

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-52741; File No. SR-Amex-2005-115)

November 4, 2005

Self-Regulatory Organizations; American Stock Exchange LLC; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change Regarding Options Quote Size Mitigation

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 November 4, 2005, the American Stock Exchange LLC (“Amex” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been substantially prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and to approve the proposal on an accelerated basis.

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

The Exchange proposes to adopt an options market data size mitigation policy (“Options Size Mitigation”) on a four (4) month pilot basis. The text of the proposed rule change is available on the Amex’s Web site at <http://www.amex.com>, the Office of the Secretary, the Amex, and at the Commission’s Public Reference Room.

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

---

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

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

the places specified in Item III below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant 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

The purpose of the proposal is to adopt an Options Size Mitigation policy for the benefit of the Exchange and the marketplace, by helping to enhance the Exchange's ability to process an increasing volume of incoming options quotes.<sup>3</sup> The Exchange believes that Options Size Mitigation will help to prevent potential data delays and enhance our existing ability to manage market data traffic.

The recent growth in options quote message traffic is largely the result of the increase in the multiple trading of equity options, conversion to decimal pricing, technological advancements in options quoting systems, the dissemination of quotes with size and changes in market structure through the greater use of electronic quoting systems by market participants and the options exchanges. In the past, the options exchanges together with the Options Price Reporting Authority ("OPRA") discussed plans to develop strategies to mitigate options message traffic.<sup>4</sup> In addition, the "Report of the

---

<sup>3</sup> In January 2000, OPRA capacity was 3,000 messages per second ("MPS") with an expectation during the year to increase to 8,000 and 12,000 MPS, respectively. As an example, one-minute and five-minute peak output rates in March 2000 were 3,515 and 3393 MPS, respectively. OPRA in 2001 increased system capacity to 24,000 MPS. Moving forward to October 2005, the current system capacity is 125,000 MPS with one-minute and five-minute peak output rates of 86,342 MPS (9/27/05) and 70,783 MPS (10/05/05), respectively.

<sup>4</sup> In December 1999, the Securities Industry Automation Corporation ("SIAC") and SRI Consulting issued a report entitled "Mitigating Options Message Traffic" (the "SRI Study") recommending short-term and long-term solutions to the growth in options message traffic at that time. The recommendations focused on a

Advisory Committee on Market Information: A Blueprint for Responsible Change” (the “Seligman Report”) issued in 2001 identified system capacity concerns as a problem for the options industry.<sup>5</sup> The Seligman Report also cited industry quote mitigation efforts.<sup>6</sup> However, to date, the options exchanges have not agreed to a quote mitigation strategy at the OPRA level.

#### Proposed Options Size Mitigation

During the last few months, the Exchange has made several upgrades to its systems to increase the ability of the Amex to handle increases in market data. The Exchange is continuing in these efforts to implement further enhancements to its system capacity so that the Exchange is able to handle expected increases in market data in the future.<sup>7</sup>

The continuing increases in options industry quote traffic rates have challenged the Exchange’s ability (as well as the industry on a whole) to process market data in a

---

reduction in the number of products quoted and traded. The options exchanges collectively have not agreed to the recommendations of the SRI Study.

<sup>5</sup> The Seligman Report maintained that capacity concerns exist at every level in the distribution chain of options market data: the options exchanges, the consolidator (SIAC), vendors and broker-dealers. In addition, due to the nature of the options business, a far larger volume of options information is disseminated than occurs in the equity markets. As reported in the Seligman Report, options data accounts for approximately 70-80% of U.S. market data traffic. This percentage may have actually increased since 2001 due to the exponential growth during the last few years in options quoting.

<sup>6</sup> The Seligman Report noted that the options exchange have been working on appropriate quote mitigation strategies as follows: (1) a “request-for-quote” system for less actively-traded options series; (2) more stringent listing standards and more aggressive delisting policies; (3) desensitization of auto-quote systems; and (4) modification of the “firm quote rule” to reduce the need to auto-quote “out-of-the-money” and away from the market quotes.

<sup>7</sup> The Exchange notes that system capacity at the OPRA level is 125,000 MPS. This level is expected to increase to 149,000 MPS on January 1, 2006.

timely manner. The Exchange believes that the proposed Options Size Mitigation policy is beneficial and will enhance our ability to process inbound quote traffic and help prevent market data delays. As detailed below, the Exchange submits that when Options Size Mitigation is in effect, specialists will nonetheless be able to comply with their trade-through and best execution obligations.

Under Options Size Mitigation, during high quote volume periods and peaks, incoming market data will be filtered prior to being forwarded to floor trading systems. When in effect, Options Size Mitigation will filter market data by not processing incoming quotes (i.e. away market quotes) with size changes below a variable percent. However, Amex systems will always maintain and display Amex quotations with accurate size regardless of whether Options Size Mitigation is in effect.

For example, if the filtering is set at 10%, away market quotations that change (i.e., increase or decrease) the existing size of the quotation by 10% or less would not be forwarded to floor trading systems or displayed to specialists. The filtering level would be set on an exchange-wide basis, based on either the number of MPS exceeding a predefined amount or when a delay of a predetermined length has occurred in the processing of market data.

The Exchange submits that the initial Options Size Mitigation filtering level will be set at 10% with the ability to increase the filtering level in 10% level increments as warranted. The head of the Exchange's Floor Operations (or his designee), in conjunction with two (2) Senior Floor Officials, will determine the appropriate filtering level. The Exchange will ensure that all options market data (including filtered quotes) is available for regulatory and surveillance purposes.

When Options Size Mitigation is in effect, an announcement will be made on the trading floor, advising members regarding the level of filtering. As a result, specialists will be able to assess (when the Amex is not the NBBO) the potential that the size of an away market NBBO quotation may be inaccurate. Thus, if a 10% filtering is in effect, for any potentially affected orders, the specialist would be required to view a third-party quotation vendor in order to verify whether the displayed size is accurate. Based on a 10% filtering level, only those orders that are greater than 10% below the NBBO size would potentially be affected. For example, if the displayed NBBO size from an away market is 1,000 contracts, any order size between 900 and 1,100 contracts would potentially be affected under Options Size Mitigation. Therefore, reliance on third-party quotation vendors by specialists is especially important for away market quotes when Options Size Mitigation is in effect.

To the extent that the NBBO quotation size (when the Amex is not the NBBO) is inaccurate and/or the specialist does not have time to view a third-party vendor, he or she will need to determine whether it is necessary to send the full order size to the away market. If the specialist does not send the full order to the away market, he or she will need to wait for a response from the away market prior to taking any action with respect to the balance of the order.

Certain Linkage Plan and related Amex Rule obligations are premised on quotation sizes being disseminated by the exchanges. For example, the definition of Firm Customer Quote Size (“FCQS”) in Section 2 of the Linkage Plan refers to disseminated quotation sizes. In addition, the obligation to provide an automatic execution is premised

on the size of a Linkage Order being no larger than the FCQS.<sup>8</sup> In all cases, the Exchange pursuant to the Linkage Plan and related rules is required to provide an execution for at least the FCQS.

The Commission recently approved Linkage Plan Amendment No. 16 and related Exchange Rules defining FCQS as the number of option contracts that the Participant Exchange<sup>9</sup> receiving a Principal Acting as Agent (“P/A”)<sup>10</sup> Order guarantees it will automatically execute at its disseminated quotation in a series of an eligible option class for public customer orders entered directly for execution in that market.<sup>11</sup> The Exchange recently incorporated a change into its systems to accommodate the change to FCQS. As a result, inbound P/A Orders are executed up to the size of the disseminated quotation for that series of an eligible options class rendering unnecessary the size of the sending Participant Exchange’s quotation. In this manner, the Exchange is fully compliant with the current definition of FCQS.

The Exchange submits that the vast majority of its options orders will be largely unaffected by the Options Size Mitigation policy. The typical order size that the

---

<sup>8</sup> See Amex Rule 941(e).

<sup>9</sup> “Participant Exchange” is defined in Amex Rule 940(b)(14) to mean a registered national securities exchange that is a party to the Linkage Plan.

<sup>10</sup> A P/A Order is defined in Amex Rule 940(b)(10)(i) to mean an order for the principal account of a specialist (or equivalent entity on another Participant Exchange that is authorized to represent customer orders), reflecting the terms of a related unexecuted public customer order for which the specialist is acting as agent.

<sup>11</sup> See Securities Exchange Act Release Nos. 52656 (October 24, 2005), 70 FR 66477 (November 2, 2005) (approval of Joint Amendment No. 16 to the Intermarket Option Linkage Plan Relating to the Definition of Firm Customer Quote Size and Restrictions on Sending Certain Principal Acting as Agent Orders; File No. 4-429) and 52657 (October 24, 2005), 70 FR 65941 (November 1, 2005)(approving the rules of the options exchanges).

Exchange receives is approximately twenty (20) contracts. As set forth above, the significance of displayed options quotations sizes concerns the Exchange's obligation to provide an execution through the Options Linkage in an amount equal to the FCQS. In connection with the Exchange's ANTE system, FCQS is largely determined by the maximum order size eligible for automatic execution (the "auto-match" size). The Options Trading Committee has determined that the auto-match size for any option class in ANTE is the disseminated quotation size. Because under Options Size Mitigation, all Amex quotations will be displayed, specialists will be able to fully comply with their regulatory obligations without additional changes or adjustments. Furthermore, the actual size of the disseminated quotation of another options exchange does not also impact a specialist's obligations under the Options Linkage due to the definition of FCQS, and therefore, specialists will be able to rely on the Amex displayed quotation without using a thirty-party market data vendor. Similarly, Firm Principal Quotation Size or "FPQS" will not be affected by Options Size Mitigation because FPQS is defined as the number of option contracts that a Participant Exchange guarantees it will execute at its disseminated quotation for incoming principal orders in an eligible option class.<sup>12</sup> As a result, since the Exchange will always display its quotes with size, specialists will be able to properly execute principal orders received through the Linkage.

---

<sup>12</sup> The definition of FPQS further provides a minimum size of 10 contracts, however if the Participant Exchange is disseminating a quotation size of less than 10 contracts, then the FPQS may equal such quotation size.

Linkage Plan Amendment No. 15 (Trade and Ship and Book and Ship)<sup>13</sup> and related Exchange rules<sup>14</sup> were also recently approved by the Commission providing that (i) an exchange may trade an order at a price that is one-tick inferior to the NBBO if a Linkage Order is transmitted to the NBBO market(s) to satisfy all interest at the NBBO price (this is the “trade and ship” concept); and (ii) an exchange may book an order that would lock another exchange if a Linkage Order is sent to such other exchange to satisfy all interest at the lock price (this is the “book and ship” concept). At a 10% filtering level for Options Size Mitigation, specialists would need to know the size of away market quotations in order to take full advantage of the “trade and ship” and “book and ship” concepts for orders greater than the 10% filter (i.e., increases or decreases). For smaller orders (those less than the 10% filter), Options Size Mitigation would have a limited effect, if any, so that specialists would be able to process orders in the normal fashion. When Options Size Mitigation is in effect, specialists to fully know and understand the depth of size of away markets would need to use a third-party market data vendor.

The Exchange submits that Options Size Mitigation will offer greater ability and flexibility to manage inbound quote traffic. Given the exponential increase in options quote traffic rates in recent years, the Exchange believes that Options Size Mitigation is a necessary tool in connection with the processing of quote traffic.

---

<sup>13</sup> See Securities Exchange Act Release No. 52413 (September 13, 2005), 70 FR 55185 (September 20, 2005) (Order Approving Amendment No. 15 to the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage Relating to a “Trade and Ship” Exception to the Definition of “Trade-Through” and a “Book and Ship” Exception to the Locked Markets Provision).

<sup>14</sup> See Securities Exchange Act Release No. 52414 (September 13, 2005), 70 FR 55186 (September 20, 2005) (SR-Amex-2005-046).

## 2. Statutory Basis

The proposed rule change is consistent with Section 6(b) of the Act<sup>15</sup> in general and furthers the objectives of Section 6(b)(5)<sup>16</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, remove impediments to and perfect the mechanisms 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 proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

No written comments were solicited or received with respect to 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 at <http://www.sec.gov/rules/sro.shtml>; or

---

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

<sup>16</sup> 15 U.S.C. 78f(b)(5).

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR-Amex-2005-115 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549–9303.

All submissions should refer to File No. SR-Amex-2005-115. 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 at <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 Room, 100 F Street, NE, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. 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 No. SR-Amex-2005-115 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

After careful consideration, the Commission finds that the proposed rule change is consistent with the requirements of the Section 6 of the Act<sup>17</sup> and the rules and regulations thereunder applicable to a national securities exchange.<sup>18</sup> In particular, the Commission believes that the proposed rule change is consistent with Section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange be 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 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.<sup>19</sup>

The Commission believes that the proposed rule change should enhance the Amex's ability to process an increasing volume of incoming options quotes during high option quote volume periods and peaks. The Commission also believes that the Options Size Mitigation program should help to limit potential data delays of incoming data without limiting the dissemination of Exchange participants' quotes and orders.

The Amex has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after publication of the notice thereof in

---

<sup>17</sup> 15 U.S.C. 78f.

<sup>18</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>19</sup> 15 U.S.C. 78f(b)(5).

the Federal Register. The Commission believes that granting accelerated approval of the proposal will allow the Amex to immediately implement the Options Size Mitigation program and thus, should facilitate the processing of an increasing volume of incoming options quotes and should avoid potential data transmission delays. Furthermore, the Commission notes that the current pilot program was approved on a temporary four-month basis to allow the Commission an opportunity to solicit comments on the proposed rule change and to evaluate the impact of the proposal on the options market. Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>20</sup> for approving the proposed rule change prior to the thirtieth day after publication of the notice thereof in the Federal Register.

---

<sup>20</sup> 15 U.S.C. 78s(b)(2).

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>21</sup> that the proposed rule change, as amended (SR-Amex-2005-115), is hereby approved on an accelerated basis for a four-month pilot period to expire on March 5, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>22</sup>

Jonathan G. Katz  
Secretary

---

<sup>21</sup> 15 U.S.C. 78s(b)(2).

<sup>22</sup> 17 CFR 200.30-3(a)(12).