

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60526; File No. SR-NYSEAmex-2009-19)

August 18, 2009

Self-Regulatory Organizations; NYSE Amex LLC; Order Granting Approval of a Proposed Rule Change as Modified by Amendment No. 1 Thereto to Adopt Rules Implementing the Options Order Protection and Locked/Crossed Market Plan

I. Introduction

On May 11, 2009, NYSE Amex LLC (“NYSE Amex” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend and adopt rules to implement the Options Order Protection and Locked/Crossed Market Plan. The proposed rule change was published for comment in the Federal Register on June 9, 2009.³ On July 12, 2009, the Exchange filed Amendment No. 1 to the proposed rule change.⁴ The Commission received no comments on the proposal. This order approves the proposed rule change, as modified by Amendment No. 1.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 60015 (June 1, 2009), 74 FR 27375 (“Notice”).

⁴ Amendment No. 1 clarified that this proposed rule change will become effective upon the Exchange’s withdrawal from the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage and the effectiveness of the Options Order Protection and Locked/Crossed Market Plan. In addition, Amendment No. 1 revised Proposed NYSE Amex Rule 992NY(b) to delete the last sentence which stated, in reference to the proposed locked/crossed market exception for non-customer quotes, that the “exemption is operative as long as the Exchange identifies the presence of Customer orders in its disseminated bid or offer” because the sentence was not included in similar rules of other exchanges. Because the amendment provided clarification and revised the Exchange’s proposed locked and crossed market rule in a non-substantive manner to conform with similar proposed rules of other exchanges, the amendment did not require notice and comment.

II. Description of the Proposal

The Exchange proposes to amend and adopt new NYSE Amex rules to implement the Options Order Protection and Locked/Crossed Market Plan (“Plan”).⁵ Specifically, the Exchange proposes to replace current NYSE Amex Rules 990NY through 993NY with new rules implementing the Plan, amend other Exchange rules to reflect the Plan, and delete rules rendered unnecessary by the Plan.

The Old Plan

Each of the Participating Options Exchanges are signatories to the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (“Old Plan”).⁶ In pertinent part, the Old Plan generally requires its participants to avoid trading at a price inferior to the national best bid or offer (“trade-through”), although it provides for a number of exceptions to trade-through liability.⁷ The Participating Options Exchanges comply with this requirement of the Old Plan by

⁵ The Plan is a national market system plan proposed by the seven existing options exchanges and approved by the Commission. See Securities Exchange Act Release No. 59647 (March 30, 2009), 74 FR 15010 (April 2, 2009) (File No. 4-546) (“Plan Notice”) and 60405 (July 30, 2009), 74 FR 39362 (August 6, 2009) (File No. 4-546) (“Plan Approval”). The seven options exchanges are: Chicago Board Options Exchange, Incorporated (“CBOE”); International Securities Exchange, LLC (“ISE”); The NASDAQ Stock Market LLC (“Nasdaq”); NASDAQ OMX BX, Inc. (“BOX”); NASDAQ OMX PHLX, Inc. (“Phlx”); NYSE Arca, Inc. (“NYSE Arca”); and NYSE Amex (each exchange individually a “Participant” and, together, the “Participating Options Exchanges”).

⁶ On July 28, 2000, the Commission approved the Old Plan as a national market system plan for the purpose of creating and operating an intermarket options market linkage proposed by the American Stock Exchange LLC (n/k/a NYSE Amex), CBOE, and ISE. See Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000). Subsequently, Philadelphia Stock Exchange, Inc. (n/k/a Phlx), Pacific Exchange, Inc. (n/k/a NYSE Arca), Boston Stock Exchange, Inc. (n/k/a BOX), and Nasdaq joined the Linkage Plan. See Securities Exchange Act Release Nos. 43573 (November 16, 2000), 65 FR 70851 (November 28, 2000); 43574 (November 16, 2000), 65 FR 70850 (November 28, 2000); 49198 (February 5, 2004), 69 FR 7029 (February 12, 2004); and 57545 (March 21, 2008), 73 FR 16394 (March 27, 2008).

