

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-56804; File No. SR-Amex-2006-107)  
November 16, 2007

Self-Regulatory Organizations; American Stock Exchange LLC; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, to Eliminate Options Specialists' Agency Responsibilities and Establish Amex Book Clerks

I. Introduction

On November 14, 2006, 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" or "Exchange Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposal to eliminate the agency obligations of Exchange options specialists and establish Amex book clerks ("ABCs"). The Exchange filed Amendment No. 1 to the proposed rule change on March 29, 2007. The proposal as amended was published for comment in the Federal Register on April 13, 2007.<sup>3</sup> The Commission received no comments on the proposal. This order approves the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal

The Exchange has proposed to eliminate the obligation and ability of an Exchange options specialist to act as an agent in connection with orders in his or her assigned options classes. This proposal would permit the Exchange to designate Exchange employees or independent contractors to serve as ABCs, responsible for maintaining and operating the ANTE Central Book (i.e., the specialist's customer limit order book) and the ANTE Display Book.<sup>4</sup>

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

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

<sup>3</sup> See Securities Exchange Act Release No. 55583 (April 5, 2007), 72 FR 18695 ("Notice").

<sup>4</sup> The Exchange submits that all incoming customer orders are represented in the ANTE Central Book, and if marketable, will be automatically executed subject to a number of limited exceptions. Orders that are otherwise eligible for automatic execution may not

The Exchange also seeks to amend certain Exchange rules relating to the operation of the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (“Linkage Plan”) to accommodate the implementation of pertinent ABC rules and other proposed rule changes described herein.<sup>5</sup> Finally, the proposed rule change would implement several other amendments to conform other Exchange rules to the proposal. The Exchange has noted that its proposal substantially mirrors changes recently adopted by the Chicago Board Options Exchange to eliminate DPM agency responsibilities and establish PAR Officials.<sup>6</sup> The following description summarizes certain significant effects this proposed rule change would have on existing Exchange rules.<sup>7</sup>

Under the current rules of the Exchange, options specialists are required to execute options orders on an agency basis for those classes of options assigned to them.<sup>8</sup> Accordingly, all options specialists on the Amex presently act as both agent and principal for orders in their respective assigned options classes.

The Exchange has now determined that it is in the best interest of the Exchange, its members, and investors to eliminate the agency obligation of options specialists. The Exchange

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receive an automatic execution: (i) whenever the Amex Best Bid or Offer (ABBO) crosses the National Best Bid or Offer (NBBO) and causes an inversion in the quote; or (ii) whenever a better bid or offer is being disseminated by another options exchange and the order is not eligible for automatic price matching. In addition, if quotes are deemed unreliable or the Exchange is experiencing communications or systems problems, non-firm markets or delays in the dissemination of quotes by the Options Price Reporting Authority, orders will not be automatically executed. In these limited cases, incoming customer orders will be routed to the ANTE Display Book for manual handling.

<sup>5</sup> Exchange rules governing the operation of the Linkage Plan are set forth under Amex Rules 940 through 945 and Amex Rule 941–ANTE.

<sup>6</sup> See Securities Exchange Act Release No. 52798 (November 18, 2005), 70 FR 71344 (November 28, 2005) (SR-CBOE-2005-46).

<sup>7</sup> For a complete description of the proposed rule change, see the Notice, supra note 3.

<sup>8</sup> See Amex Rule 950–ANTE(1), incorporating Amex Rule 170 to options transactions.

has proposed to amend its rules to remove an options specialist's obligation to act as an agent in its allocated securities on the Exchange.<sup>9</sup> The Exchange has further proposed to designate ABCs who would be responsible for handling certain orders in the same manner as they are currently handled by the options specialists.<sup>10</sup> The ABCs will maintain and operate the customer limit order book,<sup>11</sup> effect proper executions of orders that are routed to the customer limit order book,<sup>12</sup> display eligible limit orders,<sup>13</sup> undertake the obligations related to handling certain Linkage orders,<sup>14</sup> and act as agent for orders that, for various reasons, cannot be automatically executed and so are routed to the ANTE Display Book for manual handling.<sup>15</sup>

The Exchange has proposed to amend its rules to provide that the Exchange, via the ABCs, and not the options specialists, would be responsible for handling Linkage orders. Under the proposal, ABCs would: (i) use an options specialist's account to route Principal Acting as Agent ("P/A") Orders and Satisfaction Orders to away markets based on prior instructions that must be provided by the options specialist to the ABC,<sup>16</sup> and (ii) handle all Linkage orders or portions of Linkage orders received by the Exchange that are not automatically executed.<sup>17</sup> The

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<sup>9</sup> See Proposed Amex Rules 950-ANTE(f) cmt. .01 and 950-ANTE(l) cmt. .01.

<sup>10</sup> See Proposed Amex Rule 995-ANTE.

<sup>11</sup> See Proposed Amex Rule 995-ANTE(a)(i).

<sup>12</sup> See Proposed Amex Rule 995-ANTE(a)(ii). The requirement that options specialists effect proper executions would require an options specialist to use due diligence to execute customer orders at the best prices available under the rules of the Exchange. See Proposed Amex Rule 995-ANTE(b)(ii).

<sup>13</sup> See Proposed Amex Rule 995-ANTE(b)(i).

<sup>14</sup> See Proposed Amex Rule 995-ANTE(e).

<sup>15</sup> See Proposed Amex Rule 995-ANTE(b)(iv); see also supra note 4.

<sup>16</sup> See Proposed Amex Rule 950-ANTE(l) cmt. .05.

<sup>17</sup> See Proposed Amex Rule 995-ANTE(e).

ABC also would use the specialist's account to fill incoming Satisfaction Orders that result from a Trade Through<sup>18</sup> that the Exchange effects.<sup>19</sup>

The Exchange has proposed measures designed to ensure the independence of ABCs from Exchange members. An ABC would be required to be an Exchange employee or independent contractor, and his or her compensation would be determined and paid solely by the Exchange. In addition, the ABC would be prohibited from having an affiliation with any member that is approved to act as a specialist, registered options trader ("ROT"), remote registered options trader ("RROT") or supplemental registered options trader ("SROT") on the Exchange.

Because the options specialists would no longer be operating the customer limit order book, the Exchange proposes to amend Rule 958A-ANTE, which defines when an options specialist's firm quote obligation attaches. Amex Rule 958A-ANTE currently provides that, in the case of an order received by the options specialist, the options specialist's firm quote obligation attaches at the time the order is received by such specialist, regardless of whether the options specialist is actually aware of the order at that time. This rule would be modified to provide that the firm quote obligation would attach, when an options specialist is the responsible broker or dealer, at the same time those obligations attach with respect to each other responsible broker or dealer—that is, when the order is announced to the trading crowd either via electronic display or by the ABC. The Exchange has proposed this clarification in light of the fact that options specialists will no longer represent orders on the customer limit order book in an agency capacity from the moment such orders are received on the book.

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<sup>18</sup> See Amex Rule 940(b)(19).

<sup>19</sup> See Proposed Amex Rule 950-ANTE(1) cmt. .05.

Finally, to ensure a smooth and orderly transition of the responsibility for operating the customer limit order book and executing agency orders from options specialists to ABCs, the Exchange proposes to implement this rule change to all applicable trading posts over a 180-day period from the effective date of this rule change. During this 180-day transition period, any options specialist who continues to operate the customer limit order book would continue to be subject to the same agency obligations as currently provided under Amex Rules 950–ANTE(1) and 958A–ANTE(e), except that, upon the approval of this proposal, these obligations instead would be reflected in a Regulatory Circular.

### III. Discussion

After careful consideration, 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.<sup>20</sup> In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>21</sup> 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 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.

With this proposal, Amex seeks to eliminate potential conflicts of interest that may currently arise for its options specialists in the handling of customer orders. Currently, Amex options specialists trade for their own accounts in order to assist in the maintenance of a fair and orderly market on the Exchange, and also act as agents for certain orders in their allocated

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<sup>20</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>21</sup> 15 U.S.C. 78f(b)(5).

options. Amex has proposed to eliminate an options specialist's obligation and permission to act as agent for customer orders in his or her allocated securities.<sup>22</sup>

Instead, Amex has proposed that orders that currently are represented by options specialists as agent be handled by Exchange employees known as Amex Book Clerks, or ABCs. ABCs would be independent from options specialists, as Amex has proposed to prohibit affiliations between ABCs and specialists, ROTs, RROTs, and SROTs in order to ensure the ABCs are independent from Exchange members' interests. Further, the compensation of ABCs would be determined and paid exclusively by the Exchange. The Commission believes that the Amex's proposal adequately assures the independence of the ABC in a manner designed to mitigate potential conflicts of interest with the options specialist. Further, the Commission believes that eliminating an options specialist's obligation to act as agent for certain orders in its assigned classes will promote just and equitable principles of trade and protect investors and the public interest, because it will greatly reduce any potential conflicts of interest that may have previously arisen when a specialist traded for its own account while acting as agent for certain customer orders.<sup>23</sup>

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<sup>22</sup> The Commission notes that Amex Rule 950–ANTE, as amended, will no longer permit an options specialist to act as an agent for customer orders. However, to the extent that an options specialist nevertheless undertakes to represent a customer's order in violation of Amex Rule 950–ANTE, the options specialist will assume all the duties and liabilities of an agent to a principal during the course of such representation.

