without the need to apply for or receive additional Commission approval.

The direct or indirect newly created nonutility holding company subsidiaries referred to above might be corporations, partnerships, limited liability companies or other entities in which PHI, directly or indirectly, will have a 100 percent voting equity interest. These subsidiaries would engage only in businesses to the extent PHI is authorized to engage in those businesses by statute, rule, regulation or order. Applicants state that reorganizations will not result in PHI entering into any new, unauthorized line of business.

VI. Energy Related Activities

Applicants request authority for PHI existing and future nonutility subsidiaries to engage in certain ''energy-related'' activities outside the United States. These activities may include:

(i) The brokering and marketing of electricity, natural gas and other energy commodities (''Energy Marketing'');

(ii) Energy management services (''Energy Management Services''), including the marketing, sale, installation, operation, and maintenance of various products and services related to energy management and demand-side management, including energy and efficiency audits; facility design and process control and enhancements; construction, installation, testing, sales, and maintenance of (and training client personnel to operate) energy conservation equipment; design, implementation, monitoring, and evaluation of energy conservation programs; development and review of architectural, structural, and engineering drawings for energy efficiencies, design and specification of energy consuming equipment; general advice on programs; the design, construction, installation, testing, sales and maintenance of new and retrofit heating, ventilating, and air conditioning; electrical and power systems; alarm and warning systems; motors, pumps, lighting, water, water-purification and plumbing systems, and related structures, in connection with energy-related needs; and the provision of services and products designed to prevent, control, or mitigate adverse effects of power disturbances on a customer's electrical systems; and

(iii) Engineering, consulting, and other technical support services (''Consulting Services'') with respect to energy-related businesses, as well as for individuals. Consulting Services would include technology assessments, power factor correction, and harmonics mitigation analysis; meter reading and repair; rate schedule design and analysis; environmental, engineering, risk management, and billing services (including consolidation billing and bill disaggregation tools); communications and information systems/data processing; system and strategic planning; finance; feasibility studies; and other similar services.

Applicants request that the Commission (i) authorize nonutility subsidiaries to engage in Energy Marketing activities in Canada and reserve jurisdiction over Energy Marketing activities outside of Canada pending completion of the record in this proceeding; (ii) authorize nonutility subsidiaries to provide Energy Management Services and Consulting Services anywhere outside the United States and (iii) reserve jurisdiction over other activities of nonutility subsidiaries outside the United States, pending completion of the record.

Applicants note that the Commission has previously granted or reserved jurisdiction over Conectiv Nonutilities' provision of the type of services described above through its Rule 58 Subsidiaries.[6] Applicants request that this authorization and reservation of jurisdiction be extended to the Pepco Nonutilities as well.

VII. Tax Allocation Agreement

Applicants propose to enter into an agreement for the allocation of consolidated tax among the companies within the PHI system (''Tax Allocation Agreement''). The Tax Allocation Agreement provides for the retention by PHI of payments for tax losses that it will incur in connection with financing or refinancing approximately $700 million of the cash consideration to be paid in the Transaction, rather than the allocation of these losses to its subsidiaries without payment as would otherwise be required by rule 45(c)(5).

VIII. Retention of Nonutility Subsidiaries and Additional Gas System

Applicants request that PHI be authorized to retain the Pepco Nonutilities, specifically listed in Appendix A to this notice.[7] Additionally, Applicants request that PHI be authorized to retain the Conectiv Gas System, which was found retainable in the Conectiv Merger Order.

[6] *See* HCAR No. 27464 (November 8, 2001).

[7] The Commission found the Conectiv Nonutilities to be retainable in the Conectiv Merger Order.

For the Commission by the Division of Investment Management, pursuant to delegated authority.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–7769 Filed 3–29–02; 8:45 am]

BILLING CODE 8010–01–U

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC–25500; File No. 812–12630]

Northbrook Life Insurance Company, et al.; Notice of Application

March 26, 2002.

AGENCY: Securities and Exchange Commission (''SEC'' or ''Commission'').

