**American Stock Exchange's Summary of Intended Testimony
at the April 21, 2004 Hearings on
Proposed Regulation NMS**

I. Introduction

The American Stock Exchange ("Amex") applauds the Commission's goal of exploring ways to modernize the national market system so that U.S. markets retain their position as the deepest, most liquid and well regulated in the world.

II. Trade-Through Proposal

Amex supports the Commission's proposed extension of the trade-through rule to all national market system stocks regardless of where they trade. The trade-through rule is the heart of the national market system and a critical investor protection mechanism. The rule guarantees that investors—large and small—receive the best price for their orders regardless of the market where those orders are sent. The rule also encourages competitive price discovery by ensuring that investors that post the best-priced limit orders do not have their orders ignored. However, we have serious concerns about the Commission's proposed expansion of instances where investors who provide liquidity by establishing the national best price can have their orders ignored because the order resides on a market that is "inconvenient" for another trader. We are equally concerned that a broker could induce an investor to "opt out," hurting not only his own customer but also the investor who established the best price.

Specifically, we oppose allowing investors the ability to "opt-out" of the best-price provisions of the trade-through rule. As the Commission concedes in its proposing release "[t]he price at which an order can be executed is of paramount importance for most investors…."[1] However, under the current proposal, traders wanting to sacrifice the best price for idiosyncratic reasons, such as speed and certainty of execution, could. But those trades would occur at the expense of other investors, who without their consent, have had their orders involuntarily opted out. Thus, in effect, the proposed opt-out provision allows the interests of traders who prefer speed and certainty to trump the interests of investors who expect to receive the best price. We further question permitting agents the ability to execute trades on behalf of their customers at prices up to five cents away from the best price for what may amount to nothing more than the agents' own convenience or economic interests.

In our view, both these proposed changes do not modernize but threaten the heart of the national market system by effectively undermining the concept that investors must receive the best price and that their representatives owe them a fiduciary duty to find it.

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[1] Securities and Exchange Act Release No. 34-49325 (Feb. 27, 2004); 69 Fed. Reg. at 11153 (Mar. 9, 2004).

III. Market Access Proposal

Amex agrees with the Commission that fair access to the best prices available across competing market centers is essential to achieve an efficient, transparent national market system where markets vigorously compete and, as a result, investors' orders have the opportunity to interact directly and receive the best execution. Essential to that competition is the ability for one market to see and have fair and efficient access to another market's best bids and offers. Hidden markets with hidden prices or undisclosed fees undermine fair competition and access. And, we agree with the Commission that even when quoted prices are not hidden published quotes do not necessarily reflect the true price available to investors because of access fees charged by ECNs. This undermines the goals of the national market system.

However, we question whether the Commission's proposed solution of fixing maximum rates for access to quotes moves us any closer to true fair access across markets. Instead, we believe that the proposal not only places the Commission in the role of a rate maker, but also fails to acknowledge that there are different levels of service and responsibilities (regulatory and otherwise) provided across market centers for which investors are willing to pay.

For example, at an auction market like the Amex, our specialists play three important roles: auctioneers, brokers, and dealers. As auctioneers, specialists bring buyers and sellers together in one place and help them trade directly with one another. As brokers, specialists hold limit orders on behalf of customers and execute those orders if and when the market reaches the limit price specified in those orders. But it is the role that specialists play as dealers (buying and selling for their own accounts), which enhances liquidity and stability to the marketplace and sets auction markets apart from other competing market structures. As dealers, specialists have affirmative obligations to buy, using their own capital, when there are not enough sellers, which moderates trade-by-trade price movements. In short, specialists reduce daily stock-price volatility, provide liquidity, manage market imbalances, and establish fair market prices on openings and closings. To allow other market centers to access the Amex's quotes at prices set by the Commission—and not the marketplace itself—without commensurate obligations to provide liquidity, stabilize the market, and provide regulatory services is unfair.

Finally, we oppose merely lowering the fair access standard of Regulation ATS from 20 to 5 percent of trading volume. Instead, we believe that the first step in true fair access is to mandate fair access by all ATSs regardless of the percentage of their trading volume.

IV. Sub-penny Quoting Proposal

Amex believes that the Commission's proposal that would prohibit market participants from accepting or quoting in sub-pennies (other than for national market system stocks with share prices below $1.00) does not go far enough. We believe that sub-pennies should be banned not only for quoting but also for trading in all national market system securities. In addition, we believe that the Commission, at a minimum, should take this opportunity to reassess whether one-size-fits-all with respect to minimum tick size.

Professor William Christie who, along with Professor Paul Schultz, in 1994 suggested that Nasdaq market makers were maintaining artificially wide spreads, is now suggesting re-evaluating the penny tick size.[2] He contends, and we believe, that a penny creates such a small pricing increment that it destroys the critical roles played by price priority and limit orders. A penny tick size, like sub-penny quoting, encourages gaming whereby economically meaningless price improvement is used to step in front of existing limit orders. Professor Christie has suggested considering a minimum tick size of $0.05.[3] We agree.

V. Market Data Proposal

Amex commends the Commission on its market data proposal. We believe that the proposal generally moves in the right direction with the notable exception of the changes being proposed for the consolidated display requirement. In our view, maintaining the consolidated display model is the best alternative for investors and other market data users.

We have a number of issues with the proposed formula for distributing market data revenues among the market centers, which we will address in our comment letter. However, conceptually Amex believes that the proposed change in the distribution methodology will encourage participants to provide more liquidity and maintain the best possible markets.

We also generally support the creation of advisory committees to participate, but not vote, in network operating committee meetings. Such an approach will formalize a voice for users who have informally provided advice and counsel in the past. However, we do believe a risk exists that differing agendas of the advisory committee participants could limit the effectiveness of these new committees.

Finally, we are concerned that the changes that the Commission has proposed to Rules 11Aa3-1 and 11Ac1-2. We do not believe that changes to the consolidated display requirement will add more visibility to individual market centers. On the contrary, we believe that the proposed changes will fractionalize and potentially distort market data. As a result, we believe that these proposed changes would lead to investor confusion and further complicate the management of market data for vendors and broker-dealers.

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[2] William G. Christie, *A Minimum Increment Solution*, TRADERS, Nov. 2003, at 40.

[3] *Id.*