⁷ Section 8(c) of the Old Plan.

utilizing a stand alone system (“Linkage Hub”) to send and receive specific order types,⁸ namely Principal Acting as Agent Orders (“P/A Orders”), Principal Orders, and Satisfaction Orders.⁹ The Old Plan also provided that dissemination of “locked” or “crossed” markets should be avoided, and remedial actions that should be taken to unlock or uncross such market.¹⁰ Each of the Participating Options Exchanges, including the Exchange, has submitted an amendment to the Old Plan to withdraw from such Plan.¹¹ The withdrawals will be effective upon approval by the Commission of such amendments pursuant to Rule 608 of Regulation NMS under the Act (“Regulation NMS”).¹²

The Plan

The Plan does not require a central linkage mechanism akin to the Old Plan’s Linkage Hub. Instead, the Plan includes the framework for routing orders via private linkages that exist for NMS stocks under Regulation NMS.¹³ The Plan requires the Participating Options

⁸ The Linkage Hub is a centralized data communications network that electronically links the Participating Options Exchanges to one another. The Options Clearing Corporation (“OCC”) operates the Linkage Hub.

⁹ Section 2(16) of the Old Plan.

¹⁰ Section 7(a)(i)(C) of the Old Plan.

¹¹ See Securities Exchange Act Release No. 60360 (July 21, 2009) 74 FR 37265 (July 28, 2009) (File No. 4-429).

¹² 17 CFR 242.608.

¹³ See Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (File No. S7-10-04); 17 CFR 242.600 et seq. For discussions of the similarities between the provisions of Regulation NMS and the provisions in the Plan, see Plan Notice and Plan Approval, supra note 5.

Exchanges to adopt rules “reasonably designed to prevent Trade-Throughs.”¹⁴ Participating Options Exchanges are also required to conduct surveillance of their respective markets on a regular basis to ascertain the effectiveness of the policies and procedures to prevent Trade-Throughs and to take prompt action to remedy deficiencies in such policies and procedures.¹⁵ As further described below, the Plan incorporates a number of exceptions to trade-through liability.¹⁶ Some of these exceptions are carried over from the Old Plan, including exceptions for trading rotations, non-firm quotes, and complex trades.¹⁷ Others are substantially similar to exceptions available for NMS stocks under Regulation NMS, such as exceptions for systems issues, crossed markets, quote flickering, customer stopped orders, benchmark trades and, notably, intermarket sweep orders (“ISOs”).¹⁸ In addition, the Plan contains a new exception for stopped orders and price improvement.¹⁹

The Plan also requires each Participant to establish, maintain, and enforce written rules that: require its members reasonably to avoid displaying locked and crossed markets; assure the reconciliation of locked and crossed markets; and prohibit its members from engaging in a

¹⁴ Under the Plan, a “Trade-Through” is generally defined as a transaction in an option series, either as principal or agent, at a price that is lower than a Protected Bid or higher than a Protected Offer.” See Section 2(21) of the Plan. A “Protected Bid” and “Protected Offer” generally means a bid or offer in an option series, respectively, that is displayed by a Participant, is disseminated pursuant to the Options Price Reporting Authority (“OPRA”) Plan, and is the Best Bid or Best Offer. See Section 2(17) of the Plan. A “Best Bid” or “Best Offer” means the highest bid price and the lowest offer price. Section (2)(1) of the Plan. “Protected Bid” and “Protected Offer,” together are referred to herein as “Protected Quotation.” See Section 2(18) of the Plan.

¹⁵ Section 5(a)(ii) of the Plan.

¹⁶ Section 5(b) of the Plan.

¹⁷ Subparagraphs (ii), (vii), and (viii), respectively, of Section 5(b) of the Plan.

¹⁸ Subparagraphs (i), (iii), (vi), (ix), (xi), and (iv)-(v), respectively, of Section 5(b) of the Plan.

¹⁹ Subparagraph (x) of Section 5(b) of the Plan.

pattern or practice of displaying locked and crossed markets; subject to exceptions as may be contained in the rules of the Participant, as approved by the Commission.²⁰

The Exchange's Proposal

To implement the Plan, the Exchange proposes to replace its current rules relating to the Old Plan with new rules relating to the Plan, and makes amendments to other rules as necessary to conform to the requirements of the Plan.²¹ As such, the Exchange proposes to adopt all applicable definitions from the Plan into the Exchange's rules.²²

In addition, the Exchange proposes to prohibit its members from effecting Trade-Throughs, unless an exception applies.²³ Consistent with the Plan, the Exchange also proposes exceptions to the prohibition on trade throughs relating to: system issues; trading rotations; crossed markets; intermarket sweep orders; quote flickering; non-firm quotes; complex trades; customer stopped orders; stopped orders and price improvement; and benchmark trades.²⁴

The Exchange also proposes a rule to address locked and crossed markets, as required by the Plan.²⁵ Specifically, the Exchange proposes that, except for quotations that fall within a

²⁰ Section 6 of the Plan. The Plan also contains provisions relating to the operation of the Plan including, for example, provisions relating to the entry of new parties to the Plan; withdrawal from the Plan; and amendments to the Plan.