ACTION: Notice of application for an amended order pursuant to section 11(a) of the Investment Company Act of 1940, as amended (the ''Act'') approving the proposed offer of a new Longevity Reward Rider (''new LRR''), as set forth below.

Applicants: Northbrook Life Insurance Company (''Northbrook''), Northbrook Variable Annuity Account II (''Account II''), Allstate Life Insurance Company of New York (''Allstate New York''), Allstate Life of New York Variable Annuity Account II (''ALNY Account II'') and Morgan Stanley DW Inc. (formerly known as Dean Witter Reynolds Inc.) (''Morgan Stanley'') (collectively, the ''Applicants'').

Summary of Application: Applicants seek an order to amend an Existing Order (described below) approving the offer by the Applicants of the new LRR upon the terms and subject to the conditions described herein and in the Prior Application (described below).

Filing Date: The application was filed on September 4, 2001, amended on January 23, 2002, and amended and restated on March 19, 2002.

Hearing or Notification of Hearing: An order granting the application will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Secretary of the Commission and serving Applicants with a copy of the request, personally or by mail. Hearing requests must be received by the Commission by 5:30 p.m. on April 22, 2002, and should be accompanied by proof of service on Applicants in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the requester's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Secretary of the Commission.

ADDRESSES: Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549–0609. Applicants, Charles Smith, Esq., Assistant Counsel, Allstate Life Insurance Company, 3100 Sanders Road, Northbrook, Illinois 60062; with a copy to Richard T. Choi, Esq., Foley & Lardner, 3000 K Street, NW, Suite 500, Washington, DC 20007.

FOR FURTHER INFORMATION CONTACT: Alison Toledo, Senior Counsel, or Lorna MacLeod, Branch Chief, Office of Insurance Products, Division of Investment Management, at (202) 942–0670.

SUPPLEMENTARY INFORMATION: The following is a summary of the application. The complete application is available for a fee from the Public Reference Branch of the Commission, 450 Fifth Street, NW, Washington, DC 20549–0102, (202) 942–8090.

Applicant's Representations

1. Northbrook is a wholly-owned subsidiary of Allstate Life Insurance Company (''Allstate Life''). Allstate Life is an indirect subsidiary of The Allstate Corporation, a publicly-traded insurance holding company. Northbrook is Account II's depositor within the meaning of the Act.

2. Morgan Stanley is a wholly-owned subsidiary of Morgan Stanley Dean Witter & Co., a publicly-traded financial services company. Morgan Stanley is the principal underwriter of Account II. Morgan Stanley is registered as a broker-dealer under the Securities Exchange Act of 1934 (File No. 8–14172).

3. Account II is registered under the Act as a unit investment trust (File No. 811–6116). Account II funds the Morgan Stanley Dean Witter Variable Annuity II Contracts (the ''VA II Contracts'') that Northbrook and Morgan Stanley have offered and sold for a number of years.

4. The VA II Contracts, which are registered under the Securities Act of 1933 (File No. 033–35412), are deferred annuity contracts under which Contract owners may make one or more purchase payments over a period of time (called the ''accumulation phase''). During the accumulation phase, the Contract owner's purchase payments, after deduction of certain charges, earn (at the owner's election) a ''variable'' return based on the investment performance of one or more of Account II's subaccounts and/or a fixed rate of return that Northbrook declares from time to time.

5. At the end of the accumulation phase, the Contract owner elects whether to receive a ''lump sum'' payment of the VA II Contract's accumulated value, or to receive that value under one of several payment options. Payment options are available on a variable and/or fixed basis. The VA II Contracts incorporate many other features, including ''death benefit'' options, partial withdrawal rights, full surrender rights, transfer privileges and other optional rider benefits.

6. The VA II Contracts currently impose a withdrawal charge of up to 6% of any amount by which purchase payments withdrawn in any year exceed 15% of the cumulative purchase payments that had been made as of the beginning of that year (the ''annual free withdrawal amount''). The withdrawal charge associated with each purchase payment declines 1% each year until it is 0% beginning in the seventh year after the payment was made. Unused portions of the annual free withdrawal amount do not carry over to future years.

