on the book from the previous trading day, and a theoretical quote based on the previous closing price for each option series he trades. After the underlying stock opens, the options specialist would be able to open the overlying options by accessing the opening session window and allowing the submission of quotes and orders that have been entered. During the activation of the opening session window, no additional quotes, orders, or cancellations would be permitted until the series opens. Under the proposal, the ANTE System would automatically pair-off the opening orders at a suggested price based on previous day and pre-opening limit orders and the specialist's and registered options traders' theoretical quotes. In those situations when the ANTE System is unable to determine an appropriate opening price, the system would present the series to the specialist for the manual setting of an opening price in that series. Once opened, orders and quote updates again would be permitted and active trading could begin.

Unlike the current Amex Rule 918 (a)(4), which provides for a closing rotation to be held on the last trading day for expiring option series, the ANTE System under proposed Amex Rule 918—ANTE(a)(4) would require an automated closing rotation to be held in all option series at the end of every trading day. The Exchange proposes to use the automated closing rotation to execute at-the-close orders received by the Exchange prior to the close. If no at-the-close orders are received in a particular option series, then the ANTE System's automated closing rotation

²⁸ Under Amex Rule 918-ANTE, Commentary .01(b), registered options traders would not be able to submit market orders in the automated opening rotation.

would simply close trading in that series. Orders could be entered, modified or cancelled into the ANTE System up to 4:02 p.m., or 4:15 p.m. for options on Exchange Traded Fund Shares when the underlying Fund Share ceases trading at 4:15 p.m. Under proposed Amex Rule 918-ANTE, Commentary .01(f), quotes could be submitted up until the commencement of the rotation in such series, and the closing rotation could begin once the underlying security has closed.

The Commission believes that the proposed rules governing the automated opening, re-opening and closing rotations provide a reasonable process by which ANTE Participants would access and participate in the rotations and are consistent with the Act.

H. Application of “Effect v. Execute” Exemption from Section 11(a) of the Act

Section 11(a) of the Exchange Act²⁹ prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises discretion (collectively, “covered accounts”) unless an exception applies. In addition to the exceptions set forth in the statute, Rule 11a2-2(T)³⁰ provides exchange members with an exemption from this prohibition. Known as the “effect versus execute” rule, Rule 11a2-2(T) permits an exchange member, subject to certain conditions, to effect transactions for covered accounts by arranging for an unaffiliated member to execute the transactions on the exchange. To comply with the rule’s conditions, a member (i) must transmit the order from off the exchange floor; (ii) may not participate in the execution of the transaction once it has been transmitted to the member performing the execution;³¹ (iii) may not be affiliated with the executing member; and (iv) with respect to an account over which the member has investment discretion, neither the member nor its associated

²⁹ 15 U.S.C. 78k(a).

³⁰ 17 CFR 240.11a2-2(T).

³¹ The member, however, may participate in clearing and settling the transaction.

person may retain any compensation in the connection with effecting the transaction except as provided in the Rule.

In a letter dated May 20, 2004,³² the Amex represents that transactions effected on ANTE satisfy the conditions of Rule 11a2-2(T). Based on these representations, the Commission finds that the order execution algorithm of ANTE complies with the requirements of Section 11(a) of the Exchange Act and Rule 11a2-2(T) thereunder.

In particular, the Amex states that ANTE “will place all users of the Exchange’s ANTE System, members and non-members, on the ‘same footing’” and that “at no time following the submission of an order will a broker-dealer who enters an order retain any ability to control the timing of an execution or otherwise enjoy the kind of special order-handling advantages inherent in being on an exchange floor.” Specifically, orders sent to ANTE will be transmitted from remote locations (via the member interface) directly to ANTE by electronic means. Once an order is submitted to ANTE, the order is executed against another order based on an established matching algorithm. As the Amex explains, the execution does not depend on the broker-dealer but rather upon what other orders are entered into ANTE at or around the same time as the subject order, what orders are on the specialist’s book and where the order is ranked based on the price-time priority ranking algorithm. Accordingly, members do not control or influence the result or timing of orders submitted to ANTE. Finally, Amex represents that ANTE will continue the program currently in place, which allows orders for the accounts of broker-dealers to be eligible for execution through the Exchange’s Auto-Ex system. The Commission notes that the staff of the Division previously provided interpretive guidance to the Amex regarding its

³² See letter from Claire McGrath, Senior Vice President and Deputy General Counsel, Amex, to Kelly Riley, Division, Commission, dated May 20, 2004.

Auto-Ex system.³³ Based on Amex's representations, the staff believed that the execution of broker-dealer orders in the Amex Auto-Ex system satisfied the effect v. execute rule.

Based on the Amex's representations regarding ANTE, the Commission finds that ANTE's electronic order submission and execution process also satisfies the four conditions of Rule 11a2-2(T).³⁴ First, all orders are electronically submitted through remote terminals off the exchange floor. Second, because a member relinquishes control of its order after it is submitted to ANTE and will not be able to influence or guide the execution of its order, the member would not be participating in the execution of its order. Third, although the rule contemplates having an order executed by an exchange member who is not affiliated with the member initiating the order, the Commission recognizes that this requirement is satisfied when automated exchange facilities are used.³⁵ Fourth, the Amex states that members that rely on Rule 11a2-2(T) for a

³³ See letter from Paula R. Jenson, Deputy Chief Counsel, Division, Commission, to Jeffrey P. Burns, Assistant General Counsel, Amex, dated July 9, 2002.

³⁴ The Commission and its staff, on numerous occasions, have considered the application of Rule 11a2-2(T) to electronic trading and order routing systems. See, e.g., Securities Exchange Act Release Nos. 49068 (January 13, 2004) (Order approving the Boston Options Exchange as an options trading facility of the Boston Stock Exchange); 44983 (October 25, 2001) (Order approving the Archipelago Exchange as the equities trading facility of PCX Equities Inc.); 29237 (May 31, 1991) (regarding NYSE's Off-Hours Trading Facility); 15533 (January 29, 1979) (regarding the Amex Post Execution Reporting System, the Amex Switching System, the Intermarket Trading System, the Multiple Dealer Trading Facility of the Cincinnati Stock Exchange, the PCX's Communications and Execution System, and the Phlx's Automated Communications and Execution System); and 14563 (March 14, 1978) (regarding the NYSE's Designated Order Turnaround System). See also Letter from Larry E. Bergmann, Senior Associate Director, Division, Commission, to Edith Hallahan, Associate General Counsel, Phlx (March 24, 1999) (regarding Phlx's VWAP Trading System); letter from Catherine McGuire, Chief Counsel, Division, Commission, to David E. Rosedahl, PCX (November 30, 1998) (regarding Optimark); and Letter from Brandon Becker, Director, Division, Commission, to George T. Simon, Foley & Lardner (November 30, 1994) (regarding Chicago Match).

³⁵ In considering the operation of automated execution systems operated by an exchange, the Commission noted that while there is no independent executing exchange member, the execution of an order is automatic once it has been transmitted into the systems.

managed account transaction must comply with the limitations on compensation set forth in the rule.

V. Accelerated Approval of Amendment No. 7

The Commission finds good cause for approving Amendment No. 7 to the proposed rule change prior to the thirtieth day after the amendment is published for comment in the Federal Register pursuant to Section 19(b)(2) of the Act.³⁶ Amendment No. 7 addresses concerns raised by Commission staff by clarifying in proposed Amex Rule 951-ANTE, Commentary .01 that if the bid or offer of a specialist or registered options trader locks or crosses the ABBO, the ANTE System would revise the bid by the minimum price variations so that the bid or offer submitted does not lock or cross the ABBO, provided, however, if the ABBO represents an off-floor limit order, the ANTE System would execute the order and allocate the trade pursuant to the post trade allocation process. The Commission believes that the proposed change in Amendment No. 7, which provides for a clearer understanding of the operation in the ANTE System of Amex Rule 951-ANTE, Commentary .01, raises no new issues of regulatory concern and, therefore, believes that accelerated approval of Amendment No. 7 is appropriate.

VI. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with Section 6(b)(5) of the Act.³⁷

Because the design of these systems ensures that members do not possess any special or unique trading advantages in handling their orders after transmitting them to the exchange, the Commission has stated that executions obtained through these systems satisfy the independent execution requirement of Rule 11a2-2(T). See Securities Exchange Act Release No. 15533 (January 29, 1979).

³⁶ 15 U.S.C. 78s(b)(2).

³⁷ 15 U.S.C. 78f(b)(5).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,³⁸ that the proposed rule change (SR-Amex-2003-89) and Amendments No. 1, 2, 3, 4, 5 and 6 thereto are approved, and that Amendment No. 7 thereto is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.³⁹

Margaret H. McFarland
Deputy Secretary

³⁸ 15 U.S.C. 78s(b)(2).

³⁹ 17 CFR 200.30-3(a)(12).