

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50812; File No. SR-AMEX-2004-81)

December 7, 2004

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change by the American Stock Exchange LLC Relating to the Listing and Trading of Notes Linked to the Performance of the Nasdaq-100 Index

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 October 4, 2004, the American Stock Exchange LLC (“Amex” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and is approving the proposal on an accelerated basis.

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

The Exchange proposed to list and trade notes, the performance of which is linked to the Nasdaq-100 Index (“Nasdaq-100” or “Index”).

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 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

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

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

Item III below. The Amex has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

Under Section 107A of the Amex Company Guide (“Company Guide”), the Exchange may approve for listing and trading securities that cannot be readily categorized under the listing criteria for common and preferred stocks, bonds, debentures, or warrants.<sup>3</sup> The Amex proposes to list for trading under Section 107A of the Company Guide notes linked to the performance of the Nasdaq-100 (the “LUNARS” or “Notes”).<sup>4</sup> The Nasdaq-100 is determined, calculated and maintained solely by Nasdaq.<sup>5</sup> The Notes will provide for a multiplier of any positive

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<sup>3</sup> See Securities Exchange Act Release No. 27753 (March 1, 1990), 55 FR 8626 (March 8, 1990) (File No. SR-Amex-89-29) (“Approving Order”).

<sup>4</sup> Wachovia Corporation (“Wachovia”) and The Nasdaq Stock Market, Inc. (“Nasdaq”) have entered into a non-exclusive license agreement providing for the use of the Nasdaq-100 by Wachovia and certain affiliates and subsidiaries in connection with certain securities including these Notes. Nasdaq is not responsible and will not participate in the issuance and creation of the Notes.

<sup>5</sup> The Nasdaq-100 is a modified capitalization-weighted index of 100 of the largest and most active non-financial domestic and international issues listed on Nasdaq. The Index is determined, comprised and calculated by Nasdaq without regard to the Notes. The Index is calculated and disseminated every fifteen seconds to market information vendors. The Exchange states that the Nasdaq-100 reflects the largest growth companies across major industry groups with all index components of domestic issuers having a market capitalization of at least \$500 million and an average daily trading volume of at least 100,000 shares. For foreign issuers, the worldwide market capitalization must be at least \$10 billion with a U.S. market capitalization of at least \$4 billion and an average daily trading volume of at least 200,000 shares. In addition, no single security comprising the Nasdaq-100 is permitted to have more than a 24% weighting. The Nasdaq-100 was originally developed with a base value of 125 on February 1, 1985. Originally a capitalization-weighted index, on December 21, 1998, the Nasdaq-100 changed to a modified capitalization-weighted index. A modified capitalization-weighted index is a hybrid between equal weighting and capitalization-weighting. This type of

performance of the Nasdaq-100 during such term subject to a maximum payment amount or ceiling.

The “LUNARS” or “Leveraged Upside Indexed Accelerated Return Securities” will conform to the initial listing guidelines under Section 107A<sup>6</sup> and continued listing guidelines under Sections 1001-1003<sup>7</sup> of the Company Guide. The Notes are senior, non-convertible debt

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methodology is expected to: (1) retain the economic attributes of capitalization weighting; (2) promote portfolio weight diversification; (3) reduce Nasdaq-100 performance distortion by preserving the capitalization ranking of companies; and (4) reduce market impact on the smallest Nasdaq-100 securities from necessary weight rebalancings. A quarterly examination of the Nasdaq-100 is performed to gauge whether a rebalancing of the Index is necessary. If one of the following weight distribution requirements is not met, then the Index is rebalanced. These requirements are as follows: (1) the current weight of the single largest market capitalization index security must be less than or equal to 24%, and (2) the collective weight of those index securities whose individual current weights are in excess of 4.5%, when added together, must be less than or equal to 48.0%.

<sup>6</sup> Section 107A of the Amex Company Guide requires: (1) a minimum public distribution of one million units; (2) a minimum of 400 shareholders; (3) a market value of at least \$4 million; and (4) a term of at least one year. However, when the instrument will be issued in \$1,000 denominations, as here, the minimum public distribution requirement of one million units and the minimum holder requirement of 400 holders do not apply. In addition, the listing guidelines provide that the issuer has assets in excess of \$100 million, stockholder’s equity of at least \$10 million, and pre-tax income of at least \$750,000 in the last fiscal year or in two of the three prior fiscal years. In the case of an issuer that is unable to satisfy the earning criteria stated in Section 101 of the Company Guide, the Exchange will require the issuer to have the following: (1) assets in excess of \$200 million and stockholders’ equity of at least \$10 million; or (2) assets in excess of \$100 million and stockholders’ equity of at least \$20 million.

<sup>7</sup> The Exchange’s continued listing guidelines are set forth in Sections 1001 through 1003 of Part 10 to the Exchange’s Company Guide. Section 1002(b) of the Company Guide states that the Exchange will consider removing from listing any security where, in the opinion of the Exchange, it appears that the extent of public distribution or aggregate market value has become so reduced to make further dealings on the Exchange inadvisable. With respect to continued listing guidelines for distribution of the Notes, the Exchange will rely, in part, on the guidelines for bonds in Section 1003(b)(iv). Section 1003(b)(iv)(A) provides that the Exchange will normally consider suspending dealings

securities of Wachovia. The Notes will have a term of not less than one or more than ten years. The original public offering price will be \$1,000 per Note. The Notes will entitle the owner at maturity to receive an amount based upon the percentage change of the Nasdaq-100. At maturity, if the value of the Nasdaq-100 has increased over the term of the Notes, a beneficial owner will be entitled to receive a payment on the Notes equal to three (3) times the amount of that percentage increase, not to exceed a maximum payment at maturity (the “Maximum Payment”) to be determined at the time of issuance of the Notes. It is expected that the Maximum Payment will be between 116-122% of the principal amount, in other words between \$1,160 to \$1,220 per \$1,000 Note. The Notes will not have a minimum principal amount that will be repaid, and accordingly, payment on the Notes prior to or at maturity may be less than the original issue price of the Notes because the final payment per Note will be exposed to the full decrease of the Index.<sup>8</sup> The Notes are also not callable by the Issuer, or redeemable by the holder.

The payment that a holder or investor of a Note will be entitled to receive (the “Maturity Payment”) depends entirely on the relation of the value of the Nasdaq-100 at the close of the fifth scheduled trading day before the maturity date (the “Index Ending Level”) and the closing value of the Index on the date the Notes are priced for initial sale to the public (the “Index Starting Level”). In the event that the valuation date occurs on a non-trading day or if a market

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in, or removing from the list, a security if the aggregate market value or the principal amount of bonds publicly held is less than \$400,000.

<sup>8</sup> A negative return of the Nasdaq-100 will reduce the redemption amount at maturity with the potential that the holder of the Note could lose his entire investment. The Notes are not “principal protected” and are fully exposed to any decline in the level of the Nasdaq-100.

disruption event<sup>9</sup> occurs on such date, the valuation date will be the next trading day on which no market disruption event occurs.

If the Index Ending Level is greater than the Index Starting Level, the Maturity Payment per Note will equal:

$$\$1,000 \times \left[ 1 + \left( 3.0 \times \frac{\text{Index Ending Level} - \text{Index Starting Level}}{\text{Index Starting Level}} \right) \right]$$

subject to the Maximum Payment.

If the Index Ending Level is less than or equal to the Index Starting Level, the Maximum Payment per Note will equal:

$$\$1,000 \times \left( 1 + \frac{\text{Index Ending Level} - \text{Index Starting Level}}{\text{Index Starting Level}} \right)$$

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<sup>9</sup> A “market disruption event” is defined as the failure of the primary market or related markets to open for trading during regular trading hours or the occurrence or existence of any of the following events: (i) a trading disruption, if material, at any time during the one hour period that ends at the close of trading for the applicable exchange; (ii) an exchange disruption, if material, at any time during the one hour period that ends at the close of trading for the applicable exchange; or (iii) an early closure. A “trading disruption” generally means any suspension of, or limitation, imposed on trading by the primary exchange or related exchange or otherwise, whether by reason of movements in price exceeding limits permitted by the relevant exchange or related exchange or otherwise (i) relating to securities that comprise 20% or more of the level of the Index or (ii) in options contracts or futures contracts relating to the Index on any relevant related exchange. An “exchange disruption” means any event (other than a scheduled early closure) that disrupts or impairs the ability of market participants in general to (i) effect transactions in, or obtain market values on, any primary exchange or related exchange in securities that comprise 20 percent or more of the level of the Index or (ii) effect transactions in options contracts or futures contracts relating to the Index on any relevant related exchange. A “related exchange” is an exchange or quotation system on which futures or options contracts relating to the Index are traded.

The Notes are cash-settled in U.S. dollars and do not give the holder any right to receive a portfolio security, dividend payments, or any other ownership right or interest in the portfolio or index of securities comprising the Nasdaq-100. The Notes are designed for investors who want to participate or gain exposure to the Nasdaq-100, subject to a cap, and who are willing to forego market interest payments on the Notes during such term. The Commission has previously approved the listing of options on, and securities the performance of which have been linked to or based on, the Nasdaq-100.<sup>10</sup>

As of September 24, 2004, the market capitalization of the securities included in the Nasdaq-100 ranged from a high of \$297.5 billion to a low of \$1.4 billion. The average daily trading volume for these same securities for the last six (6) months, as of the same date, ranged from a high of 14.4 million shares to a low of 1 million shares.

Because the Notes are issued in \$1,000 denominations, the Amex's existing debt floor trading rules will apply to the trading of the Notes. First, pursuant to Amex Rule 411, the Exchange will impose a duty of due diligence on its members and member firms to learn the essential facts relating to every customer prior to trading the Notes.<sup>11</sup> Second, even though the

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<sup>10</sup> Approval of the Nasdaq-100 for underlying an option contract was originally granted to the Chicago Board Options Exchange ("CBOE") in 1994. See Securities Exchange Act Release Nos. 33428 (January 4, 1994), 59 FR 1576 (January 11, 1994) (approval to list and trade options on the Nasdaq-100); 34052 (May 12, 1994), 59 FR 25972 (May 18, 1994) (approval to list and trade Flex Options on the Nasdaq-100); 40157 (July 1, 1998), 63 FR 37426 (July 10, 1998) (approval to list and trade options on ETFs); 41119 (February 26, 1999), 64 FR 11510 (March 9, 1999) (approval to list and trade QQQ); 43000 (June 30, 2000), 65 FR 42409 (July 10, 2000) (approval of a Reduced Value Nasdaq-100); and 45966 (May 20, 2002), 67 FR 36942 (May 28, 2002) (approval to list and trade notes linked to the performance of the Nasdaq-100).

<sup>11</sup> Amex Rule 411 requires that every member, member firm or member corporation use due diligence to learn the essential facts, relative to every customer and to every order or account accepted.

Exchange's debt trading rules apply, the Notes will be subject to the equity margin rules of the Exchange.<sup>12</sup> Third, the Exchange will, prior to trading the Notes, distribute a circular to the membership providing guidance with regard to member firm compliance responsibilities (including suitability recommendations) when handling transactions in the Notes and highlighting the special risks and characteristics of the Notes. With respect to suitability recommendations and risks, the Exchange will require members, member organizations and employees thereof recommending a transaction in the Notes: (1) to determine that such transaction is suitable for the customer, and (2) to have a reasonable basis for believing that the customer can evaluate the special characteristics of, and is able to bear the financial risks of such transaction. In addition, Wachovia will deliver a prospectus in connection with the initial sales of the Notes.

The Exchange represents that its surveillance procedures are adequate to properly monitor the trading of the Notes. Specifically, the Amex will rely on its existing surveillance procedures governing equities, which have been deemed adequate under the Act. In addition, the Exchange also has a general policy which prohibits the distribution of material, non-public information by its employees.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6 of the Act<sup>13</sup> in general and furthers the objectives of Section 6(b)(5)<sup>14</sup> in particular in that it is designed

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<sup>12</sup> See Amex Rule 462 and Section 107B of the Company Guide.

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

<sup>14</sup> 15 U.S.C. 78f(b)(5).

to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, protect investors and the public interest.

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

The Exchange 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

The Exchange did not receive any written comments on the proposed rule change.

III. 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 SR-Amex-2004-81 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 SR-Amex-2004-81. 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 SR-Amex-2004-81 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

After careful consideration, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder, applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b)(5) of the Act.<sup>15</sup> The Commission has approved the listing of securities with a structure similar to that of the Notes.<sup>16</sup> Accordingly, the Commission finds that the listing and trading of the Notes based on the Index is consistent with the Act and will promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling,

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<sup>15</sup> Id.

<sup>16</sup> See Securities Exchange Act Release Nos. 48152 (July 10, 2003), 68 FR 42435 (July 17, 2003) (approving the listing and trading of the UBS Partial Protection Note linked to the Index); 47983 (June 4, 2003), 68 FR 35032 (June 11, 2003) (approving the listing and trading of a CSFB Accelerated Return Notes linked to Index); 47911 (May 22, 2003), 68

processing information with respect to, and facilitating transactions in securities, and, in general, protect investors and the public interest consistent with Section 6(b)(5) of the Act.<sup>17</sup>

The requirements of Section 107A of the Company Guide were designed to address the concerns attendant to the trading of hybrid securities, like the Notes. For example, Section 107A of the Company Guide provides that only issuers satisfying substantial asset and equity requirements may issue securities such as the Notes. In addition, the Exchange's "Other Securities" listing standards further require that the Notes have a market value of at least \$4 million.<sup>18</sup> The Commission also notes that the 100 component stocks that comprise the Index are reporting companies under the Act, and the Notes will be registered under Section 12 of the Act. Thus, by imposing the hybrid listing standards, suitability, disclosure, and compliance requirements noted above, the Commission believes the Amex has addressed adequately the potential problems that could arise from the hybrid nature of the Notes.

In approving the product, the Commission recognizes that the Index is a modified capitalization-weighted index<sup>19</sup> of 100 of the largest and most active non-financial domestic and international companies listed on Nasdaq. Given the large trading volume and capitalization of the compositions of the stocks underlying the Index, the Commission believes that the listing and trading of the Notes that are linked to the Index should not unduly impact the market for the

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FR 32558 (May 30, 2003) (approving the listing and trading of notes (Wachovia TEES) linked to the Index).

<sup>17</sup> 15 U.S.C. 78f(b)(5). In approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>18</sup> See Company Guide Section 107A.

<sup>19</sup> See supra Note 5.

underlying securities compromising the Index or raise manipulative concerns.<sup>20</sup> Moreover, the issuers of the underlying securities comprising the Index are subject to reporting requirements under the Act, and all of the component stocks are either listed or traded on, or traded through the facilities of, U.S. securities markets.

The Commission also believes that any concerns that a broker-dealer, such as Wachovia, or a subsidiary providing a hedge for the issuer, will incur undue position exposure are minimized by the size of the Notes issuance in relation to the net worth of Wachovia.<sup>21</sup>

Finally, the Commission notes that the value of the Index will be widely disseminated at least once every fifteen seconds throughout the trading day. The Exchange represents that the Nasdaq-100 will be determined, calculated and maintained solely by Nasdaq.

The Commission finds good cause for approving the proposed rule change prior to the 30th day after the date of publication of the notice of filing thereof in the Federal Register. The Exchange has requested accelerated approval because this product is similar to several other

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<sup>20</sup> The issuer Wachovia disclosed in the prospectus that the original issue price of the Notes includes commissions (and the secondary market prices are likely to exclude commissions) and Wachovia's costs of hedging its obligations under the Notes. These costs could increase the initial value of the Notes, thus affecting the payment investors receive at maturity. Such hedging activity must, of course, be conducted in accordance with applicable regulatory requirements.

<sup>21</sup> See Securities Exchange Act Release Nos. 44913 (October 9, 2001), 66 FR 52469 (October 15, 2001) (order approving the listing and trading of notes whose return is based on the performance of the Nasdaq-100 Index) (File No. SR-NASD-2001-73); 44483 (June 27, 2001), 66 FR 35677 (July 6, 2001) (order approving the listing and trading of notes whose return is based on a portfolio of 20 securities selected from the Amex Institutional Index) (File No. SR-Amex-2001-40); and 37744 (September 27, 1996), 61 FR 52480 (October 7, 1996) (order approving the listing and trading of notes whose return is based on a weighted portfolio of healthcare/biotechnology industry securities) (File No. SR-Amex-96-27).

instruments currently listed and traded on the Amex.<sup>22</sup> The Commission believes that the Notes will provide investors with an additional investment choice and that accelerated approval of the proposal will allow investors to begin trading the Notes promptly. Additionally, the Notes will be listed pursuant to Amex's existing hybrid security listing standards as described above. Therefore, the Commission finds good cause, consistent with Section 19(b)(2) of the Act,<sup>23</sup> to approve the proposal on an accelerated basis.

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<sup>22</sup> See Securities Exchange Act Release Nos. 45966 (May 20, 2002), 67 FR 36942 (May 28, 2002) (approval to list and trade notes linked to the performance of the Nasdaq-100); 47911 (May 22, 2003), 68 FR 32558 (May 30, 2003) (approving the listing and trading of notes (Wachovia TEES) linked to the S&P 500); 47983 (June 4, 2003), 68 FR 35032 (June 11, 2003) (approving the listing and trading of a CSFB Accelerated Return Notes linked to S&P 500); and 50019 (July 14, 2004), 69 FR 43635 (July 21, 2004) (approving the listing and trading of Morgan Stanley PLUS Notes).

<sup>23</sup> 15 U.S.C. 78f(b)(5) and 78s(b)(2).

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>24</sup> that the proposed rule change (SR-Amex-2004-81) is hereby approved on an accelerated basis.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>25</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>24</sup> 15 U.S.C. 78o-3(b)(6) and 78s(b)(2).

<sup>25</sup> 17 CFR 200.30-3(a)(12).