7. The VA II Contracts also impose an annual Contract maintenance charge of $ 30, a $ 25 charge applicable to certain transfers in excess of twelve during a one-year period (which is currently being waived), a daily administrative charge at an annual rate of 0.10% of the Contract's value in Account II, a mortality and expense risk charge at an annual rate of 1.25% of the Contract's value in Account II (or higher if certain optional rider benefits are selected), and a charge corresponding to any applicable state premium taxes.

8. Allstate New York is a stock life insurance company organized in New York in 1967. Like Northbrook, Allstate New York is a wholly-owned subsidiary of Allstate Life.

9. ALNY Account II funds the Allstate New York Variable Annuity II Contracts (''ALNY Contracts''). The ALNY Contracts are substantially similar to the VA II Contracts (together with the ALNY Contracts, the ''Contracts'') covered by the Existing Order, and have the same withdrawal charge schedule, base mortality and expense charge, contract maintenance charge, and administrative expense charge. However, due to limitations imposed by the New York Insurance Department, the ALNY Contracts do not offer the following income and death benefit riders that are offered by the VA II Contracts: Death Benefit Combination Option, Income Benefit Combination Option 2, Income and Death Benefit Combination Option 2 and Enhanced Earnings Death Benefit Option. Other than the optional riders, there are no material differences between the ALNY Contracts and the VA II Contracts.

10. By order dated June 8, 2000 (the ''Existing Order''),[1] the Commission approved, pursuant to Section 11 of the Act, the offer by Northbrook, Account II, and Morgan Stanley of a Longevity Reward Rider to owners of certain variable products as described in the application for the Existing Order (''Prior Application'').[2] Applicants are seeking to amend the Existing Order to approve the offer by Applicants of the new LRR. The new LLR is identical to the LRR currently offered through the VA II Contracts (''existing LRR''), with the modifications described below. Both the ALNY Contracts and the VA II Contracts are distributed exclusively by Morgan Stanley.

11. The existing LRR provides the following benefits: (a) An option whereby a deceased owner's surviving spouse may continue the Contract using the then-current death benefit value as the new Contract value, if higher, rather than the current Contract value; (b) a reduced mortality and expense risk charge (*i.e.,* at an annual rate that is .07% less than the rate that otherwise would apply); (c) a permanent waiver of the $30 annual Contract maintenance charge if the Contract's value exceeds $40,000 at any time; and (d) a reduction in the withdrawal charge that will apply to the withdrawal of any purchase payments that are made after the existing LRR is added to the Contract.

12. Contract owners who elect the existing LRR have a new three-year withdrawal charge schedule that applies to withdrawals made after the rider's issue date (the ''Rider Date''). The new schedule applies to any amount of such a subsequent withdrawal of purchase payments that exceeds the 15% annual free withdrawal amount, regardless of whether such withdrawn purchase payments were made before or after the Rider Date.

13. The withdrawal charge under the new withdrawal charge schedule begins at 3% and declines by 1% per year over three years to 0% by the end of the third year. For purchase payments made prior to the Rider Date, the three-year period runs from the Rider Date. For any purchase payment made subsequent to the Rider Date, the three-year period runs from the date of that payment.

14. The same exceptions to imposing the existing LRR withdrawal charge apply as apply to the Contract's basic withdrawal charge. Specifically, no existing LRR withdrawal charge is

[1] *Northbrook Life Insurance Company,* Investment Company Act Release No. 24493 (June 8, 2000) (File No. 812–12092).

[2] *Northbrook Life Insurance Company,* Investment Company Act Release No. 24456 (May 16, 2000) (File No. 812–12092).

imposed at the time a payment option commences, upon the death of a Contract owner or annuitant, upon amounts withdrawn to satisfy any applicable minimum distribution requirements under the Internal Revenue Code, or upon amounts withdrawn that are within the 15% annual free withdrawal amount. These are the same exceptions as would apply to the Contracts without the existing LRR.

15. Contract owners are not permitted to elect for the existing LRR to apply to part of a contract and not to the rest. Any election of the existing LRR must apply to the whole contract.