<sup>23</sup> In addition, the Commission notes that Amex Rule 193, Affiliated Persons of Specialists, will have the effect of mitigating conflicts of interest that might arise when an affiliate of the options specialist acts as agent for a customer order in one of the specialist's assigned options classes. Amex Rule 193 provides that any approved person or member organization which is affiliated with a specialist must either: (a) be subject to Amex Rule 170(e), which provides that “[n]o member . . . , officer, employee, or approved person who is affiliated with a specialist or specialist member organization, shall, during the period of such affiliation, purchase or sell any security in which such specialist is registered for any account in which such person or party has a direct or indirect interest”; or (b) “establish[] and obtain[] Exchange approval of procedures restricting the flow of material, non-public corporate or market information between itself and the specialist

Pursuant to the proposed rule change, ABCs will undertake responsibilities comparable to those currently held by options specialists with respect to customer orders. For example, an ABC must use due diligence to execute the orders placed in his or her custody at the best prices available to him or her under Exchange rules. In addition, ABCs will assume the obligations related to displaying public customer orders that improve Amex's disseminated quote by maintaining the ANTE Central Book, the Exchange's automated limit order display facility, and keeping it active. Accordingly, the Commission believes that the Exchange's proposal should ensure that customers' orders continue to be represented and handled in a timely fashion on the Exchange. The Commission therefore believes that the proposal will continue to protect customer orders while preventing fraudulent and manipulative acts and practices.

The ABCs also would assume responsibilities related to Linkage orders. An ABC would use an options specialist's account to route P/A Orders and Satisfaction Orders to other participants in the Linkage Plan based on prior written instructions provided by the options specialist to the ABC.<sup>24</sup> The written instructions provided by the options specialist will also include direction as to how the ABC should handle responses to Linkage orders routed to other

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member organization, and any member, officer, or employee associated therewith." The Exchange represented that Rule 193 will have the effect of restricting the sharing of material, nonpublic information between the options specialist and any affiliate of the options specialist who acts as agent for a customer order. Telephone conversation between Jeffrey P. Burns, Vice President and Associate General Counsel, Amex, and Nathan Saunders, Special Counsel, Division, Commission, on November 14, 2007.

<sup>24</sup> The Commission today is also granting the Exchange a conditional exemption from the requirement in Rule 608(c) of Regulation NMS promulgated under the Act that the Exchange comply with and enforce compliance by its members with certain provisions of the Linkage Plan to facilitate the establishment of ABCs and their handling of Linkage Orders. See Letter from Elizabeth K. King, Associate Director, Division of Trading and Markets, Commission, to Jeffrey P. Burns, Vice President and Associate General Counsel, Amex, dated November 16, 2007.

Linkage Participants that are not responded to in a timely manner.<sup>25</sup> The ABC will also use the options specialist's account to fill any Satisfaction Order that results from a Trade Through that is effected on the Exchange by ABCs. Finally, the ABC will handle all Linkage orders or portions of Linkage orders received by the Exchange that are not automatically executed.

The Commission believes that the proposed rules governing the handling of Linkage orders by the ABC and the use of the options specialist's accounts for routing Linkage orders is consistent with the promotion of a national market system because, among other things, it will allow P/A Orders that reflect the terms of Amex customer orders to be generated by Amex and routed to other Linkage Participant markets, which will allow a Amex customer order to receive possible execution at a price better than the price disseminated by Amex.

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<sup>25</sup> Amex Rule 942(d)(3) specifically addresses the situations in which an Amex member (or, as proposed to be amended, an ABC acting as employee the Exchange) does not receive a response to a Linkage order within 20 seconds of sending the order.



IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>26</sup> that the proposed rule change (File No. SR-Amex-2006-107), 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.<sup>27</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>26</sup> 15 U.S.C. 78s(b)(2).

<sup>27</sup> 17 CFR 200.30-3(a)(12).