²¹ A more detailed description of the Exchange's proposed rule change may be found in the Notice, supra, note 3.

²² Proposed NYSE Amex Rule 990NY.

²³ Proposed NYSE Amex Rule 991NY(a).

²⁴ Proposed NYSE Amex Rule 991NY(b)(1)-(10). In addition, the Exchange proposes to add ISOs as a new type of order under proposed NYSE Amex Rule 900.3NY(t).

²⁵ A "locked market" is defined as a quoted market in which a Protected Bid is equal to a Protected Offer. Proposed NYSE Amex Rule 990NY(9). A "crossed market" is defined as a quoted market in which a Protected Bid is higher than a Protected Offer. Proposed NYSE Amex Rule 990NY(5).

stated exception, members shall reasonably avoid displaying, and shall not engage in a pattern or practice of displaying, any quotations that lock or cross a Protected Quote.²⁶

The Exchange proposes four exceptions to the prohibition against locked and crossed markets: when the Exchange is experiencing a failure, material delay, or malfunction of its systems or equipment; when the locking or crossing quotation was displayed at a time where there is a crossed market; when an Exchange member simultaneously routes an ISO to execute against the full displayed size of any locked or crossed Protected Bid or Protected Offer; and, with respect to a locking quotation, when the order entered on the Exchange that will lock a Protected Bid or Protected Offer, is (i) not a customer order, and the Exchange can determine via identification available pursuant to the OPRA Plan that such Protected Bid or Protected Offer does not represent, in whole or in part, a customer order; or (ii) a customer order, and the Exchange can determine via identification available pursuant to the OPRA Plan that such Protected Bid or Protected Offer does not represent, in whole or in part, a customer order, and, on a case-by-case basis, the customer specifically authorizes the member to lock such Protected Bid or Protected Offer.²⁷ The Exchange believes that, in most cases, locked market maker quotes are good for the investing public, but recognizes that the benefits of a locked market become more complicated when one or both of the locking quotations represent a customer order. Where there is market interest willing to trade with a customer, the Exchange believes that the customer order should be filled. Thus, the Exchange proposes that it would not exempt from the locked market prohibition situations involving customer orders unless the customer entering the locking order specifically

²⁶ Proposed NYSE Amex Rule 992NY(a).

²⁷ Proposed NYSE Amex Rule 992NY(b)(1)-(4).

authorizes the lock on a case-by-case basis.²⁸ As a result, its members would not be permitted to lock another Participant's quotation unless the Exchange can establish that the quotation on the other Participant's market is not for the account of a customer.

The Exchange also proposes rules to permit it to continue to accept P/A Orders and Principal Orders from Participating Options Exchanges that are not able to send ISOs in order to avoid Trade-Throughs.²⁹ The Exchange noted that, even upon the approvals of the Plan and the implementing rules of the various Participating Options Exchanges, it is possible that not all the Participants will be functionally able to operate pursuant to the Plan. Thus, the Exchange has proposed to retain certain rules governing the receipt of P/A Orders and Principal Orders until such time that all Participating Options Exchanges are operating pursuant to the Plan.

The Exchange also proposes to delete certain provisions of NYSE Amex Rules to reflect the Exchange's withdrawal from the Old Plan.³⁰ Finally, the Exchange proposes to amend NYSE Amex 476A, the Exchange's Minor Rule Plan, to replace references to the Old Plan with references to the Plan.

²⁸ NYSE Amex noted that it can envision a customer authorizing a lock when the fees associating with trading against the locked market make the execution price uneconomical to the customer. See Notice, supra note 3 at 27378.

²⁹ Proposed NYSE Amex Temporary Rule 993NY.

³⁰ See Notice, supra note 3 at 27378, discussing proposed changes to NYSE Amex Rule 921NY, Commentaries .01 - .03 to NYSE Amex Rule 923NY, NYSE Amex Rule 964NY, and NYSE Amex Rule 476A.

II. Discussion and Commission's Findings

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.³¹ In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act³² which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The Commission also finds that the proposal is consistent with Rule 608(c) of Regulation NMS under the Act, which requires that each exchange comply with the terms of any effective national market system plan of which it is a participant.³³ Finally, the Commission finds that the proposed rule change is consistent with the requirements of the Plan.³⁴

Proposed NYSE Amex Rule 990NY would define applicable terms in a manner that are substantively identical to the defined terms of the Plan. As such, the Commission finds that proposed NYSE Amex 990NY are consistent with the Act and the Plan.

Proposed NYSE Amex Rule 991NY(a) would prohibit members from effecting Trade-Throughs unless an exception applies. Proposed NYSE Amex Rule 991NY(b) would provide for ten exceptions to the general Trade-Through prohibition, relating to systems issues, trading

³¹ 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).

³² 15 U.S.C. 78f(b)(5).

³³ 17 CFR 242.608(c). Section 1 of the Plan provides in pertinent part that, "The Participants will submit to the [Commission] for approval their respective rules that will implement the framework of the Plan."

³⁴ See supra note 5.

rotations, crossed markets, ISOs, quote flickering, non-firm quotes, complex trades, customer stopped orders, stopped orders and price improvement, and benchmark trades.³⁵ Aside from the proposed exception relating to systems issues, each proposed exception would be substantively identical to the parallel exception under Section 5(b) of the Plan.

The systems issues exception under proposed NYSE Amex Rule 991NY(b)(1) would implement the parallel exception available under Section 5(b)(i) of the Plan and would permit the Exchange to bypass the Protected Quotation of another Participant if such other Participant repeatedly fails to respond within one second to incoming orders attempting to access its Protected Quotations. The Exchange's rule would require the Exchange to notify such non-responding Participant immediately after (or at the same time as) electing self-help, and assess whether the cause of the problem lies with the Exchange's own systems and, if so, take immediate steps to resolve the problem. Finally, the Exchange would be required to promptly document its reasons supporting any such determination to bypass a Protected Quotation. The Commission believes that this exception should provide the Exchange with the necessary flexibility for dealing with problems that occur on an away market during the trading day. At the same time, the exception's requirements to immediately notify such away market of its determination and also assess its own system should help prevent the use of this exception when there in fact is a problem with the Exchange's own systems, rather than those of an away market.

The Commission notes that included among the exception in proposed NYSE Amex Rule 991NY(b) would be an exception for certain transactions involving ISOs.³⁶ An order identified as an ISO would be immediately executable by the Exchange (or any other Plan Participant that

³⁵ Proposed NYSE Amex Rule 991NY(b)(1)-(10).

³⁶ Proposed NYSE Amex Rule 991NY(b)(4).

received such an order) based on the premise that the market participant sending the ISO has already attempted to access all better-priced Protected Quotations up to their displayed size. The Commission believes that this exception should help ensure more efficient and faster executions in the options markets.

The Commission notes that, in addition to these rules regarding Trade-Throughs, the Plan requires that each Participant establish, maintain and enforce written policies and procedures that are reasonably designed to prevent Trade-Throughs in that Participant's market that do not fall within an applicable exception and, if relying on such exception, that are reasonably designed to assure compliance with the terms of the exception. In addition, the Commission notes that the Plan requires each Participant to conduct surveillance of its market on a regular basis to ascertain the effectiveness of such policies and procedures and to take prompt action to remedy any deficiencies in such policies and procedures.

Accordingly, the Commission finds that proposed NYSE Amex Rule 991NY is consistent with Section 5 of the Plan and Section 6(b)(5) of the Act³⁷ which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

Proposed NYSE Amex Rule 992NY(a) would require Exchange members to reasonably avoid displaying, and not engage in a pattern or practice of displaying, any quotation that locks or crosses a Protected Quotation, subject to certain exceptions delineated in proposed NYSE Amex Rule 992NY(b). The Commission recognizes that locked and crossed markets may occur accidentally and cannot always be avoided. However, the Commission believes that giving

³⁷ 15 U.S.C. 78f(b)(5).

priority to the first-displayed Protected Bid or Protected Offer, particularly when it includes a public customer's order, will encourage price discovery and contribute to fair and orderly markets. Therefore, the Commission believes that the proposed rule, which corresponds to the Plan's language, to require members to reasonably avoid displaying, and not engaging in a pattern or practice of, locks and crosses is appropriate.

Proposed NYSE Amex Rule 992NY(b) would permit four exceptions to the Exchange's general rule relating to locked and crossed markets.³⁸ The first three would be similar to analogous certain trade-through exceptions under proposed NYSE Amex Rule 991NY(b), and relate to when the Exchange is experiencing systems issues, when there is exists a crossed market, and when a member simultaneously routes ISOs against the full displayed size of any locked or crossed Protected Bid or Protected Offer.

The fourth exception would permit an order entered onto the Exchange to lock a Protected Bid or Protected Offer when such order is: (1) not a customer order, and the Exchange can determine that such Protected Bid or Protected Offer does not represent, in whole or in part, a customer order; or (2) a customer order, and the Exchange can determine that such Protected Bid or Protected Offer does not represent, in whole or in part, a customer order and, on a case-by-case basis, the customer specifically authorizes the Exchange's member to lock such Protected Bid or Protected Offer. This exception would not protect a market maker quote or broker-dealer order from being locked.

The Commission believes that the Exchange's proposed rules relating to locked and crossed markets are consistent with the Plan and the Act and should help ensure that the display of locked or crossed markets will be limited and that any such display will be promptly

³⁸ Section 6 of the Plan permits exceptions to the Plan's locked and crossed market rules as may be contained in the rules of a Participant approved by the Commission.

reconciled. The Commission also believes that each of the proposed exceptions to locked and crossed markets relate to circumstances when it is appropriate to permit a limited, narrow exception to the general locked and crossed market rule.

In particular, the Commission believes that the fourth exception is appropriate because it would protect customer orders that are Protected Bids or Protected Offers from being locked, and would only permit a customer order entered on to the Exchange to lock a Protected Bid or Protected Offer when a customer specifically authorizes an Exchange member, and only when such Protected Bid or Protected Offer itself does not represent, in whole or in part, a customer order. Because of the rapidity with which options quotes are often updated today, particularly in response to changes in the underlying, there is an increasing likelihood that market maker quotations will lock each other. The proposed exception accounts for this dynamic by not prohibiting such locking instances. Importantly, the proposed exception in the Exchange's rules that the Commission is approving would allow non-customer orders to lock an away market's Protected Quotation only if the Exchange is able to affirmatively determine that the Protected Quotation on the away market is not, in whole or in part, for the account of a customer. If any portion of such away market's Protected Quotation is for the account of a customer, such Protected Quotation may not be locked. In addition, the Commission notes that the rule requires that such determination be made via identification available pursuant to the OPRA Plan, which is working with the participating options exchanges on a method to so identify customer quotations through OPRA. The Exchange has represented that, absent the ability to identify a customer quote as part of an exchange's BBO, the Exchange would assume that the quote represents, in whole or in part, a customer order. As such, the Exchange has represented that it would not permit its members to avail themselves of this exemption unless the away market has informed

the Exchange that it would designate all customer orders as such in OPRA and such exchange's quotation does not contain such designation. Finally, the Exchange has represented that if an exchange chooses not to identify its customer quotations, the Exchange would treat all of such exchange's quotations as customer orders and, absent application of another exception, would not permit locks of such quotations.

Therefore, the Commission finds that Exchange's rule regarding locked and crossed markets appropriately implements Section 6 of the Plan, and is consistent with Section 6(b)(5) of the Act³⁹ which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission also finds that proposed NYSE Amex Temporary Rule 993NY, which facilitates the participation of certain Participating Options Exchanges who may require the use of P/A Orders and Principal Orders after implementation of the Plan, is consistent with the Act. Although the Commission has already approved the Plan,⁴⁰ the Commission also recognizes that there may be one or more Participating Options Exchanges that may require a temporary transition period during which they may want to continue to utilize these order types that exist currently under the Old Plan.⁴¹ The Exchange and each of the other Participating Options Exchanges have proposed substantially identical temporary provisions to accommodate this

³⁹ 15 U.S.C. 78f(b)(5).

⁴⁰ See Plan Approval, supra, note 5.

⁴¹ The Commission notes that any Participating Options Exchange that wishes to utilize such order types in a manner that would result in a Trade-Through would need to separately request an exemption from the Plan for such use.

possibility.⁴² Thus, the Commission finds that the proposed rule relating to the Exchange's receipt and handling of P/A Orders and Principal Orders, and imposing certain obligations on the Exchange with respect to such orders that are similar to those that exist under the Old Plan, is appropriate and consistent with Section 6(b)(5) of the Act⁴³ which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

Finally, the Commission finds that NYSE Amex's other proposed changes, including the proposed modifications to NYSE Amex Rule 921NY, Commentaries .01 - .03 to NYSE Amex Rule 923NY, NYSE Amex Rule 964NY, and NYSE Amex Rule 476A are appropriate and consistent with the Act.

⁴² The Commission notes that the rules contained in NYSE Amex Temporary Rule 993NY are not required by the Plan, but rather are rules proposed by the Exchange in order to facilitate the participation in the Plan of certain exchanges during an initial transition period.

⁴³ 15 U.S.C. 78f(b)(5).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁴⁴ that the proposed rule change (SR-NYSEAmex-2009-19), as modified by Amendment No. 1, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁵

Florence E. Harmon
Deputy Secretary

⁴⁴ 15 U.S.C. 78s(b)(2).

⁴⁵ 17 CFR 200.30-3(a)(12).