16. The new LRR is identical to the existing LRR, except that the new LRR will be available to an expanded class of eligible Contract owners. The existing LRR is available only to Contract owners whose entire Contract value is no longer subject to a withdrawal charge. By contrast, the new LRR would be available to any Contract owner if on the date of application for the new LRR (''Application Date''):

- the Contract owner's initial purchase payment is no longer subject to a withdrawal charge; and
- the Contract owner's additional purchase payments, if any, would be subject to total withdrawal charges (assuming a current surrender of the Contract) equal to an amount not greater than 0.25% of the current Contract value.

The following example illustrates the operation of the new eligibility criteria: In 1990, an individual purchases a Contract with an initial purchase payment of $150,000. On January 1, 1997, the Contract owner makes an additional purchase payment of $20,000. In 2001, the Contract owner applies to add the new LRR. At that time, the Contract value is $200,000, and the additional purchase payment is subject to the Year 4 surrender charge of 2%:

(A) Contract value = $200,000

(B) Hypothetical withdrawal charge (assuming full surrender) = $20,000 x .02 = $400

(C) Eligibility Calculation (< .25%) = (B) / (A) = 400 / 200,000 = 0.20%

Because the withdrawal charge upon surrender on the Application Date is less than .25% of the Contract value, the Contract owner is eligible to add the LRR.

17. The principal purpose of the new LRR is the same as that of the existing LRR, namely, to reward eligible Contract owners for their persistency. However, the broader eligibility criteria for the new LRR is intended to meet the demands of Contract owners for such additional flexibility. Specifically, many Contract owners have expressed the desire that additional purchase payments, especially where small compared to the initial purchase payment, should not defeat eligibility for the LRR. In addition, the new LRR, like the existing LRR, will better allow Northbrook and Allstate New York to maintain the Contracts on a competitive footing with other newer variable annuity contracts in the marketplace that offer the same or similar benefits.

Applicants' Legal Analysis

1. Section 11(a) of the Act makes it unlawful for any registered open-end company, or any principal underwriter for such a company, to make or cause to be made an offer to the holder of a security of such company, or of any other open-end investment company, to exchange that security for a security in the same or another such company on any basis other than the relative net asset values of the respective securities, unless the terms of the offer have first been submitted to and approved by the Commission.

2. Section 11(c) of the Act, in pertinent part, requires, in effect, that any offer of exchange of the securities of a registered unit investment trust for the securities of any other investment company be approved by the Commission regardless of the basis of the exchange.

3. Standing alone, Section 11(a) by its terms applies only to exchanges of securities issued by ''open-end'' investment companies, which, under section 5(a)(1) of the Act, includes only management-type investment companies. ALNY Account II and Account II are unit investment trust-type (rather than a management-type) investment companies under section 4(2) of the Act. It would appear, therefore, that Section 11 could require Commission approval for Applicants' offer of the new LRR only if that offer falls within the ambit of Section 11(c).

4. Applicants do not concede that their offer of the new LRR to existing Contract owners necessarily constitutes an offer of securities of a registered unit investment trust in exchange for securities of any other investment company within the purview of Section 11(c). Nor do Applicants concede that, for purposes of Section 11, a Contract with the new LRR is a different security than a Contract without the new LRR. Nevertheless, Applicants request an exemption pursuant to Section 11(a) of the Act to the extent deemed necessary to permit the offer of the new LRR as described herein.

5. Applicants have considered whether they could rely on Rule 11a-2 under the Act. Applicants believe and represent that the only provision in Rule 11a-2 that could prevent such reliance would be the so-called ''tacking'' requirement in Rule 11a-2(d)(1). Applicants state that since the new LRR withdrawal charge continues for only three years, and since the new LRR is only available to a Contract owner if on the Application Date (a) the Contract owner's initial purchase payment was made at least six years prior to the date the new LRR is added to the Contract (''Rider Date''); and (b) the Contract owner's additional purchase payments, if any, would be subject to total withdrawal charges (assuming a current surrender of the Contract) equal to an amount not greater than 0.25% of the current Contract value, the tacking requirement effectively would prohibit the imposition of some or all of the new LRR's withdrawal charge with respect to purchase payments made prior to the Rider Date. For that reason, Applicants have concluded that Rule 11a-2 is unavailable to them.

6. Congress enacted Section 11 to prevent ''switching,'' *i.e.,* the practice of inducing security holders of one investment company to exchange their securities for those of a different investment company solely for the purpose of exacting additional selling charges. Applicants assert that the new LRR would not involve ''switching.'' Applicants maintain, to the contrary, that the purpose of the new LRR is to enable Contract owners to enhance their Contracts through the rider without having to buy a new variable annuity contract. Applicants represent that because the new LRR provides clear benefits, as described above, the new LRR's sole purpose is not to exact additional selling charges (or any other type of charge).

7. Applicants state that the new LRR would not result in any duplicative charges. Applicants represent that the limited withdrawal charge provided under the new LRR is reasonable in relation to the benefits that the rider provides and the costs that Applicants will incur in providing those benefits. Those costs will include costs of developing and administering the new LRR, the direct dollar costs of the charges that will be waived or reduced and the benefits that will be paid under the new LRR, and the costs of distributing the new LRR to Contract owners and educating them about it.

8. Applicants represent that any possible withdrawal charge under the new LRR is modest in amount. For Contract owners with additional purchase payments subject to withdrawal charges, the new LRR waives all outstanding withdrawal charges applicable under the Contract's existing withdrawal schedule and applies instead the withdrawal charge under the new withdrawal schedule,

which may result in a lower withdrawal charge. Applicants state that, if the Contract owner makes no withdrawals during the three years after the Rider Date, there is no possibility that any withdrawal charge will ever be deducted that exceeds what would have been deducted absent the new LRR. Applicants also state that even if purchase payments are withdrawn during that three-year period, the new LRR withdrawal charge will apply only if more than the 15% annual free withdrawal amount is withdrawn in any year.

9. The new LRR will be offered only to Contract owners who already have demonstrated an inclination to maintain their Contracts for substantial periods of time. Applicants believe that the income taxes that are generally payable when earnings are withdrawn from a Contract, as well as the tax penalties that may apply if those withdrawals are made prior to the owner's reaching age 59 1/2, serve as additional motivations that cause most owners to hold their Contracts for a substantial number of years (and often until retirement).

10. Applicants state that any withdrawal charge will be waived for withdrawals of any amounts necessary to meet any federal tax law minimum distribution requirements applicable to a Contract.

11. Under all these circumstances, Applicants believe that, as a practical matter, few owners that add the new LRR to their Contracts will ever actually pay any additional withdrawal charges as a result; and to the extent that the new LRR succeeds in its purpose of maintaining the Contracts on a competitive footing in the marketplace, withdrawals should be even further reduced.

12. Applicants state that except for the withdrawal charge as described above, the new LRR will not result in any increase in or imposition of any charge. Accordingly, Applicants assert that except for the potential imposition of the new LRR withdrawal charge on certain withdrawals that occur within three years after the Rider Date, every aspect of a Contract will be at least as favorable after the new LRR is added as it was before. Applicants maintain that adding the new LRR to a Contract will have no adverse tax consequences to a Contract's owner.

13. In light of these considerations, Applicants do not believe there is any public policy or purpose under Section 11 (or otherwise) that would preclude offering the new LRR on the terms and subject to the conditions stated herein.

Applicants' Conditions

1. The Offering Document will contain concise, plain English statements that: (a) the new LRR is suitable only for Contract owners who expect to hold their Contracts as long term investments; and (b) if a significant amount of the Contract's value is surrendered or withdrawn during the first three years after the Rider Date, the new LRR's benefits may be more than offset by that charge, and a Contract owner may be worse off than if he or she had rejected the new LRR.

2. The Offering Document will disclose in concise plain English the only aspect in which adding the new LRR rider could disadvantage a Contract owner (*i.e.,* through the possible imposition of the new LRR withdrawal charge).

3. A Contract owner choosing to add the new LRR will complete and sign the election form, which will prominently restate in concise, plain English the statements required in Condition No. 1, and will return it to Northbrook or Allstate New York, as appropriate. If the election form is more than two pages long, Northbrook or Allstate New York, as appropriate, will use a separate document to obtain the Contract owner's acknowledgment of the statements referred to in Condition No. 1 above.

4. Applicants will maintain and make available the following separately identifiable records, for the time periods specified below, for review by the Commission upon request: (a) Northbrook or Allstate New York, as appropriate, will maintain records showing the level of new LRR purchases and how it relates to the total number of Contract owners eligible to acquire the new LRR (at least quarterly as a percentage of the number eligible); (b)(i) Northbrook or Allstate New York, as appropriate, will maintain copies of any form of Offering Document, prospectus disclosure, election form, acknowledgment form, or offering letter, regarding the offering of the new LRR, including the dates(s) used, and (ii) Morgan Stanley will maintain copies of any other written materials or scripts for presentations used by registered representatives regarding the new LRR, including the dates used; (c) records showing information about each new LRR purchase that occurs, including (i) the following information to be maintained by Northbrook or Allstate New York, as appropriate: the name of the Contract owner; the Contract number; the election form (and separate acknowledgment form, if any, used to obtain the Contract owner's acknowledgment of the statements required in Condition No. 1 above), including the date such election or acknowledgment form was signed; the date of birth, address and telephone number of the Contract owner; the issue date of the new LRR; the amount of the Contract's value on that date; and persistency information relating to the Contract (date of any subsequent withdrawals and withdrawal charges paid); and (ii) the following information to be maintained by Morgan Stanley: the name of the Contract owner, the Contract number, the registered representative's name, CRD number, firm affiliation, branch office address and telephone number; the name of the registered representative's broker-dealer; and the amount of commissions paid to the registered representative that relates to the new LRR; and (d) each of Northbrook or Allstate New York, as appropriate, and Morgan Stanley will maintain logs showing any Contract owner complaints received by it about the new LRR, state insurance department inquiries to it about the new LRR, or litigation, arbitration or other proceedings to which it is a party regarding the new LRR.

5. Applicants will include the following information on the logs referred to in Condition No. 4(d) above: date of complaint or commencement of proceeding; name and address of the person making the complaint or commencing the proceeding; nature of the complaint or proceeding; and persons named or involved in the complaint or proceeding.

6. Applicants will retain (a) the records specified in Condition Nos. 4(a) and (d) above for six years from creation of the record; (b) the records specified in Condition No. 4(b) above for six years after the date of last use; and (c) the records specified in Condition No. 4(c) for five years from the Rider Date. The records referred to in these conditions will be prepared and retained, for the periods specified herein, by Northbrook or Allstate New York, as appropriate, and Morgan Stanley. Nevertheless, upon request of the Commission or its staff, Northbrook or Allstate New York, as appropriate, and Morgan Stanley shall coordinate the prompt assembly of such records for review at a single easily accessible location.

Conclusion

For the reasons discussed above, Applicants submit that the new LRR offer is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policies and provisions of the Act. Applicants submit

that the requested order should therefore be granted.

For the Commission, by the Division of Investment Management, pursuant to delegated authority.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–7778 Filed 3–29–02; 8:45 am]

BILLING CODE 8010–01–P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–45643; File No. SR–Amex–2001–95]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1, 2, and 3 by the American Stock Exchange LLC Relating to Its Performance Evaluation Procedures for Option, Equity and ETF Specialists

March 25, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on February 19, 2001, 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, II, and III below, which Items have been prepared by the Exchange. On December 17, 2001, the Exchange submitted Amendment No. 1 to the proposed rule change.[3] On February 1, 2002, the Exchange submitted Amendment No. 2 to the proposed rule change.[4] On February 19, 2002, the Exchange submitted Amendment No. 3 to the proposed rule change.[5] The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Exchange proposes to amend Amex Rule 26, and adopt Commentaries .04, .05, .06, and .07 to Amex Rule 26 to for options, equity and Exchange Traded Fund (''ETF'') specialists.

The text of the proposed rule change is available at the Office of the Secretary, the Amex, and at the Commission.

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 Exchange 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 Item IV 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 Exchange's Allocations Committee is responsible for allocating securities to specialists that can do a quality job with respect to the functions of a specialist. The Committee on Floor Member Performance (''Performance Committee'') reviews specialist performance and may take remedial action up to terminating a specialist's registration as such or reallocating securities when it identifies inadequate performance. The Exchange believes that these Committees protect the interests of investors, issuers and ETF sponsors by ensuring that only qualified specialists receive and retain allocations, and the institutional interests of the Exchange by ensuring that the Amex is as competitive as possible with other markets.[6]

We believe that the reallocation of a market maker's (or a specialist's) security due to poor performance is neither an action responding to a violation of an exchange rule nor an action where a sanction is sought or intended. Instead, we believe that performance-based security reallocations are instituted by exchanges to improve market maker performance and to ensure quality of markets. Accordingly, in approving rules for performance-based reallocations, we historically have taken the position that the reallocation of a specialist's or a market maker's security due to inadequate performance does not constitute a disciplinary sanction.

We believe that an SRO's need to evaluate market maker and specialist performance arises from both business and regulatory interests in ensuring adequate market making performance by its market makers and specialists that are distinct from the SRO's enforcement interests in disciplining members who violate SRO or Commission Rules. An exchange has an obligation to ensure that its market makers or specialists are contributing to the maintenance of fair and orderly markets in its securities. In addition, an exchange has an interest in ensuring that the services provided by its members attract buyers and sellers to the exchange. To effectuate both purposes, an SRO needs to be able to evaluate the performance of its market makers or specialists and transfer securities from poor performing units to the better performing units. This type of action is very different from a disciplinary proceeding where a sanction is meted out to remedy a specific rule violation. (Footnotes omitted.)

See also In re James Niehoff and Company, Administrative Proceeding File No. 3–6757, (November 30, 1986), and the other authorities cited in the Commission's *Post X–17* decision.

The Performance Committee may take remedial action on transactions that involve poor performance that are identified through Amex's surveillance or complaints. For equity securities, the Performance Committee currently reviews identified situations and ''rates'' transactions that involve inadequate

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[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Letter from Geraldine M. Brindisi, Vice President and Corporate Secretary, Amex, to Nancy J. Sanow, Esq., Assistant Director, Division of Market Regulation (''Division''), Commission (December 13, 2001) (''Amendment No. 1''). Amendment No. 1 adds specialist performance evaluation procedures for equity and ETF specialists to the proposed rule text and the purpose section of the proposal.

[4] *See* Letter from Geraldine M. Brindisi, Vice President and Corporate Secretary, Amex, to Nancy J. Sanow, Esq., Assistant Director, Division, Commission (January 31, 2002) (''Amendment No. 2''). Amendment No. 2 changes the proposed rule text, including the proposed Commentaries, from Rule 27 (''Allocations Committee'') to Rule 26 (''Performance Committee''). In addition, Amendment No. 2 clarifies that the Exchange will assign weightings to each criterion used to evaluate specialists, and notify specialists of any changes to the criteria or the weightings used by the Exchange.

[5] *See* Letter from Geraldine M. Brindisi, Vice President and Corporate Secretary, Amex, to Nancy J. Sanow, Esq., Assistant Director, Division, Commission (February 14, 2002) (''Amendment No. 3''). Amendment No. 3 clarifies the rule text to reflect the criteria that the Exchange will initially use to evaluate specialists. In addition, Amendment No. 3 clarifies that the Exchange will allocate weightings to the criteria, and notify specialists of these relative weightings before implementation. Amendment No. 3 also adds to the proposed rule text that the Exchange may change the criteria or weightings allocated to the criteria in order to enhance competitiveness relative to other markets and/or to improve market quality. Finally, Amendment No. 3 corrects typographical errors made in the proposed rule text.

[6] *See In the Matter of the Application of Pacific Stock Exchange's Options Floor Post X–17,* Admin. Proc. File No. 3–7285, Securities Exchange Act Release No. 31666 (December 29, 1992), 51 SEC Dkt. 261. The Commission determined that performance evaluation processes fulfill a combination of business and regulatory interests at exchanges and are not disciplinary in nature. The Commission states in the *Post X–17* case: