

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54552; File No. SR-Amex-2005-104]

### Self-Regulatory Organizations; American Stock Exchange LLC; Order Approving a Proposed Rule Change and Amendments No. 1, 2, 3, 4, and 5 Thereto, and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 6, To Establish a New Hybrid Trading System Known as AEMI<sup>SM</sup>

September 29, 2006.

#### I. Introduction

On October 17, 2005, the American Stock Exchange LLC (“Amex” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), 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> a proposed rule change to implement a new hybrid market structure for equities and exchange-traded funds (“ETFs”) known as the “Auction & Electronic Market Integration” (“AEMI”). Amex amended the proposal on January 19, 2006;<sup>3</sup> March 10, 2006;<sup>4</sup> March 14, 2006;<sup>5</sup> July 3, 2006;<sup>6</sup> and July 13, 2006.<sup>7</sup> The proposed rule change, as amended, was published for comment in the **Federal**

**Register** on July 21, 2006.<sup>8</sup> The Commission received no comments on the proposal. On September 29, 2006, Amex filed Amendment No. 6 to the proposal.<sup>9</sup> This order approves the proposed rule change, as amended by Amendments No. 1, 2, 3, 4, and 5, grants accelerated approval to Amendment No. 6, and solicits comments from interested persons on Amendment No. 6.

#### II. Description of Proposal

Utilizing AEMI, Amex proposes to implement a new hybrid market structure to integrate automated and floor-based trading for equities and ETFs. The Exchange has designed AEMI to enable it to comply with Regulation NMS,<sup>10</sup> particularly Rules 610 (the Access Rule) and 611 (the Order Protection Rule),<sup>11</sup> and to operate as an automated trading center<sup>12</sup> whose quotes would be protected by Rule 611. Although AEMI includes many new features, many of Amex’s existing floor-based rules are being incorporated into the new AEMI rules.

##### A. General Overview of AEMI

Central to the AEMI system is the electronic order book where marketable trading interest will automatically execute. AEMI by default will publish an automated best bid and offer for the Exchange (also referred to as the “Amex Published Quote” or “APQ”), and the default state of operation will be automatic execution (“auto-ex”). Generally, if an incoming order is marketable, it would automatically execute against any contra-side interest on the AEMI Book until its limit price, if any, is reached. Any remainder would be displayed on the AEMI Book as part of the new APQ. Market participants also can use the “hit or take” functionality to trade immediately against the APQ. Notwithstanding the foregoing, if an incoming order locks or crosses a protected quotation of another trading center and that protected quotation is better priced than the APQ, AEMI would send an intermarket sweep order (“ISO”) for the displayed quantity of the protected quotation. Any remaining size could execute on the AEMI system or be displayed in the AEMI Book, as appropriate. Executions would occur according to the

Exchange’s rules of parity and priority, discussed in more detail below.

Amex will retain a physical trading floor, although verbal bids and offers have no standing until entered into the AEMI system.<sup>13</sup> A trade negotiated on the floor, when entered into the system, can be broken up by electronic orders at the same price on the AEMI Book or by better-priced protected quotations at other trading centers. In addition, auto-ex will be disabled in certain limited circumstances where Amex believes that an auction market is appropriate to seek additional liquidity or to dampen volatility in the market.

In its new hybrid market, Amex will continue to have Specialists, Registered Traders, Floor Brokers, and off-floor members.<sup>14</sup> Every equity security traded on the Exchange will be assigned to a Specialist. Like today, Specialists will have affirmative and negative obligations to maintain a fair and orderly market in the securities in which they are registered. Registered Traders will act as supplemental market makers in ETFs. Floor Brokers can trade in the crowd or submit orders directly to the book. Off-floor members can send orders directly to the book or to Floor Brokers for representation in the crowd. In addition, Amex proposes to create a number of new order types and retain or revise certain existing order types. Generally, all AEMI order types will be available to all members, except for reserve orders and percentage orders which may be used only by Floor Brokers.

##### B. Regulation NMS Compliance

###### 1. Automated Trading Center

Amex intends to operate AEMI as an automated trading center under Regulation NMS whose default state will be to disseminate automated quotations.<sup>15</sup> However, Amex has designed AEMI to revert to an auction market to provide additional liquidity and price discovery, or to dampen volatility in the market, as determined by market conditions. Thus, the AEMI rules contemplate situations where the system would disable auto-ex and mark the Amex quotation as non-firm. The Exchange intends to continuously monitor the frequency and cause of automatic execution being disabled, and has represented that it would, as necessary and with the appropriate

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

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

<sup>3</sup> See Form 19b-4 dated January 19, 2006, which replaced the original filing in its entirety (“Amendment No. 1”).

<sup>4</sup> See Form 19b-4 dated March 10, 2006, which replaced Amendment No. 1 in its entirety (“Amendment No. 2”).

<sup>5</sup> See Form 19b-4 dated March 14, 2006, which replaced Amendment No. 2 in its entirety (“Amendment No. 3”).

<sup>6</sup> See Form 19b-4 dated July 3, 2006, which replaced Amendment No. 3 in its entirety (“Amendment No. 4”). Amendment No. 4, among other things: (1) Removed the Passive Price Improvement order type from the proposal; (2) stated the Exchange’s commitment to make AEMI’s depth-of-book information broadly available; (3) added additional size and value requirements for certain cross orders; (4) distinguished two quote indicators that may be disseminated in connection with the Exchange’s publishing of non-firm quotes; (5) revised the procedures regarding the receipt of a partial fill or no response to an outgoing intermarket sweep order; and (6) made various other minor corrections and clarifications to the proposed rule change.

<sup>7</sup> See Partial Amendment to Form 19b-4 dated July 13, 2006. (“Amendment No. 5”). In Amendment No. 5, the Exchange, among other things: (1) Set forth a timeframe for the availability of depth-of-book data; (2) clarified when Specialists may charge commissions; (3) clarified when the Exchange will send intermarket sweep orders to other markets; and (4) acknowledged that the Exchange’s rules would not obviate or invalidate any trade made pursuant to another market’s rules.

<sup>8</sup> See Securities Exchange Act Release No. 54145 (July 14, 2006), 71 FR 41654 (“Notice”).

<sup>9</sup> See Partial Amendment to Form 19b-4 dated September 29, 2006 (“Amendment 6”). See *infra* Section III.

<sup>10</sup> Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37495 (June 29, 2005) (“Regulation NMS Release”).

<sup>11</sup> 17 CFR 242.610 and 242.611.

<sup>12</sup> See 17 CFR 242.600(b)(3) (defining “automated trading center”).

<sup>13</sup> See Rule 123-AEMI(a).

<sup>14</sup> In a separate filing, Amex also has proposed rules relating to Registered Equity Market Makers (“REMMs”). See File No. SR-Amex-2006-35.

<sup>15</sup> See 17 CFR 242.600(b)(3) (defining “automated quotation”) and 242.600(b)(4) (defining “automated trading center”).

regulatory approvals, adjust the conditions under which auto-ex could be disabled to maintain market quality for investors and retain its status as an automated trading center.<sup>16</sup>

a. Integration of Floor Trading

The AEMI system will be augmented by a traditional trading floor. Verbal bids and offers in the crowd do not have standing in the AEMI Book. A trade negotiated in the crowd cannot be consummated until entered into the AEMI system, and such a trade could potentially be broken up by existing interest in the AEMI Book or by protected quotations at other trading centers. Negotiated trades are one-to-one trades between two crowd members (possibly including the Specialist) and are allowed only while auto-ex is enabled. Auction trades, on the other hand, may take place while auto-ex is enabled or while auto-ex is disabled. In the latter case, an auction trade may occur for the sole purpose of resolving the condition that caused auto-ex to be disabled.

An auction trade is: (1) A trade executed between or among members on the floor by open outcry (which could incorporate orders on the AEMI Book); or (2) a cross trade executed by a member on the floor by open outcry.<sup>17</sup> A Specialist would immediately enter an auction trade into AEMI if it participates in the trade. If the Specialist is not part of an auction trade, the member who initiates the trade would immediately be required to report the trade to the Specialist for input into AEMI. Upon input, AEMI would: (1) Send a report of the trade to the tape, less the size of any outbound ISOs;<sup>18</sup> (2) execute any orders on the AEMI Book that could be executed at the price of the auction trade; (3) generate outbound ISO(s), as necessary; and (4) if auto-ex had been disabled, re-enable auto-ex and disseminate a new automated APQ. Auction trades could not take place outside the APQ when auto-ex is enabled.

The Specialist would confirm and conduct the post-trade allocation for trades with more than one contra-side member, and AEMI would then send notification of individual trades to active crowd participants. The Specialist is required to confirm the initial post-trade allocation (which is an estimate computed by AEMI based on assumed participation by all of the active crowd participants and the

Exchange's priority and parity rules) to allow the active crowd participants to verbally confirm whether they participated. AEMI would compute any necessary adjustments in the Specialist's allocation. If the allocation is not confirmed by the Specialist within a three-minute period following the trade, AEMI's estimated allocation to the Specialist and the active crowd participants would be used.<sup>19</sup>

b. Disabling Auto-Ex

Automatic execution on AEMI would be disabled, resulting in the dissemination of a non-firm quote, in six enumerated circumstances generally relating to a large order imbalance, high volatility, or a systems malfunction. When auto-ex is disabled under the six circumstances, members may not trade in the open outcry market, other than to consummate an auction trade to remove the condition that caused auto-ex to be disabled. While auto-ex is disabled, market participants may enter or cancel bids, offers, and orders in AEMI.<sup>20</sup>

i. Spread Tolerance

The spread tolerance would be breached and auto-ex disabled if an inbound order walks the book beyond a predefined price level relative to the price of the security at the time of the initial execution against the order.<sup>21</sup> The spread tolerance is designed to mitigate volatility caused by the entry of a large order if there is no natural contra-interest on the book. The spread tolerance is an Exchange-set parameter per security and would be dynamically applied according to the first execution price of the security against the incoming order, based on the table below:

Stock price	Tolerance (cents)
Less Than \$5 .....	5
\$5 to \$15 .....	15
More Than \$15 .....	25

ii. Momentum Tolerance

The momentum tolerance would be breached, and auto-ex disabled, if multiple orders moved the price of a security in one direction beyond a predefined boundary in a 30-second time period.<sup>22</sup> The momentum tolerance is designed to mitigate volatility caused by a rapid succession of small orders in a short time frame. The Exchange designed the spread and momentum tolerances to work together to prevent

excessive volatility. Thus, while a series of small orders might not individually trigger the spread tolerance, their combined effect could trigger the momentum tolerance.

iii. Gap Trade Tolerance

A gap trade tolerance would be breached if the gap between the current quotation and the last sale exceeded the parameters of the Exchange's "1%, 2, 1, 1/2" point rule.<sup>23</sup>

iv. Delayed Opening, Gap Quote, or Trading Halt

AEMI also would disable auto-ex if the opening is delayed, Amex is disseminating a gap quote, or trading is halted in a security.<sup>24</sup>

A specialist may "gap the quote" when an order imbalance exists.<sup>25</sup> A Specialist could gap the quote when either: (1) A large order has been represented in the crowd; or (2) an incoming electronic order has swept the book, disabled auto-ex, and left a large imbalance. If the Specialist gaps the quote, auto-ex would be disabled and a non-firm quote disseminated to reflect the order imbalance. If auto-ex had already been disabled by a tolerance breach, it would remain disabled and the existing non-firm quote would be updated with a non-firm gapped quote. After publishing the gapped quote, the Specialist would be required to ask a Senior Floor Official or an Exchange Official to supervise the process.

In such a situation, the Specialist would display on the imbalance side a bid or offer equal to the price of the automated NBBO on the same side corresponding to the order causing the imbalance and show the full size of the electronic imbalance or the order represented in the crowd. The Specialist would display one round lot for the contra-side size. If the gapped quote were the result of an order represented in the crowd, the Floor Broker whose order imbalance caused the quote to be gapped would be required to enter his order into AEMI immediately. The price of the contra-side of the quotation would represent the Specialist's determination of the price at which the stock would trade if no contra-interest develops or no cancellations occur as a result of the gapped quotation. A gapped quote could be displayed up to two minutes or until offsetting interest is received electronically, such that the Specialist could pair off the imbalance and re-enable auto-ex. Auto-ex would be

<sup>16</sup> See Amendment No. 4, at 12.

<sup>17</sup> See Rule 128B-AEMI.

<sup>18</sup> See *infra* Section II(B)(2)(b) (discussing use of ISOs).

<sup>19</sup> See Rule 128B-AEMI(b).

<sup>20</sup> See Amendment No. 6, *supra* note 9.

<sup>21</sup> See Rule 128A-AEMI(f)(i).

<sup>22</sup> See Rule 128A-AEMI(f)(ii).

<sup>23</sup> See Rule 128A-AEMI(f)(iv); Rule 154-AEMI(e). These rules do not apply to ETFs.

<sup>24</sup> See Rule 128A-AEMI(f)(iii).

<sup>25</sup> See Rule 170-AEMI(f).

disabled until the Specialist performs a pair-off trade and the APQ is updated and re-automated. While the quotation is gapped, orders, cancellations, and other messages would continue to enter AEMI, but would not update the APQ and no trades would occur. In addition, commitments received via the Intermarket Trading System ("ITS") during a gapped quote would be canceled.

The Senior Floor Official or Exchange Official supervising the process will determine whether: (1) To execute the orders immediately and terminate the gapped quote; (2) direct the Specialist to maintain the gapped quotation to allow time for contra-side interest to develop or cancellations to occur (but in any event not more than two minutes); or (3) halt trading in the stock. At the end of the two minutes from the initiation of the gapped quote, the Specialist, in consultation with the supervising Senior Floor Official or Exchange Official, must either: (1) Conduct an auction trade and disseminate an automated quotation; or (2) halt trading in the stock.

The size of an imbalance suitable for gapped quoting is at least 10,000 shares or a quantity of stock having a value of \$200,000 or more. However, "depending on the trading characteristics of the security, the appropriate conditions for gapped quoting may be higher."<sup>26</sup>

#### v. Unusual Market Conditions

AEMI also will disable auto-ex when the Exchange determines that unusual market conditions exist in one or more securities.<sup>27</sup> If the Exchange is unable to accurately collect, process, and/or disseminate quotation data in one or more securities due to a high level of trading activity or the existence of unusual market conditions, AEMI would immediately disable auto-ex and disseminate the indicator "N" to indicate that Amex's quotation, if a trading halt has not been declared and quotations are being published for such security or securities, is not firm. An unusual market condition affecting the Exchange's ability to disseminate quotation data would include, but not be limited to, situations where the equipment used to collect, process, and disseminate quotation data becomes inoperable.<sup>28</sup>

If a Specialist were unable to update its quotation on a timely basis due to the high level of trading activity or the existence of an unusual market condition, it would be required to

promptly notify a Floor Official.<sup>29</sup> Once the Floor Official, with the involvement of a member of the Amex regulatory staff, promptly verifies the existence of the unusual market activity or condition, the Floor Official would notify Amex's Market Operations Division, which would then promptly disable auto-ex and disseminate the indicator "N" to indicate that Amex's quotation, if a trading halt has not been declared and quotations are being published for such security or securities, is not firm. The Floor Official also would consult with Amex's Market Operations Division to determine whether to declare a non-regulatory halt in such security or securities if the ability of the Specialist to promptly communicate quotation data is adversely affected. In the absence of such a non-regulatory halt, incoming orders would continue to execute against orders for the security or securities in the AEMI Book.

#### vi. Cash-Close Pair-Off in ETFs

For automatic execution eligible securities that trade until 4 p.m., auto-ex would be disabled one second prior to 4 p.m. if there were any on-close orders in the AEMI Book. However, for ETFs that trade until 4:15 p.m., auto-ex would be disabled: (1) One second prior to 4 p.m., if there were any cash close orders in the AEMI Book, and resume immediately after the Specialist performed the cash close; and/or (2) one second prior to 4:15 p.m., if there were on-close orders in the AEMI Book.<sup>30</sup>

#### vii. Re-Enabling Auto-Ex

If auto-ex were disabled due to any tolerance breach, the Specialist would have ten seconds to attempt to re-enable auto-ex and disseminate a new automated APQ.<sup>31</sup> Thereafter, AEMI would periodically attempt to resume auto-ex and disseminate a new automated APQ. If the remainder of the aggressing order causing the breach expires or cancels, or if the AEMI Book is not locked or crossed, the Specialist could re-enable auto-ex prior to the expiration of the ten-second period through a "front end" device. If the order imbalance remains or if the AEMI Book remains locked or crossed, the Specialist could conduct an auction for the imbalance, and the action of printing the auction trade or performing a pair-off would automatically re-enable auto-ex and publish an automated quote. If the Specialist does not take

such action or gap the quote by the end of the ten-second period, auto-ex would automatically resume if the AEMI Book is not locked or crossed. If the AEMI Book is still locked or crossed after the initial ten-second period and the Specialist has not acted, AEMI would attempt to re-enable auto-ex in ten-second intervals. When auto-ex is disabled due to the breach of a spread or momentum tolerance or a gap trade, orders and quotations (with the exception of the Specialist's quotation) that enter the AEMI Book and are priced better than the contra-side of the APQ would participate in the auction trade to eliminate the locked or crossed market. Once the pair-off is completed, AEMI would automatically disseminate a new automated APQ.

#### 2. Compliance with Rule 611 of Regulation NMS

##### a. Generally

AEMI would generate an ISO to clear the displayed size of any better-priced protected quotation of another automated trading center before executing a trade at an inferior price, except as set forth below.<sup>32</sup> ISOs may be sent or received through ITS or private linkages.<sup>33</sup> However, AEMI would not generate an ISO when one of the exceptions in Rule 611 applies.

##### b. Intermarket Sweep Orders

The AEMI rules contemplate both inbound and outbound ISOs.<sup>34</sup> An inbound ISO is a limit order for an NMS stock received by AEMI from a member which is to be executed: (1) Immediately at the time such order is received in the AEMI Book; (2) without regard for better-priced protected quotations displayed at one or more other trading centers; and (3) at prices equal to or better than the limit price, with any portion not so executed to be treated as canceled. An inbound ISO could trade at multiple prices on AEMI up to its limit price, except for an inbound ISO received through the ITS or any successor thereto, which would trade only at a single price, the Amex best bid or offer.<sup>35</sup>

An outbound ISO would be generated by AEMI to execute against all better-priced protected quotations displayed by other trading centers up to their displayed size.<sup>36</sup> An ISO would be marked as such to inform the receiving trading center that it can be executed immediately without regard to protected

<sup>32</sup> See Rule 126A-AEMI.

<sup>33</sup> See Amendment No. 4, at 111.

<sup>34</sup> See Rule 131-AEMI(j).

<sup>35</sup> See *id.*

<sup>36</sup> See *id.*

<sup>26</sup> Rule 170-AEMI(f).

<sup>27</sup> See Rule 128A-AEMI(f)(vi).

<sup>28</sup> See Rule 115-AEMI, Commentary .01(2).

<sup>29</sup> See Rule 115-AEMI, Commentary .01(1)(a) and .01(1)(b).

<sup>30</sup> See Rule 131-AEMI, Commentary .03.

<sup>31</sup> See Rule 128A-AEMI(g).

quotations in other trading centers. Unless an appropriate exception applied, AEMI would send ISOs for the full displayed size of any better-priced protected quotation of another trading center before executing a trade at a worse price.<sup>37</sup> An outbound ISO also would be generated if an order entered into the AEMI system would lock or cross a protected quotation in an away market.<sup>38</sup>

Each outbound ISO would be designated as immediate-or-cancel and carry an expiration delay timer.<sup>39</sup> If AEMI receives a no-fill or partial fill in response to the outbound ISO and the quotation at the away market is not updated, AEMI would release the corresponding order that had been suspended so that it may re-aggress the AEMI Book (and generate new ISOs to other trading centers, if necessary). AEMI would, however, continue to route ISOs to that particular trading center's protected quotation in that security.<sup>40</sup>

If AEMI receives no response at all to an outbound ISO and assuming no system errors have been detected, AEMI would issue a cancellation at the expiration of the delay timer. This action would release the corresponding order that had been suspended on the AEMI Book pending the response to the ISO.<sup>41</sup> The released order would then re-aggress the AEMI Book (and generate new ISOs to other away markets, if necessary). Amex has acknowledged that, if it ultimately receives a trade report from the away market, it will be bound by the away market's rules regarding such trades.<sup>42</sup>

#### c. Trade Reporting of Rule 611 Exceptions

Following the "Trading Phase Date" of Regulation NMS (February 5, 2007),<sup>43</sup> the Exchange will identify all trades executed pursuant to an exception or exemption from Rule 611 of Regulation

NMS in accordance with specifications approved by the operating committee of the relevant national market system plan for an NMS stock.<sup>44</sup> If a trade is executed pursuant to both the intermarket sweep order exception of Rule 611(b)(5) or (6)<sup>45</sup> and the self-help exception of Rule 611(b)(1),<sup>46</sup> such trade shall be identified as executed pursuant to the ISO exception.

#### d. Self Help

The AEMI rules also provide that the Exchange may invoke "self help" in certain circumstances and thereby disregard what appears to be a protected quotation of another trading center. In Amendment No. 6, Amex added new language to Rule 126A-AEMI to provide that, in accordance with Rule 611(a) of Regulation NMS,<sup>47</sup> the Exchange may, pursuant to objective industry-wide established interpretations and policies, determine to bypass the quotations displayed by another trading center if such trading center repeatedly fails to respond within one second to orders attempting to access such trading center's protected quotations, provided such failures are attributable to such trading center and are not attributable to transmission outside the control of such trading center. In connection with any such determination, the Exchange will immediately notify the non-responding trading center of such determination.

#### e. Order Routing

Amex would route orders to other trading centers under certain circumstances. Such routing services would occur pursuant to three separate agreements: (1) An agreement between the Exchange and each member on whose behalf orders would be routed; (2) an agreement between the Exchange and each third-party broker-dealer that would serve as a "give-up" on an away trading center when the member on whose behalf an order is routed is not also a member or subscriber of the away trading center; and (3) an agreement between the Exchange and a third-party service provider pursuant to which the Exchange licenses the routing technology used by the Exchange for its routing services.<sup>48</sup>

With respect to these routing services, Amex would establish and maintain procedures and internal controls reasonably designed to adequately restrict the flow of confidential and proprietary information between the

Exchange (including its facilities) and the third-party service provider. To the extent the provider reasonably receives confidential and proprietary information, its use of such information would be restricted to legitimate business purposes necessary for the licensing of routing technology.

#### f. Locked and Crossed Markets

Amex has proposed rules regarding locked and crossed markets, as required by Rule 610(d) of Regulation NMS.<sup>49</sup> Exchange members shall reasonably avoid displaying, and shall not engage in a pattern or practice of displaying, any quotations that lock or cross a protected quotation, and any manual quotations that lock or cross a quotation previously disseminated pursuant to an effective national market system plan,<sup>50</sup> except if one of the following exceptions applies:<sup>51</sup>

- The locking or crossing quotation was displayed at a time when the trading center displaying the locked or crossed quotation was experiencing a failure, material delay, or malfunction of its systems or equipment.
- The locking or crossing quotation was displayed at a time when a protected bid was higher than a protected offer in the NMS stock.
- The locking or crossing quotation was an automated quotation, and the member displaying such automated quotation simultaneously routed an ISO to execute against the full displayed size of any locked or crossed protected quotation.
- The locking or crossing quotation was a manual quotation that locked or crossed another manual quotation, and the member displaying the locking or crossing manual quotation simultaneously routed an ISO to execute against the full displayed size of the locked or crossed manual quotation.

The rule addresses intentional locks and crosses by requiring that all locks and crosses of protected quotations be reasonably avoided and prohibiting a pattern or practice of locks or crosses. The rule also restricts the display of manual quotations that would lock or cross any type of quotation, whether automated or manual. There is no restriction on the display of automated quotations that lock or cross manual quotations.<sup>52</sup>

#### g. MPV

The minimum price variation ("MPV") on AEMI for quotations and

<sup>37</sup> See Rule 126-AEMI.

<sup>38</sup> See Rule 126A-AEMI.

<sup>39</sup> The expiration delay timer would control how long AEMI would wait before attempting to cancel the ISO. See *id.*

<sup>40</sup> See *id.*

<sup>41</sup> See *id.* See also Rule 128B-AEMI(c) (describing similar procedure when Amex does not receive a response to an outbound ISO generated by an auction trade).

<sup>42</sup> See Amendment No. 4, Item 9.

<sup>43</sup> By no later than February 5, 2007, all trading centers intending to qualify their quotations for trade-through protection must bring a Regulation NMS-compliant trading system into full operation for all NMS stocks intended to be traded during the phase-in period (*i.e.*, through October 8, 2007). See Securities Exchange Act Release No. 53829 (May 18, 2006), 71 FR 30038 (May 24, 2006) (extending compliance dates for Rules 610 and 611 of Regulation NMS).

<sup>44</sup> See Rule 126A-AEMI(a).

<sup>45</sup> 17 CFR 242.611(b)(5) or (6).

<sup>46</sup> 17 CFR 242.611(b)(1).

<sup>47</sup> 17 CFR 242.611(a).

<sup>48</sup> See Rule 126B-AEMI.

<sup>49</sup> 17 CFR 242.610(d).

<sup>50</sup> See Rule 128C-AEMI(b).

<sup>51</sup> See Rule 128C-AEMI(d).

<sup>52</sup> See Rule 128C-AEMI, Commentary .01.

orders priced above \$1.00 per share is \$0.01.<sup>53</sup> For quotations and orders priced below \$1.00 per share, the MPV on AEMI is \$0.0001.

#### h. AEMI Implementation

Rule 1A–AEMI describes the roll-out of the AEMI system. AEMI's anticipated roll-out would commence prior to the Trading Phase Date for Regulation NMS (February 5, 2007). By the Trading Phase Date, all ETFs, equities, and securities that trade like equities that are traded on the Exchange would be on the AEMI platform. During the roll-out period, while the Exchange has securities trading on its legacy and AEMI platforms, the Exchange's current rules (as amended from time to time) would apply to those securities continuing to trade on the legacy platform. The AEMI rules would apply to those securities trading on the new trading platform. When a security transfers to AEMI, the AEMI rules will govern trading in that security and the corresponding legacy rule would no longer have any applicability. When all securities have transferred off the legacy platform, Amex will submit a proposed rule change to delete any unnecessary legacy rules.

The AEMI rules would cover the operation of the AEMI platform to become effective on and after the Trading Phase Date. However, Amex intends to operate a modified early version of the AEMI platform to operate prior to the Trading Phase Date. Amex has submitted a separate rule change for this interim system, which would be referred to as "AEMI–One." That proposal makes minor modifications to the AEMI rules to account for the fact that other trading centers may not have fully implemented their Regulation NMS-compliant trading systems.<sup>54</sup>

#### C. Other Rules

##### 1. Role of Specialists

Amex would have a Specialist for each security traded on AEMI. A Specialist is required "to engage in a course of dealings for its own account to assist in the maintenance, insofar as reasonably practicable, of a fair and orderly market on the Exchange."<sup>55</sup> The Specialists must, among other things, maintain a two-sided quotation in every

security in which it is registered.<sup>56</sup> To facilitate the Specialists' obligation to maintain a continuous two-sided quotation, AEMI would provide an emergency quote function. If the Specialist's quote were exhausted or decremented below a specified size, and a new quote were not automatically generated, AEMI would generate an emergency quote based on the parameters programmed by the Specialist.

##### a. Openings

At the opening, the Specialist is required to perform a pair-off of orders in the AEMI Book.<sup>57</sup> AEMI will permit the opening pair-off session to last no more than three seconds. During the opening pair-off session, the Specialist must select a single opening pair-off price at which AEMI will execute all market and marketable limit orders. Incoming orders, cancellations, and other messages will be held in a Message Queue and not included in the opening pair-off. If the Specialist has not completed the opening pair-off within three seconds, the pair-off session will terminate, all messages in the Message Queue will enter the AEMI Book, and the Specialist will have to reinitiate the opening pair-off session to open the security. During the actual pair-off, orders that are being processed as part of the pair-off cannot be altered or canceled. If no orders on the AEMI Book are eligible for execution on the open, the Specialist will open the security on a quotation without a trade.

##### b. Closings

The Specialist also will conduct a pair-off session at the closing. In both UTP and listed securities, an on-close imbalance of 25,000 shares or more would be automatically published to the tape at 20 and then at ten minutes before the market close at 4 p.m.<sup>58</sup> In all securities, the closing pair-off session would commence automatically at the official closing time and disable auto-ex. To participate in the close, all orders must have been entered electronically.

<sup>56</sup> Specialists would have a variety of ways to submit quotations into AEMI. They could: (1) Stream two-sided quotes up to five price points on each side (one quote per price point) of the AEMI Book; (2) generate automatic quotes ("auto-quotes") within AEMI based on user-specified parameters relating to size, ticks, and underlying market data; or (3) physically enter single, two-way quotes into AEMI ("solo quotes"). A Specialist could enter solo quotes at any time, which would override the best existing auto-quote or streaming quote.

<sup>57</sup> See Rule 108–AEMI(d).

<sup>58</sup> The imbalances would be published to Consolidated Tape Association ("CTA") Tape B for Amex listed securities. Amex is working with the Nasdaq SIP to publish the imbalances in Nasdaq UTP securities to Tape C.

The Specialist will manually close each security.

The Specialist would execute any imbalance at an auction price in accordance with auction market procedures and pair off and execute the remaining executable orders at that closing price. Percentage orders and stop orders elected at the closing price could be included in the close. The Specialist would conduct a post-trade allocation with respect to the shares necessary to offset the imbalance, as with a regular auction. Until this post-trade allocation process is completed, the Specialist would be responsible for the contra-side of the imbalance traded. If there are no on-close orders, the closing price would be the last sale in the security. If at the close the imbalance is too large for the Specialist and the crowd to offset, the Exchange would declare a trading halt and there would be no closing rotation for that security.

In the case of certain ETFs that trade until 4:15 p.m., the Specialist could perform a "cash close" pair-off during the regular trading session at 4 p.m. prior to the official closing session on the Exchange. This would be an added service for investors wishing to mark positions to the cash close. In the event there are "market at 4 p.m. cash close" orders for an ETF, auto-ex would be disabled for that security at 4 p.m. Once the pair-off is concluded, auto-ex would resume until it is disabled for the official closing pair-off at 4:15 p.m.

##### c. Stabilization

Because of the AEMI automated environment, Amex proposes to modify certain existing rules related to Specialist obligations, in particular its existing requirements for certain transactions for the Specialist's own account involving destabilizing ticks requiring Floor Official approval.<sup>59</sup> In Rule 170–AEMI, Commentary .01, Amex proposes to ease the restrictions relating to a Specialist effecting transactions for its own account for the purpose of establishing or increasing a position. The following types of transactions generally would be prohibited, except with the approval of a Floor Official:

- A purchase on the offer at a price above the last regular way trade in the same trading session, or a sale short to the bid at a price below the last regular way trade in the same trading session where permitted by the Commission's short sale regulations;
- The purchase of all or substantially all of the stock offered on the AEMI Book on a zero plus tick, when the stock

<sup>59</sup> See Rule 170–AEMI.

<sup>53</sup> See Rule 127–AEMI.

<sup>54</sup> See Securities Exchange Act Release No. 54413 (September 8, 2006), 71 FR 54318 (September 14, 2006) ("AEMI–One Notice").

<sup>55</sup> Rule 170–AEMI(b). Thus, a Specialist's quotation in an ETF or other derivatively priced security should bear a proper relation to the value of underlying or related securities. See Rule 170–AEMI, Commentary .03.

so offered represents all or substantially all the stock offered in the market;

- The supplying short of all or substantially all the stock bid for on the AEMI Book on a zero minus tick where permitted by the Commission's short sale regulations, when the stock so bid for represents all or substantially all the stock bid for in the market; and
- Failing to re-offer or re-bid where necessary after effecting the transactions described above.

A Specialist may also effect an auto-ex transaction on a destabilizing tick without the approval of a Floor Official in the situations described above if: (1) The buy is on the APQ (which must be equal to the Specialist's bid) when its bid is accessed by a sell order; or (2) the sale is on the APQ (which must be equal to its offer) when its offer is accessed by a buy order.<sup>60</sup>

In addition, Amex proposes to ease the restrictions relating to a Specialist's transactions for its own account in liquidating or decreasing a position in a registered stock.<sup>61</sup> Unless such transactions are reasonably necessary in relation to the Specialist's overall position and prior approval of a Floor Official has been obtained, a position may not be liquidated by selling stock to the bid on a direct minus tick or by purchasing stock on the offer on a direct plus tick. The Specialist would be permitted to effect an auto-ex transaction on a destabilizing tick without Floor Official approval if: (1) The buy is on the Amex Published Bid (which must be equal to its bid) when its bid is accessed by a sell order; or (2) the sale is on the Amex Published Offer (which must be equal to its offer) when the offer is accessed by a buy order. Furthermore, a Specialist's quotation should be such that a transaction effected at its quoted price or within the quoted spread, whether having the effect of reducing or increasing the Specialist's position, "would bear a proper relation to preceding transactions and anticipated succeeding transactions."<sup>62</sup> In the case of ETFs or other derivatively priced securities, the Specialist's quotation should bear a proper relation to the value of the underlying or related securities.<sup>63</sup>

#### d. Duty to Yield

A Specialist must give precedence to orders in the Specialist Order Book, which is a subset of the AEMI Book, in any security in which it is registered before executing at the same price any

trade in the same security in which it has an interest.<sup>64</sup> Three types of trades are excepted from that general rule:

- The member entering a percentage order has permitted the Specialist to be on parity.
- In ETFs, the Specialist may be on parity with a broker-dealer order pursuant to Rule 126-AEMI.
- The Specialist need not give precedence to an order that has been suspended in AEMI because an outbound ISO has been routed to another trading center on its behalf.

The Exchange anticipates allowing a Specialist to charge commissions under AEMI for orders that require special handling or for which the Specialist otherwise provides a service as agent for the order (e.g., percentage orders).<sup>65</sup> However, existing Amex Rule 152(c) prohibits the Specialist from charging a commission if it is a party to the trade. Furthermore, Amex has represented that the Specialist will not be allowed to charge a commission on any transaction in AEMI to which the Specialist's proprietary position is not required to yield by AEMI rules or the Specialist's agency responsibility. For instance, an ETF Specialist will be allowed to trade on parity with, but not charge a commission for, a broker-dealer order in that ETF.

#### 2. Role of Registered Traders

Registered Traders will act as supplemental market makers in ETFs and certain other related securities.<sup>66</sup> The functions of a Registered Trader would essentially remain the same as today,<sup>67</sup> although its quote would not be imbedded in the Specialist's quote.<sup>68</sup> Instead, a Registered Trader would be required to maintain a quote that is competitive and separate from the Specialist. Registered Traders and Specialists are required to compete with each other to improve the quoted markets in all securities in which they trade.<sup>69</sup>

A Registered Trader's transactions should constitute a course of dealings

<sup>64</sup> See Rule 155-AEMI. See also Rule 126-AEMI(2)(a)(iv)(A)(I) (requiring an in-parity Specialist quotation to yield to any public order at the same price).

<sup>65</sup> See Amendment No. 5, Item 3.

<sup>66</sup> See Rule 1A-AEMI(g) (defining "Registered Trader"); Rule 110-AEMI(o).

<sup>67</sup> See Rule 110-AEMI.

<sup>68</sup> Like a Specialist, a Registered Trader could: (1) Stream two-sided quotes up to five price points on each side (one quote per price point) of the AEMI Book; (2) auto-quote within AEMI based on user-specified parameters relating to size, ticks, and underlying market data; or (3) manually enter solo quotes. The entry of a Registered Trader's solo quotes would override its best existing auto-quote or streaming quote.

<sup>69</sup> See Rule 110-AEMI(u).

reasonably calculated to contribute to the maintenance of a fair and orderly market, and no Registered Trader should enter into transactions to make bids or offers that are inconsistent with such a course of dealings.<sup>70</sup> Whenever a Registered Trader enters the trading crowd in other than a floor brokerage capacity, or is called upon by a Floor Official or a Floor Broker, the Registered Trader is required to make competitive bids and offers as reasonably necessary to contribute to the maintenance of a fair and orderly market and shall engage, to a reasonable degree under the circumstances, in dealings for its own account when there exists a lack of price continuity in, or a temporary disparity between the supply of and demand for, the security it is trading.<sup>71</sup> A Registered Trader must meet certain trading thresholds in the securities it trades to be designated a specialist under the Act.<sup>72</sup>

#### 3. Role of Floor Brokers

Floor Brokers on AEMI would be able to participate in automatic execution while continuing to represent orders in the crowd.<sup>73</sup> To represent a crowd order, a Floor Broker would have to be physically present. Upon leaving a crowd or logging out, a Floor Broker would be required to: (1) Cancel all crowd orders in the AEMI Book for securities in the crowd it is leaving; (2) electronically submit the orders in the form of percentage or limit orders to the Specialist for handling; or (3) electronically route the crowd orders to another Floor Broker in the crowd, via a hand-held terminal. In addition, as described in greater detail below, Floor Brokers would have exclusive use of percentage orders and reserve orders.

#### 4. Priority and Parity

As a general matter, the highest bid and the lowest offer shall have priority on AEMI.<sup>74</sup> Among orders and quotations at the same price, execution priority depends on a number of factors, including time priority, whether the order is public (*i.e.*, it is submitted the Specialist Book) or crowd (*i.e.*, it is represented by a Floor Broker in the crowd), whether it is a customer or broker-dealer order, and whether the order is deemed to be "in parity."

##### a. Parity Generally

Orders in parity are deemed to have been received by the AEMI system

<sup>70</sup> See Rule 110-AEMI(r).

<sup>71</sup> See Rule 110-AEMI(s).

<sup>72</sup> See Rule 110-AEMI, Commentary .02 and .03.

<sup>73</sup> See Amendment No. 4, at 6.

<sup>74</sup> See Rule 126-AEMI(1).

<sup>60</sup> See Rule 170-AEMI, Commentary .01.

<sup>61</sup> See Rule 170-AEMI, Commentary .02.

<sup>62</sup> Rule 170-AEMI, Commentary .03.

<sup>63</sup> See *id.*

simultaneously. Therefore, an order in parity generally cannot have time priority over another order in parity. By allowing later-arriving orders to be deemed in parity, Amex seeks to mitigate the effects of minute differences in processing time or latency between competing order routing systems. Parity can be established in the following circumstances:<sup>75</sup>

- If a bid (offer) in a security establishes a new highest bid (lowest offer), any bid (offer) in that security communicated to AEMI within two seconds of AEMI's receipt of the original bid (offer) shall be in parity with the original bid (offer) for the next trade.

- If AEMI effects a trade in a security, all visible bids and offers in that security at each price point shall be in parity for the next trade, as well as any bid (offer) in that security communicated to AEMI within two seconds of the original trade.

- If all bids (offers) at the APQ are canceled, all visible bids (offers) at each lower (higher) price point shall be in parity for the next trade, as well as any bid (offer) in that security communicated to AEMI within two seconds of the cancellation of the last remaining bid (offer).<sup>76</sup>

There are some exceptions to these rules for establishing parity. In ETFs, a broker-dealer (including the Specialist) whose order is in parity must yield to any customer order at the same price (regardless of whether it is a public or crowd customer order).<sup>77</sup> In equities, the Specialist whose order is in parity must yield to a public order at the same price, regardless of when the public order was entered into the AEMI system.<sup>78</sup>

#### b. Allocation Rules for ETFs

For a transaction in an ETF, all customer orders (regardless of whether they are crowd customer orders or public customer orders) will be filled ahead of all broker-dealer orders at the same price.<sup>79</sup> Any customer orders in parity will be filled ahead of any customer orders not in parity at that price. In determining the allocation for all in-parity orders, AEMI will count all of the crowd customer orders in parity at that price point, deeming all public customer orders in parity on the Specialist Order Book as a single crowd customer order for this purpose.<sup>80</sup> AEMI

will then allocate the remaining size of the aggressing order pro rata between the "crowd bucket" and the "public bucket." If there are multiple public customer orders in the public bucket, they will be filled from the allocation given to the public bucket in time priority.<sup>81</sup> In-parity crowd customer orders in the crowd bucket will be distributed pursuant to an "allocation wheel."<sup>82</sup> If any size remains to the aggressing order, any crowd customer orders and public customer orders not in parity will then be filled based on time priority.<sup>83</sup>

If any size remains to the aggressing order after any remaining customer orders have been filled, or if there were no customer orders to begin with, AEMI will give execution priority to crowd broker-dealer orders and public broker-dealer orders (including the Specialist's quote) in a manner similar to its handling of crowd customer order and public customer orders. However, if the Specialist quote is in parity with the broker-dealer orders, AEMI will first provide an allocation to the Specialist based on the following table set forth in Rule 126-AEMI(2)(d)(vi)(B):

Number of crowd participants	Specialist allocation (percent)	Crowd/Public allocation (percent)
1 .....	60	40
2-4 .....	40	60
5-7 .....	30	70
8-15 .....	25	75
16+ .....	20	80

Regardless of whether or not there are any customer orders, replenished reserve size will be executed after any visible size at that price. Any percentage orders elected by the trade event will have last priority at that price point.<sup>84</sup>

#### c. Allocation Rules for Equity Securities

For transactions in a non-ETF equity securities, execution priority under the AEMI rules depends to a greater extent on whether the order is crowd or public rather than, in ETFs, whether it is customer or broker-dealer. If there are no public orders, the crowd orders and Specialist quote could be in parity. Any such in-party orders would be distributed pursuant to an allocation wheel.<sup>85</sup> Any crowd orders or the

specialist quote not in parity would then trade based on time priority.<sup>86</sup>

If there are public orders, execution priority would depend on whether the public orders are in parity or not in parity, or whether some public orders are in parity and some not. If there are any public orders not in parity, the Specialist—even if its quote is in parity—will not receive any allocation until all public orders are filled.<sup>87</sup> For orders that are in parity, AEMI will divide the aggressing order into allocations for the "crowd bucket" and the "public bucket," similar to the process for ETFs. All of the public orders and the Specialist's quote together count as a single crowd order for purposes of this allocation.<sup>88</sup> For distribution within the public bucket, the Specialist quote must yield to all public orders, regardless of the Specialist's time priority.<sup>89</sup> Any orders not in parity, regardless of whether they are crowd orders or public orders, will be filled in time priority, with the exception of the not-in-parity Specialist quote, which must yield to all public orders regardless of time priority.<sup>90</sup> As with ETFs, replenished reserve size would be executed after any visible size at that price. Any percentage orders elected by the trade event would have last priority at that price point.<sup>91</sup>

#### 5. Order Types

Amex proposes to retain several of its current order types in AEMI, including market orders, limit orders, stop orders, stop limit orders, good-til-canceled orders, fill-or-kill orders, and immediate-or-cancel orders.<sup>92</sup> In addition, Amex would eliminate certain order types that exist in its current equity trading rules.<sup>93</sup> Amex also proposes to create, or modify, the following order types.

<sup>86</sup> See Rule 126-AEMI(2)(b)(i)(B).

<sup>87</sup> See Rules 126-AEMI(2)(b)(iii)(C) and 126-AEMI(2)(b)(iv)(C).

<sup>88</sup> See Rule 126-AEMI(2)(d)(ii)(A).

<sup>89</sup> See Rule 126-AEMI(2)(d)(ii)(B).

<sup>90</sup> See Rules 126-AEMI(2)(b)(iii)(B) and 126-AEMI(2)(b)(iv)(B).

<sup>91</sup> See Rule 126-AEMI(b).

<sup>92</sup> See Rule 131-AEMI.

<sup>93</sup> The AEMI system would not accept the following order types, although such orders would still be acceptable on the floor: not held orders, company buy-back orders in conformity with the safe harbor provisions of Commission Rule 10b-18, and stabilizing orders entered pursuant to Rule 104 of Regulation M in connection with purchases of a security in distribution. The following order types would no longer be permitted on the Exchange generally: "alternative" or "either/or" orders, "all-or-none orders," "good until a specified time" orders, "scale" orders, "switch" or "contingent" orders, "time" orders, and "G" orders.

<sup>81</sup> See Rule 126-AEMI(2)(d)(v)(B).

<sup>82</sup> See Rule 126-AEMI(2)(d)(vii). In general, the allocation wheel works by ranking the orders participating in the wheel in time priority. The system distributes round lots of the incoming order against the orders in the wheel through successive "rounds" until it is executed in full.

<sup>83</sup> See Rule 125-AEMI(2)(c)(i)(C).

<sup>84</sup> See Rules 126-AEMI(2)(c)(i) and 126-AEMI(2)(c)(ii).

<sup>85</sup> See Rule 126-AEMI(2)(d)(i).

<sup>75</sup> See Rule 126-AEMI(2)(a).

<sup>76</sup> However, priority and parity of orders on one side of the book shall not be affected by the cancellation of orders at the APQ on the other side. See Rule 126-AEMI(2)(a)(iii).

<sup>77</sup> See Rule 126-AEMI(2)(a)(iv)(B)(I).

<sup>78</sup> See Rule 126-AEMI(2)(a)(iv)(A)(I).

<sup>79</sup> See Rule 126-AEMI(2)(c).

<sup>80</sup> See Rule 126-AEMI(2)(d)(v)(A).

#### a. Electronic Cross Orders

The Exchange proposes to introduce the following types of electronic cross orders exclusively for ETFs and Nasdaq securities admitted to dealings on an unlisted basis: (1) Cross; (2) cross only; (3) mid-point cross; (4) IOC cross; (5) PNP cross; and (6) auction cross.<sup>94</sup> The electronic cross order type selected by the market participant would dictate whether the cross order could be broken up by orders on the AEMI Book, whether price improvement is being sought for the cross order, and how any residual of the cross order would be handled. For instance, “cross” and “cross only” orders are differentiated by their interaction with the book. A cross order could interact with orders in the AEMI Book at the cross price whereas a cross only order would not. Thus, if there were interest on the AEMI Book at the proposed price of a cross only transaction, AEMI would cancel the proposed cross.

An auction cross order would actively seek price improvement, and the sender of the order would designate which side (or sides) of the cross is eligible for price improvement. AEMI would display the selected side(s) for a three-second “Auction Cross Duration.” The side(s) of the cross selected for price improvement would be displayed one minimum trading increment worse than the proposed cross price (*i.e.*, the buy side of the cross must be displayed one tick below the proposed cross price and/or the sell side of the cross must be displayed one tick above the proposed cross price). During the three second Auction Cross Duration, the displayed order could be price improved by new bids, offers, or orders entering the AEMI Book. If the cross price is equal to or better than the automated NBBO and is between the APQ at the end of the Auction Cross Duration, AEMI would execute the auction cross at the cross price. If not, the order would be cancelled to avoid trading through the automated NBBO or at or through the APQ. If one or both sides selected for display were executed in part during the Auction Cross Duration, the unfilled balance would continue to be displayed and be executed at the end of the Auction Cross Duration at the cross price, so long as it continues to be equal to or better than the automated NBBO and between the APQ. Any remainder would be canceled at the end of the Auction Cross Duration unless the order were designated Cross and Post (“CNP”), in which case the unexecuted balance would be added to the AEMI

Book. If a side selected for display is executed in full during the Auction Cross Duration, the other side of the auction cross order would be canceled unless the order is designated CNP. AEMI would reject an auction cross order if the proposed cross price were at or outside the APQ or outside the automated NBBO.

#### b. Floor Crosses

A cross with size precedence<sup>95</sup> could not be broken up at the cross price by resting bids, offers or orders in the AEMI Book. In executing a cross trade by open outcry, members would be required to follow the crossing procedures set forth in Rule 152–AEMI (if a member or member organization is taking or supplying stock to fill a customer’s order) or Rule 151–AEMI (in all other situations). A clean agency cross, satisfying the size and value parameters in Commentaries .02 and .03 to Rule 126–AEMI, could not be broken up at the cross price by resting orders on the book. Only the member who executed the cross would receive a trade notification from AEMI in the event that the cross is not broken up at the cross price by the crowd (verbally) or by resting orders on the book.

#### c. Reserve Orders

AEMI would accept the reserve order, which is a limited price order submitted to AEMI by a Floor Broker standing in the crowd consisting of both a visible and an undisplayed (reserve) size.<sup>96</sup> The Floor Broker would specify the visible size of the order subject to a visible size minimum established by the Exchange. If the visible size of a reserve order is decremented, AEMI would replenish the displayed size from the order’s reserve quantity up to the lesser of the displayed size or the remainder of the reserve size. The reserve size would not be visible to market participants—and thus not would not be included in the APQ—but the cumulative reserve size at each price point would be visible to the Specialist. The Specialist would not be allowed to disclose reserve size in response to a market probe by a member or in response to an inquiry from a representative of the security’s issuer.

#### d. Hit or Take Orders

AEMI would have a “hit or take” order, which would trade against the APQ and could be entered by any member on or off the floor of the Exchange.<sup>97</sup> Members who wish to use the hit or take functionality must

specify the price and quantity of the hit or take order. A hit or take order would expire if not immediately executed, but unlike an IOC order it is capable of generating ISOs to clear better away markets before executing on the Exchange. A hit or take order could be specified as “sell short.”

#### e. Percentage Orders

AEMI would support percentage orders, which are limited price, day orders to buy (or sell) 50% of the Amex volume of a specified stock after entry into the Specialist Order Book.<sup>98</sup> Such orders may be entered only with “last sale” or buy-minus/sell-plus election instructions. Only a Floor Broker may enter a percentage order. A percentage order is a public order represented by the Specialist. For ETFs, a percentage order must be for a customer as opposed to a broker-dealer. Percentage orders would be executed after a “trade event” through “election” or “conversion.” Every execution due to an aggressing order is considered to be a trade event by AEMI. The elected portion of every percentage order would be executed immediately in whole or in part at the price of the electing transaction, or better. Any elected portion not so executed would revert to an unelected percentage order and could subsequently be elected or converted.

A percentage order could also be automatically converted into an IOC order or manually converted into either an IOC order (active manual conversion) or a regular limit order (passive manual conversion). Automatic conversions could occur during an opening, a re-opening, or the closing pair-off, and would be governed by conditions in the AEMI Book. The parameters triggering automatic conversions would be configurable. The automatically converted portion of a percentage order would be executed immediately, in whole or in part, at the price of the conversion, or better. Any portion not so executed would revert to its status as an unelected percentage order and be subject to subsequent election or conversion. The Specialist would manually convert percentage orders depending on the instruction on the percentage order. A manually converted percentage order would become an IOC order and immediately aggress the AEMI Book. A passive, manually converted percentage order would become a limit order at the APQ, and could set a new APQ or join the existing APQ.

Amex proposes to remove the current restriction requiring a 5,000 share

<sup>94</sup> See Rule 131–AEMI(r).

<sup>95</sup> See Rule 126–AEMI, Commentary .01.

<sup>96</sup> See Rule 131–AEMI(s).

<sup>97</sup> See Rule 131–AEMI(t).

<sup>98</sup> See Rule 131–AEMI(m).

minimum order size for certain conversions. Because the average trade size at the Amex is substantially less than 5,000 shares, Amex believes that eliminating this restriction would increase the execution opportunities for percentage orders.

#### 6. Trade Nullification and Revision

Rule 135–AEMI sets forth procedures for revising the terms of a transaction or cancelling it entirely if both parties agree to the revision or cancellation. A transaction may not be canceled or revised unless it was made in error or the cancellation or revision is made for another proper reason, and prior approval of the cancellation or revision is obtained from a Floor Official.<sup>99</sup>

The AEMI rules also provide that a Floor Official can cancel or revise a trade, even when one party does not agree to doing so, if the transaction is clearly erroneous.<sup>100</sup> The terms of a transaction are clearly erroneous when there is an obvious error in any term, such as price, number of shares or other unit of trading, or identification of the security. In reviewing a trade that is claimed to be clearly erroneous, the Floor Official shall have a view toward maintaining a fair and orderly market and the protection of investors and the public interest. A member of the Exchange's regulatory staff shall advise and participate in all steps of the Floor Official's review of the transaction. If the Floor Official determines to revise the terms of the transaction, he or she shall seek equitable rectification of the error that would place the parties in the same position, or as close as possible to the same position, as they would have been in had the error not occurred. The AEMI rules also set out procedural requirements for requesting review of a trade on the grounds that it is clearly erroneous and a procedure for appealing the Floor Official's determination.

#### 7. Policy Regarding Communication to and on the Floor

Amex has proposed to update its policy regarding communications to and on the floor in light of AEMI implementation.<sup>101</sup> These changes, among other things, would require Registered Traders to develop, or secure for use, hand-held terminals that would allow: (1) Communication of their bids and offers to AEMI; (2) execution of trades against orders in AEMI; and (3) notifications from the Specialist

regarding the Registered Trader's post-trade allocation. Members, their employees, and their approved persons would be required to maintain a record of each transmission to or from a hand-held terminal. In addition, members would be required to implement firewalls to ensure that inappropriate communications are not sent to the floor. All clock sources would be required to be synchronized to a Stratum-1 time source using millisecond increments. The Exchange would use industry standard radio frequencies for the wireless portion of the data communications infrastructure. Amex would eliminate the current restriction on image transmission through the data communications infrastructure.

#### 8. Carry-Over Rules

Rule 1A–AEMI(d) provides that, except to the extent governed by the AEMI rules or unless the context otherwise requires, the provisions of the Amex Constitution, the current Amex Rules, and the policies of the Board of Governors would be applicable to securities traded on AEMI. Rule 1A–AEMI(d) also expressly notes that certain current Amex rules would be applicable to trading on AEMI, including Rule 117 (relating to trading halts), Rule 190 (relating to Specialist transactions with public customers), and Rules 230 through 236 (relating to the ITS Plan). The following other rules, principally applicable to floor transactions, would continue to apply after AEMI is implemented: Rules 100, 101, 102, 103, 104, 105, 120, 122, 125, 128, 129, 153A, 171, 172, 173, 175, 176, 177, 183, 184, 185, 186, 191, 192, 193, 208, 221, and 222.

##### III. Amendment No. 6

In Amendment No. 6, Amex proposed the following:

- To replace an old Amex rule with a new Rule 24–AEMI to place limitations on proprietary trading by members and member organizations if the person entering the order has knowledge of an unexecuted customer order that could be executed at the same price;<sup>102</sup>

- To add Commentary .01, paragraph 1(b) to Rule 115–AEMI providing for the prompt disabling of auto-ex and the dissemination of a non-firm quote indicator if a Specialist or Registered Trader is unable to update its quotations on a timely basis due to a high level of trading activity or an unusual market condition;

- To amend Rule 126A–AEMI requiring the Exchange to identify all

trades executed pursuant to an exception or exemption from Rule 611 of Regulation NMS;

- To amend Rule 126A–AEMI providing that the Exchange may invoke “self-help” under Rule 611(a) of Regulation NMS, pursuant to objective industry-wide established interpretations and policies;

- To add Rule 126B–AEMI relating to agreements that govern the routing of orders to away markets;<sup>103</sup>

- To delete certain rule text in Rule 126–AEMI relating to the Specialist allocation table;

- To delete Commentaries .08 and .09 to Rule 170–AEMI;

- To make minor, technical or clarifying changes to Rules 115–AEMI, 118–AEMI, Rule 128A–AEMI, 128B–AEMI, 131–AEMI, 131A–AEMI, 170–AEMI (Commentary .02(b)), and 170B–AEMI;

- To make minor changes to Rule 128A–AEMI to clarify that members may not trade in the open outcry market but may enter and cancel bids, offers, and orders in AEMI under all six of the specified circumstances in the rule when auto-ex is unavailable; and

- To confirm that, during the period when the Specialist is performing a pair-off under the proposed AEMI rules, the Specialist has agency responsibility to orders on the AEMI Book and is subject to traditional agency obligations and to further confirm that, when the Specialist is performing a pair-off, the Specialist may participate at the pair-off price but only after all other orders at the pair-off price trade first and that participation by the Specialist is for the

<sup>103</sup> The Commission recently noticed another Exchange proposal to establish a modified initial version of AEMI that the Exchange expects to become operational prior to the Trading Phase Date. See AEMI–One Notice, *supra* note 54. The routing arrangements specified in the AEMI–One Notice are the same routing arrangements that the Exchange has described in Amendment No. 6, to which the Commission is granting accelerated approval. Thus far, the Commission has received one comment letter on the AEMI–One filing. See Letter to Nancy M. Morris, Secretary, Commission, from Michael A. Barth, Senior Vice President, Exchange and Market Centers, Order Execution Services, Inc., dated September 22, 2006. The commenter asserts that Amex will inappropriately perform duties required to be performed by a broker-dealer, such as making decisions on when, how, and where orders are routed. Rule 611(a) of Regulation NMS requires trading centers to adopt policies and procedures reasonably designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks displayed by other trading centers. In addition, an exception in Rule 611(b) requires that ISOs be routed to other market's better priced protected quotations. See Regulation NMS Release, 70 FR at 37501–02. The Exchange has developed its outbound routing functionality to facilitate its compliance with Regulation NMS. The Commission believes that the Exchange's arrangements for providing this functionality are consistent with the Act.

<sup>99</sup> See Rule 135–AEMI(a).

<sup>100</sup> See Rule 118–AEMI(k) (clearly erroneous transactions in Nasdaq securities); Rule 135A–AEMI (clearly erroneous transactions non-Nasdaq securities).

<sup>101</sup> See Rule 220–AEMI.

<sup>102</sup> The new Rule 24–AEMI is substantially similar to NYSE Rule 92.

purpose of absorbing the imbalance of shares that cannot participate in the pair-off.

#### IV. Discussion

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 and, in particular, with the requirements of Section 6(b) of the Act.<sup>104</sup> Specifically, the Commission finds that approval of the proposal is consistent with Section 6(b)(5) of the Act<sup>105</sup> in that the proposal is 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 Section 6(b)(8) of the Act,<sup>106</sup> which prohibits an exchange's rules from imposing a burden on competition that is not necessary or appropriate in furtherance of the Act. Finally, the Commission believes that the proposal is consistent with Section 11A(a)(1)(C) of the Act,<sup>107</sup> in which Congress found that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure: (1) Economically efficient execution of securities transactions; (2) fair competition among brokers and dealers and among exchange markets, and between exchange markets, and markets other than exchange markets; (3) the availability to brokers, dealers, and investors of information with respect to quotations and transactions in securities; (4) the practicability of brokers executing investors' orders in the best market; and (5) an opportunity for investors' orders to be executed without the participation of a dealer. This Order approves the proposed rule change, as amended, in its entirety, although only certain more significant aspects of the proposed rules governing AEMI are discussed below.<sup>108</sup>

<sup>104</sup> 15 U.S.C. 78f(b). In approving this proposal, the Commission has considered the proposed rules' impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>105</sup> 15 U.S.C. 78f(b)(5).

<sup>106</sup> 15 U.S.C. 78f(b)(8).

<sup>107</sup> 15 U.S.C. 78k-1(a)(1)(C).

<sup>108</sup> The Commission notes that certain of the proposed AEMI rules are substantially similar to existing Amex rules but with reasonable modifications for the new AEMI system. The Commission believes that these rules are reasonable and consistent with the Act. Some of these rules relate to the hours of business (Rule 1-AEMI; the authority of Floor Officials (Rule 3-AEMI);

#### A. Rules Designed To Comply With Regulation NMS Requirements

##### 1. Automated Quotations/Automated Trading Center

Amex has designed the AEMI system to display automated quotations and qualify the Exchange as an automated trading center under Rule 600(b)(3) of Regulation NMS.<sup>109</sup> Amex has stated that the visible size of the top of book for each security traded on AEMI will by default be marked as an automated quotation, and auto-ex will be the default state of operation. The AEMI platform will accept electronic bids and offers from both the Specialist and Registered Traders and include them in the AEMI Book. The AEMI platform also will accept Crowd Orders from Floor Brokers standing in the crowd and other off-floor orders transmitted to AEMI electronically, and file all such orders in the AEMI Book. On the basis of this input of bids, offers, and orders, AEMI will disseminate the Amex best quote, together with the associated visible size, to the tape. Members in the crowd can make verbal bids and offers, but these would have no standing in the AEMI Book. A trade negotiated on the floor could not be consummated until it were entered into the AEMI system.

Orders sent to the AEMI system will be processed immediately and automatically without human intervention, except in certain limited circumstances. As described in Section II(B)(1)(b) above, four of these situations involve trading circumstances that could otherwise result in price volatility in an individual security. Of the four trading situations, three relate to breaching predefined tolerance levels held within the system, namely "spread tolerance," "momentum tolerance," and a "gap trade tolerance." In the fourth circumstance ("gapping the quote"), the Specialist would manually take certain steps to address a large order imbalance. The fifth situation is the "cash close" for certain ETFs, and the sixth situation is when unusual market conditions (as defined in Rule 602 of Regulation NMS) occur.

The Commission believes that Amex's general approach to integrating auto-ex with a traditional floor is reasonable and

handling of odd lots (Rule 205-AEMI); and trade reporting (Rule 719-AEMI). Various rules relate to openings, closings, and states of operation, including: priority and parity at opening and reopenings (Rule 108-AEMI); trading in Nasdaq securities (Rule 118-AEMI); indications, openings, and reopenings (Rule 119-AEMI); manner of bidding and offering (Rule 123-AEMI); types of bids and offers (Rule 124-AEMI); and market-on-close policy and expiration procedures (Rule 131A-AEMI).

<sup>109</sup> 17 CFR 242.600(b)(3).

consistent with the Act. The Commission previously has found similar hybrid trading rules of another exchange, the NYSE, to be consistent with the Act.<sup>110</sup> The increased availability of auto-ex should facilitate the efficient execution of orders on the Exchange and enhance the opportunity for executions to occur without the participation of a dealer.

Amex believes that disabling auto-ex under certain specific and published circumstances—such as where market volatility results in a breach of a spread, momentum, or gap trade tolerance—would balance the demand for speed of execution with the need to provide a stable and fair marketplace. In such circumstances, no execution, automatic or manual, would be available, except to consummate an auction trade to remove a condition that caused auto-ex to be disabled.<sup>111</sup> NYSE's Hybrid rules contemplate the disabling of auto-ex in similar circumstances.<sup>112</sup> As the Commission stated in the NYSE Hybrid Approval Order, a hybrid market model—where auto-ex is disabled in limited circumstances to reduce market volatility—is within the realm of judgment generally left to the discretion of individual markets and is consistent with the Act.<sup>113</sup> Accordingly, the Commission finds that Amex's use of the "spread tolerance," "momentum tolerance," and "gap trade tolerance" in the context of the Amex's hybrid market is consistent with the requirements of the Act.

Amex's proposed rule regarding "gapping the quote" is similar to a rule on NYSE's Hybrid trading system.<sup>114</sup> Under the proposed rule, an Amex Specialist would gap the quote when either: (1) A large order has been represented in the crowd; or (2) an incoming order has swept the book, disabled auto-ex, and left a large order imbalance in the security.<sup>115</sup> Similar to NYSE, Amex has sought to ensure that a Specialist does not frequently enter gapped quotations for the purpose of disabling auto-ex by requiring that, when the Specialist gaps the quote, it must follow certain procedures and

<sup>110</sup> See Securities Exchange Act Release No. 53539 (March 22, 2006); 71 FR 16353 (March 31, 2006) ("NYSE Hybrid Approval Order").

<sup>111</sup> See Rule 128A-AEMI(f).

<sup>112</sup> See NYSE Rule 1000(a)(i)-(vi).

<sup>113</sup> See NYSE Hybrid Approval Order, 71 FR at 16377.

<sup>114</sup> See NYSE Rule 1000(a)(iv).

<sup>115</sup> Rule 170-AEMI(f) provides that the size of an imbalance suitable for gapped quoting must be at least 10,000 shares or a quantity of stock having a value of \$200,000 or more, although depending on the trading characteristics of the security, the appropriate conditions for gapped quoting may be higher.

consult with a Senior Floor Official or an Exchange Official to supervise the process.<sup>116</sup> As it noted in the NYSE Hybrid Approval Order, the Commission believes that this limited ability to disable auto-ex is a reasonable approach for addressing the practical difficulties of integrating orders on the electronic book with large orders on the floor and addressing large order imbalances generally.<sup>117</sup>

The Commission also believes that the other limited instances when auto-ex will be turned off are reasonable and consistent with the Act. Auto-ex would be disabled to allow the Specialist to perform a “cash close” pair-off during the regular trading session at 4 p.m., which would occur prior to the official closing session on the Exchange and would be an added service for those investors who wish to mark positions to the cash close.

When auto-ex is disabled, whether due to a breach of a tolerance or any of the other events that cause the AEMI to revert to a manual market, the Amex quote would not be an “automated quotation,” and thus not entitled to protection under Rule 611 of Regulation NMS. When this occurs, Amex also would be required under Regulation NMS to immediately identify its quotation as a manual quotation if it is to be considered an “automated trading center.”<sup>118</sup> When the Amex quotation is not available for automatic execution because of a breach of a tolerance or gapped quotation, Amex would identify such quotes as non-firm.<sup>119</sup> Specifically, Rule 123–AEMI(h) provides that: (1) Bids and offers disseminated through AEMI, such as when the Exchange is conducting an auction or when the Exchange is unable to accurately collect, process, and/or make available quotations under certain circumstances, are non-firm;<sup>120</sup> and (2) AEMI will disseminate a specified indicator<sup>121</sup>

<sup>116</sup> See NYSE Info Memo 04–27 (June 9, 2004) (specifying that the size of an imbalance suitable for gap quoting is at least 10,000 shares or a quantity of stock having a value of \$200,000 or more although, depending on the conditions, these levels could be higher).

<sup>117</sup> See NYSE Hybrid Approval Order, 71 FR at 16377.

<sup>118</sup> See 17 CFR 242.600(b)(4)(iii).

<sup>119</sup> See Notice, 71 FR at 41655. The Commission also notes that proposed Rule 115–AEMI addresses situations where Amex has reason to believe it is not capable of displaying automated quotations, including communicating to members its procedures concerning a change from automated to manual quotations. See Rule 115–AEMI.

<sup>120</sup> On the other hand, automated bids and offers disseminated through AEMI are firm until revised or withdrawn. Rule 123–AEMI(h).

<sup>121</sup> The Exchange has represented that it will use: (1) The indicator “N” to denote a non-firm quote when the Exchange is unable to accurately collect,

whenever the APQ is not firm. In addition, the Specialist is required by Rule 128A–AEMI to take steps to re-enable auto-ex and could be subject to discipline for not acting appropriately. The Commission believes that these rules are reasonably designed to minimize the frequency and length of auto-ex unavailability and are consistent with the Act. The Commission also believes that Amex’s procedures for marking its quotations as automated or non-firm are reasonable and consistent with the Act.

## 2. Means of Protecting of Protected Quotations

The AEMI platform and rules were designed to enable Amex to comply with Rule 611 of Regulation NMS, which requires, among other things, that the Exchange adopt and enforce written policies and procedures that are reasonably designed to prevent trade-throughs of protected quotations.<sup>122</sup> Therefore, when the APQ is not at the automated NBBO, AEMI would first determine whether a trade-through may nevertheless occur pursuant to one of eight enumerated circumstances stated in Rule 126A–AEMI.<sup>123</sup> If there is no applicable exception, AEMI would generate an ISO, consistent with the requirements of Rule 611 of Regulation NMS, to any trading center displaying better-priced protected quotations simultaneously with the execution of any transaction on Amex that would constitute a trade through.<sup>124</sup>

process, and/or make available quotations; and (2) the indicator “U” to denote a non-firm quote (and that the Specialist is arranging an auction) when (a) auto-ex has been disabled due to the breach of a tolerance, and auto-ex and the dissemination of an automated quotation have not yet resumed, or (b) a gap quote situation exists due to an order imbalance. These quote indicators are not to be confused with the indicators “A,” “B” and “H,” which are for firm quotes and denote that a trading center is not meeting the Regulation NMS definition of an automated trading center even though auto-ex is on. See Rule 123–AEMI(h).

<sup>122</sup> The Exchange has filed separate rules with the Commission for a modified version of the AEMI platform to be in effect during the roll-out period and prior to the Trading Phase Date. See Securities Exchange Act Release No. 54413 (September 7, 2006), 71 FR 54318 (September 14, 2006) (noticing SR–Amex–2006–72). Prior to the Trading Phase Date, the Exchange would still be required to comply with the applicable provisions of the ITS Plan unless and until appropriate exemptions are obtained.

<sup>123</sup> The Commission notes that each of these eight enumerated circumstances corresponds to one of the trade-through exceptions listed in Rule 611(b) of Regulation NMS.

<sup>124</sup> However, if the incoming order is designated IOC, AEMI would cancel it and not route it to another market. See Rules 126A–AEMI and 131–AEMI.

## a. Intermarket Sweep Orders

To implement the requirements of Rule 600(b)(30) of Regulation NMS,<sup>125</sup> the Exchange is adopting Rule 131–AEMI(k) that sets out the requirements for ISOs. An ISO is a limit order designated for automatic execution in an NMS stock that is: (1) Received on the Exchange by AEMI from a member or another market center which is to be executed: (a) Immediately at the time such order is received in the AEMI Book, (b) without regard for better-priced protected quotations displayed at one or more other trading centers, and (c) at prices equal to or better than the limit price, with any portion not so executed to be treated as canceled;<sup>126</sup> or (2) generated by AEMI in connection with the execution of an order by AEMI and routed to one or more trading centers to execute against all better-priced protected quotations displayed by the other trading centers up to their displayed size. An ISO would have to be marked as such to inform the receiving trading center that it could be immediately executed without regard to protected quotations in other markets. The Commission believes that Amex’s definition of ISO is consistent with the Act because it is reasonably designed to meet the requirements of Regulation NMS. The Commission notes that it previously approved similar provisions for ISOs.<sup>127</sup>

The rules governing the usage of ISOs are reasonably designed to meet the requirements of Rule 611 and, thus, are consistent with the Act. For example, Rule 126A–AEMI provides that the system would generate an ISO to any away market displaying a protected quotation simultaneously with the execution of a trade on Amex that would constitute a trade-through. Similarly, Rule 128A–AEMI(d) provides that an “[a]utomated execution will not occur without protected quotations in away markets being satisfied through the issuance of intermarket sweep orders” and proposed Rule 128B–AEMI includes provisions to generate ISOs to away markets.

## b. Routing of Orders

As described in Section II(B)(2)(e) above, Amex would enter into agreements that govern the routing of an order to away markets with automated quotations displaying better prices. Rule

<sup>125</sup> 17 CFR 242.600(b)(30).

<sup>126</sup> However, if an order is received through the communications network operated pursuant to the ITS Plan or any successor to the ITS Plan, the order would trade only at a single price. See Rule 131–AEMI(k).

<sup>127</sup> See, e.g., NYSE Hybrid Approval Order, 71 FR at 16383.

126B–AEMI describes the arrangement between the Exchange and a third-party non-facility provider of routing services. The Commission believes that engaging such a provider is a reasonable means of assuring compliance with Rule 611 of Regulation NMS. The Commission notes that the Exchange would retain control of the routing logic, which would help the Exchange assure compliance with Rule 611.<sup>128</sup> The Commission also notes that the rule provides for the establishment and maintenance of procedures and internal controls designed to protect confidential and proprietary information, which should help ensure that the third party does not use such information for purposes other than legitimate business purposes necessary for the licensing of routing technology. In addition, the rule provides for the equitable allocation of reasonable dues, fees, and other charges among Exchange members and issuers and other persons using the Exchange's facilities.

#### c. Self Help

Rule 611 of Regulation NMS protects only quotations that are immediately and automatically available and, as such, includes exceptions designed to assure that marketable orders are routed only to well-functioning trading centers displaying automated quotations. In this regard, Rule 611(b)(1) of Regulation NMS permits a trade through of a protected quotation if the trading center displaying the protected quotation were experiencing a failure, material delay, or malfunction of its systems or equipment when the trade-through occurred. The Commission stated in the Regulation NMS Adopting Release that this exception “gives trading centers a self-help remedy if another trading center repeatedly fails to provide an immediate response (within one second) to incoming orders attempting to access its quotes.”<sup>129</sup> The Commission believes that the self-help provisions of Rule 126A–AEMI—stating that the Exchange may, pursuant to objective, industry-wide established interpretations and policies and subject to certain conditions, bypass the quotations displayed by another trading center if such trading center repeatedly fails to respond within one second to orders attempting to access such trading center's protected quotations—is reasonably designed to allow Amex to invoke self-help in a manner consistent with Rule 611 of Regulation NMS. The Commission believes, therefore, that

these provisions are consistent with the Act.

#### d. Trade Reporting of Permissible Trade-Throughs

Following the Trading Phase Date, one provision of Rule 126A–AEMI would require the Exchange to identify all trades executed pursuant to an exception or exemption from Rule 611 in accordance with specifications approved by the operating committee of the relevant national market system plan.<sup>130</sup> This provision of Rule 126A–AEMI is designed to create uniformity across the markets regarding how permissible trade-throughs are reported, and should create more transparency for investors and regulators. The Commission believes, therefore, that this provision of Rule 126A–AEMI furthers the public interest and is consistent with the Act.

#### 3. Access Rule

Paragraph (a) of the Access Rule<sup>131</sup> prohibits a national securities exchange from imposing unfairly discriminatory terms that prevent or inhibit any person from obtaining efficient access through a member of the exchange to a quotation in an NMS stock displayed through the SRO quoting facility. The Commission believes that the AEMI rules and the AEMI platform have been reasonably designed to meet the standard in paragraph (a) of the Access Rule.

In addition, paragraph (d) of the Access Rule<sup>132</sup> requires a national securities exchange to establish, maintain, and enforce rules that generally require its members to avoid displaying quotations that lock or cross any protected quotation in an NMS stock and that are reasonably designed to assure the reconciliation of locked or crossed quotations in an NMS stock. Rule 128C–AEMI requires members of the Exchange, as of the Trading Phase Date of Regulation NMS, to reasonably avoid displaying, and to not engage in a practice of displaying, any quotations that lock or cross a protected quotation, and any manual quotations that lock or cross a quotation previously disseminated pursuant to an effective national market system plan, subject to certain limited exceptions.<sup>133</sup> The rule

<sup>130</sup> In addition, if a trade is executed pursuant to both the ISO exception of Rule 611(b)(5) or (6) and the self-help exception of Rule 611(b)(1), such trade shall be identified as executed pursuant to the ISO exception. See Rule 126A–AEMI.

<sup>131</sup> 17 CFR 242.610(a).

<sup>132</sup> 17 CFR 242.610(d).

<sup>133</sup> Prior to the Trading Phase Date, the Exchange would still be required to comply with the applicable provisions of the ITS Plan relating to locks and crosses, unless and until appropriate exemptions are obtained.

also requires that, if a member of the Exchange displays a manual quotation that locks or crosses a quotation previously disseminated pursuant to an effective national market system plan, the member must promptly either withdraw the manual quotation or route an ISO to execute against the full displayed size of the locked or crossed quotation. The Commission believes that this rule is consistent with Rule 610(d) of Regulation NMS.

#### 4. Sub-Penny Rule

Paragraph (a) of the Sub-Penny Rule,<sup>134</sup> among other things, prohibits an exchange from displaying, ranking, or accepting a quotation or order in any NMS stock priced in an increment smaller than \$0.01 if the quotation or order is priced equal to or greater than \$1.00 per share. If the quotation or order is priced less than \$1.00, the minimum permissible increment is \$0.0001.<sup>135</sup> The AEMI rules require quotations and orders above \$1.00 to be priced in increments of at least \$0.01 and quotations and orders below \$1.00 to be priced in increments of at least \$0.0001.<sup>136</sup> The Commission believes that the AEMI rules relating to minimum increments are consistent with the Sub-Penny Rule and consistent with the Act.

#### 5. Transitioning from Legacy System to NMS Environment

Amex intends a phased roll-out of AEMI beginning early in the fourth quarter of 2006. By the Trading Phase Date, all equities and ETFs traded by the Exchange would be on the AEMI platform. The Exchange has filed separate rules with the Commission for a modified version of the AEMI platform to be in effect during the roll-out period and prior to the Trading Phase Date.<sup>137</sup> The Commission believes that the Exchange's proposal for a phased roll-out of AEMI should provide it with time to test AEMI in a real trading environment with a limited number of securities. The Commission believes that this is a reasonable approach in light of the extension of the Regulation NMS compliance dates and should help ensure that the appropriate Amex rules are in place at the time that Regulation NMS compliance is required.

<sup>134</sup> 17 CFR 242.612(a).

<sup>135</sup> See 17 CFR 242.612(b).

<sup>136</sup> See Rule 127–AEMI; Rule 1000–AEMI, Commentary .03(e); Rule 1000A–AEMI, Commentary .02(e).

<sup>137</sup> See *supra* note 122. The Commission has not taken any action on this proposal.

<sup>128</sup> See *supra* note 103.

<sup>129</sup> See Regulation NMS Adopting Release, 70 FR at 37535.

### B. Other Rules

Amex has proposed a number of rule changes in addition to those designed to promote compliance with Regulation NMS. These other rule changes primarily reflect the Exchange's proposed shift from a floor-based auction market to a new hybrid market structure for equity products and ETFs.

#### 1. Liquidity Available for Auto-Ex

To facilitate automatic executions, the Exchange proposes to increase the ability of Specialists and, for ETFs, Registered Traders, to provide liquidity to the marketplace. In addition, the Exchange proposes to allow Floor Brokers to participate in automatic executions by permitting them to enter Crowd Orders, Reserve Orders, and Percentage Orders. In general, the Commission believes that allowing greater electronic access to liquidity is consistent with Section 6(b)(5) of the Act in that it should help perfect the mechanism of a free and open market.<sup>138</sup>

##### a. Specialist and Registered Trader Liquidity

A Specialist would be required to continue to provide liquidity to meet its obligation to assist in the maintenance of a fair and orderly market and of price continuity with reasonable depth. Under the proposal, Specialists and Registered Traders (in ETFs) can add liquidity to the AEMI Book at multiple price levels. Registered Traders also are permitted to participate in auctions, provided they are actively quoting. The Commission finds that the provisions allowing both Specialists and Registered Traders to electronically participate in AEMI is consistent with the requirements of the Act. This capability generally should increase the liquidity available for auto-ex and improve the prices at which orders that access the AEMI system may execute.

##### b. Floor Broker Liquidity

Under the AEMI rules, off-floor members are permitted access to the electronic environment by sending orders directly to the AEMI Book or by directing orders to booths on the floor for representation by a Floor Broker. Floor Brokers are permitted to provide liquidity to the electronic environment in the form of Crowd Orders. In addition, Floor Brokers standing in the crowd would be able to enter Reserve Orders on behalf of their customers—which would consist of both a visible size and an undisplayed (reserve) size that would not be included in the APQ.

As a Reserve Order receives executions, the displayed size would be replenished up to the maximum of the defined display size or the remainder of the order. A price point could not be traded through until all the reserve size has been exhausted. Amex also has proposed to allow Floor Brokers to use Percentage Orders.

The Commission previously approved substantially similar rules relating to Floor Brokers in the NYSE Hybrid proposal.<sup>139</sup> The Commission believes generally that Reserve Orders and Percentage Orders are consistent with the Act because they are designed to allow Floor Brokers to replicate in a more electronic environment the services they offer to customers today, and because they offer Floor Brokers a reasonable degree of flexibility in handling and working larger customer orders.

#### 2. Role of Specialists and Registered Traders

##### a. Generally

In AEMI, Specialists—and for transactions in ETFs, Registered Traders—will continue to be required to perform their obligations to maintain a fair and orderly market.<sup>140</sup> For example, pursuant to Rule 170–AEMI, a Specialist must trade for its own account when there is a lack of price continuity, depth, or a disparity between supply and demand. In addition, the Specialist must continue to oversee the auction market; pair-off orders at openings, closings, and the conclusion of auctions; and play an active role when large orders are routed to the floor for execution. However, Amex proposes to grant the Specialist additional flexibility in engaging in certain transactions in its specialty securities, without the need to obtain the prior approval of a Floor Official. Amex also proposes in Rule 110–AEMI to reduce some of the Registered Trader stabilization requirements.

The Commission finds that these proposed changes are consistent with the requirements of the Act in light of the evolving responsibilities of Specialists and Registered Traders to the market. Because of the AEMI system, Floor Brokers and off-floor members will be able to see order and quotation information at the same time as Specialists and Registered Traders, thereby diminishing many time and place advantages currently enjoyed by

the latter.<sup>141</sup> Amex has committed to make AEMI depth-of-book information broadly available, and intends to implement this program with the rollout of AEMI prior to the Trading Phase Date.<sup>142</sup> In addition, the expansion of auto-ex capabilities will provide market participants from off the floor much more efficient access to liquidity in AEMI. In light of these market structure changes, the Commission concludes that Amex's proposed revisions to certain of the stabilization requirements for Specialists and Registered Traders is reasonable and consistent with the Act.

##### b. Application of "Effect v. Execute" Exemption from Section 11(a) of the Act

Section 11(a) of the Act<sup>143</sup> prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises discretion (collectively, "covered accounts") unless an exception applies.<sup>144</sup> In addition to the exemptions set forth in the Act,<sup>145</sup> Rule 11a2–2(T)<sup>146</sup> under the Act, known as the "effect versus execute" rule, provides exchange members with an exemption from the Section 11(a) prohibition. Rule 11a2–2(T) permits an exchange member, subject to certain conditions, to effect transactions for covered accounts by arranging for an unaffiliated member to execute the transactions on the exchange. To comply with Rule 11a2–2(T)'s conditions, a member (i) Must transmit the order from off the exchange floor; (ii) may not participate in the execution of the transaction once it has been transmitted to the member performing the execution; (iii) may not be affiliated with the executing member; and (iv) with respect to an account over which

<sup>141</sup> However, Specialists will be the only market participants to have information regarding stop orders, percentage orders, and the aggregate size of reserve orders.

<sup>142</sup> In approving Amex's proposed stabilization rules, the Commission relied on the Exchange's representation that it intends to provide depth-of-book information to vendors and direct subscribers simultaneously with the first day of AEMI operation. Moreover, the Exchange commits to providing vendors and limited direct subscribers sufficient information including technical specifications to permit them to obtain the depth-of-book data feed as of the first day of AEMI operation. See Notice, 71 FR at 41655.

<sup>143</sup> 15 U.S.C. 78k(a).

<sup>144</sup> The Commission notes that Exchange members will no longer be able to enter "G" orders, *i.e.*, orders for covered accounts that rely on the exemption provided in Section 11(a)(1)(G) of the Act and Rule 11a1–1(T) thereunder, for an exemption from the restrictions set forth in Section 11(a) of the Act. See Rule 131–AEMI(u).

<sup>145</sup> 15 U.S.C. 78k(a)(1)(A) through (H).

<sup>146</sup> 17 CFR 240.11a2–2(T).

<sup>139</sup> See NYSE Hybrid Approval Order, 71 FR at 16378.

<sup>140</sup> See Rules 110–AEMI and 170–AEMI.

<sup>138</sup> 15 U.S.C. 78f(b)(5).

the member has investment discretion, neither the member nor its associated person may retain any compensation in the connection with effecting the transaction except as provided in the Rule.

The Exchange represented that it believes that transactions for covered accounts effected in the AEMI system meet the requirements of Rule 11a2-2(T).<sup>147</sup> Based upon these representations, and for the reasons set forth below, the Commission believes that transactions for covered accounts executed in the AEMI system satisfy the four conditions of Rule 11a2-2(T).

First, the Exchange stated that all orders sent to the Exchange for execution through AEMI will be transmitted from remote locations (via the member firm's interface) directly to the Exchange floor by electronic means.<sup>148</sup> The Commission has previously found that the off-floor transmission requirement may be met if a covered account order is transmitted from a remote location directly to an exchange's floor by electronic means,<sup>149</sup> and believes that orders sent to the Exchange for execution through AEMI from remote locations by electronic means (via the member firm interface)

similarly satisfy the off-floor transmission requirement.<sup>150</sup>

The second requirement of Rule 11a2-2(T) is that the exchange member and its associated persons may not participate in the execution of a transaction once the order has been transmitted to the exchange floor. The Exchange represented that orders submitted to AEMI will enter the queue and may be executed against a limit order on the Specialist's Book, or the account of a Registered Trader or Specialist. According to Amex, the execution of an order depends upon the other orders or quotes entered into AEMI at or around the same time as the subject order, the orders residing in the order book, and order ranking based upon the AEMI rules of precedence.<sup>151</sup> The Exchange stated that at no time following the submission of an order will a member retain any ability to control the timing of an execution or otherwise enjoy any special order-handling advantage.<sup>152</sup>

The third requirement of Rule 11a2-2(T) is that the order must be executed by an exchange member that is not affiliated with the initiating member. The Commission has recognized that this requirement is not applicable when automated systems are utilized.<sup>153</sup> Amex represented that orders delivered directly to AEMI by Amex members will be automatically matched, routed, or executed. The Commission notes that Amex members that direct orders to

Amex Floor Brokers for representation and execution in AEMI must use an unaffiliated Amex Floor Broker if they seek to rely on Rule 11a2-2(T) for an exemption from Section 11(a) of the Act.<sup>154</sup> Finally, the Exchange has represented that, as a prerequisite to the use of AEMI, if a member is to rely on Rule 11a2-2(T) for a covered account transaction, the member must comply with the limitations on compensation set forth in the rule.

### 3. Priority and Parity

#### a. Parity Joining Time

Amex has indicated that the "parity joining time" feature is intended to replicate in a more electronic environment the more flexible way that parity is established on the trading floor. The Commission believes that Amex's proposal to provide for a two-second parity joining time is broadly consistent with the Act and within the realm of judgment generally left to the discretion of individual markets.

#### b. Priority and Parity for Equities

The Commission believes that the proposed rules relating to order priority and order execution for non-ETF equities are consistent with the Act. The Commission notes that a Specialist's quotation must yield to any public order being represented in the Specialist Order Book. This approach is consistent with the traditional obligations of the Specialist and is consistent with the Act.<sup>155</sup> The priority and parity rules for equities appear to reasonably balance the interests of the various classes of market participants in a manner consistent with the Act. The Commission believes these rules are not designed to permit unfair discrimination and do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

#### c. Priority and Parity for ETFs

The Commission also believes that the AEMI rules relating to order priority and order execution for ETFs are reasonable and consistent with the Act. These rules require customer orders, whether represented on the book or in the crowd, to be executed before any broker-dealer orders (including orders/quotations of the Specialist and Registered Traders) at

<sup>147</sup> See Letter from Claire P. McGrath, Senior Vice President and General Counsel, Amex, to Kelly M. Riley, Assistant Director, Division, Commission, dated August 24, 2006 ("Amex Letter"); see also Amendment No. 6, *supra* note 9.

<sup>148</sup> See Amex Letter, *supra* note 147.

<sup>149</sup> See, e.g., Securities Exchange Act Release Nos. 29237 (May 24, 1991), 56 FR 24853 (May 31, 1991) (regarding NYSE Off-Hours Trading Facility); 15533 (January 29, 1979), 44 FR 6084 (January 31, 1979) (regarding the Amex Post Execution Reporting System, the Amex Switching System, the Intermarket Trading System, the Multiple Dealer Trading Facility of the Cincinnati Stock Exchange, the Pacific Exchange's ("PCX") Communications and Execution System, and the Philadelphia Stock Exchange's ("Phlx") Automated Communications and Execution System ("1979 Release")); and 14563 (March 14, 1978), 43 FR 11542 (March 17, 1978) (regarding the NYSE's Designated Order Turnaround System). See also Letter from Paula R. Jensen, Deputy Chief Counsel, Division, Commission, to Angelo Evangelou, Senior Attorney, Chicago Board Options Exchange ("CBOE"), dated March 31, 2003 (regarding CBOE's CBOEdirect system ("CBOEdirect Letter")); Letter from Paula R. Jensen, Deputy Chief Counsel, Division, Commission, to Jeffrey P. Burns, Assistant General Counsel, Amex, dated July 9, 2002 (regarding Amex's Auto-Ex system for options); Letter from Paula R. Jensen, Deputy Chief Counsel, Division, Commission, to Richard S. Rudolph, Counsel, Phlx, dated April 15, 2002 (regarding Phlx's AUTOM System and its automatic execution feature AUTO-X); Letter from Paula R. Jensen, Deputy Chief Counsel, Division, Commission, to Kathryn L. Beck, Senior Vice President, Special Counsel and Antitrust Compliance Officer, PCX, dated October 25, 2001 (regarding Archipelago Exchange ("ArcaEx")) ("ArcaEx Letter"); Letter from Brandon Becker, Director, Division, Commission, to George T. Simon, Foley & Lardner, dated November 30, 1994 (regarding Chicago Match ("Chicago Match Letter")).

<sup>150</sup> The Commission notes that Amex members off of the Exchange floor may submit proprietary orders directly into the AEMI system or may send proprietary orders to the Amex physical floor for representation by Amex Floor Brokers.

<sup>151</sup> See Amex Letter, *supra* note 147.

<sup>152</sup> See Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (Order approving ArcaEx as the equities trading facility of PCX Equities Inc.); 1979 Release, *supra* note 149. See also CBOEdirect Letter, *supra* note 149; Letter from Larry E. Bergmann, Senior Associate Director, Division, Commission, to Edith Hallahan, Associate General Counsel, Phlx, dated March 24, 1999 (regarding Phlx's VWAP Trading System); Letter from Catherine McGuire, Chief Counsel, Division, Commission, to David E. Rosedahl, PCX, dated November 30, 1998 (regarding Optimark); and Chicago Match Letter, *supra* note 149.

<sup>153</sup> For example, in considering the operation of automated execution systems operated by an exchange, the Commission noted that while there is no independent executing exchange member, the execution of an order is automatic once it has been transmitted into the systems. Because the design of these systems ensures that members do not possess any special or unique trading advantages in handling their orders after transmitting them to the exchange floors, the Commission has stated that executions obtained through these systems satisfy the independent execution requirement of Rule 11a2-2(T). See Securities Exchange Act Release No. 15533 (January 29, 1979). See also e.g., Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001).

<sup>154</sup> See Amendment No. 6, *supra* note 9. The Commission notes Amex members will not be able to rely on Section 11(a)(1)(G) of the Act. See Amex Rule 131-AEMI(u).

<sup>155</sup> The Commission notes that a Specialist bid (offer) in a non-ETF equity security would yield to a public bid (offer) even when AEMI receives the public bid (offer) outside the in-parity time window.

the same price, regardless of the customer orders' time priority. The Commission believes that giving priority to customer orders in this manner is consistent with the Act.

After all visible customer orders at a price are exhausted, Amex will allocate to the Specialist (if the Specialist quote is on parity with other broker-dealer orders), a percentage of the remaining order pursuant to an allocation table. The precise allocation granted to the Specialist will be based on the number of crowd participants. In view of the Specialist's obligations, such as maintaining a fair and orderly market, the Commission believes that this allocation methodology is broadly consistent with the Act and is within the realm of judgment generally left to the discretion of individual markets.

#### 4. Cross Orders

##### a. Electronic Crosses

Amex is introducing new electronic cross order types in order to provide more trading opportunities to off-floor participants in ETFs and Nasdaq securities. The electronic cross order type selected by the market participant would dictate whether the cross could be broken up by interacting with orders on the AEMI Book, whether price improvement is being sought for the cross order, and how any residual of the cross order would be handled if it is broken up. One new cross order type in particular, the auction cross, is designed to seek price improvement for one or both sides of the cross.

The Commission finds that the rules relating to electronic cross orders are consistent with the Act and should provide market participants additional flexibility in executing transactions while protecting displayed interest on the book. The auction cross order in particular would afford an opportunity for price improvement by allowing market participants to compete for one or both sides of the cross.

##### b. Floor Crosses

The Exchange proposes to continue to permit Floor Brokers to negotiate crosses in the crowd. Rule 126–AEMI, Commentaries .01 (Precedence Based on Size) and .02 (Clean Agency Cross) allow a cross to occur ahead of other orders on the book at the cross price if: (1) The cross order is valued at \$100,000 or more; (2) in the case of precedence based on size, the cross order is greater than each individual Crowd Order, as well as greater than the aggregate size of all orders on the Specialist Order Book at the cross price; and (3) in the case of a Clean Agency Cross, the size of the

cross order is greater than the largest customer order on the Specialist Order Book at the cross price.<sup>156</sup> The Commission believes that these provisions are consistent with the Act. The Commission notes that it previously has approved similar crossing rules of other exchanges, and Amex's crossing rules raise no new issues.<sup>157</sup>

##### 5. Unusual Markets Rule

The Commission believes that Rule 115–AEMI, setting forth Exchange procedures for the use of the Unusual Markets Exception provided by Rule 602 under Regulation NMS, is consistent with the Act. If the Exchange is unable to accurately collect, process, and/or disseminate quotation data in one or more securities owing to the high level of trading activity or the existence of unusual market conditions, Amex will immediately disable auto-ex and disseminate the indicator "N" to indicate that Amex's quotation, if a trading halt has not been declared and quotations are being published for such security or securities, is not firm. Similarly, if the Specialist were unable to update its quotation on a timely basis due to the high level of trading activity or the existence of an unusual market condition, it would be required to promptly notify a Floor Official and the Floor Official would notify Amex's Market Operations Division, which shall then promptly disable auto-ex and disseminate the indicator "N" to indicate that Amex's quotation, if a trading halt has not been declared and quotations are being published for such security or securities, if not firm. The Commission also believes that the procedures for declaring the existence of an unusual market condition are consistent with the Act in that these procedures appear to be reasonably designed to promote a fair and orderly market when unusual market conditions arise.

##### 6. Trade Nullification and Revision

The AEMI rules regarding nullification or revision of clearly erroneous trades<sup>158</sup> are generally similar to the Exchange's current rules. In addition, new Rule 118–AEMI(k) would permit the Exchange to nullify or modify a trade if the Exchange determines that the transaction is

<sup>156</sup> Rule 126–AEMI, Commentaries .01 and .02, retain the existing requirement that the cross order must be for 5,000 shares or more.

<sup>157</sup> See Securities Exchange Act Release No. 54391 (August 31, 2006), 71 FR 52836 (September 7, 2006) (approving SR–NSX–2006–08); Securities Exchange Act Release No. 54422 (September 11, 2006), 71 FR 54537 (September 15, 2006) (approving SR–CBOE–2004–21).

<sup>158</sup> Rules 118–AEMI(k) and 135A–AEMI.

erroneous as a result of the automatic execution of an order, bid, or offer by AEMI against an Amex quote that was not firm under one of the three exceptions to the firm quote requirement for bids and offers set forth in Rule 123–AEMI(h). The Commission believes that it is reasonable and consistent with the Act for an exchange to make transparent to its members the procedures for claiming that a trade is clearly erroneous, the standards for assessing such a claim, and the remedies available if the claim is substantiated. The AEMI rules also set forth procedures to be followed for the appeal of a determination made by a Floor Official or Floor Governor regarding such a claim.<sup>159</sup> These appeals procedures also are consistent with the Act as they should contribute to the trade nullification and revision procedures being exercised in a fair and reasonable manner.

##### C. Accelerated Approval

Pursuant to Section 19(b)(2) of the Act, the Commission finds good cause to approve the proposal, as amended by Amendment No. 6, prior to the thirtieth day after the amended proposal is published for comment in the **Federal Register**. Many of the changes in Amendment No. 6 are technical in nature and are intended only to make minor clarifications to the rule text. Other changes are designed to make AEMI more transparent and raise no issues of new regulatory concern. Accordingly, the Commission finds good cause to accelerate approval of the amended proposal prior to the thirtieth day after publication in the **Federal Register**.

##### V. Solicitation of Comments on Amendment No. 6

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 6, including whether the amendment is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR–Amex–2005–104 on the subject line.

##### Paper Comments

- Send paper comments in triplicate to Nancy M. Morris, Secretary,

<sup>159</sup> Rules 118–AEMI and 135A–AEMI.

Securities and Exchange Commission,  
100 F Street, NE., Washington, DC  
20549-1090.

All submissions should refer to File Number SR-Amex-2005-104. 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 (<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. 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 Number SR-Amex-2005-104 and should be submitted on or before October 31, 2006.

## V. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and in particular with Sections 6(b)(5) and 6(b)(8) of the Act.<sup>160</sup>

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>161</sup> that the proposed rule change (SR-Amex-2005-105), as amended by Amendments No. 1, 2, 3, 4, and 5, be, and it hereby is, approved, and that Amendment No. 6 is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>162</sup>

**Nancy M. Morris,**

Secretary.

[FR Doc. E6-16628 Filed 10-6-06; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54553; File No. SR-Amex-2006-91]

### Self-Regulatory Organizations; American Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to the Extension of the Pilot Period Applicable to the Listing and Trading of Options on the iShares MSCI Emerging Markets Index

September 29, 2006.

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 September 28, 2006, 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 prepared by the Exchange. The Amex has filed the proposed rule change, pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission.<sup>5</sup> The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange proposes to extend the pilot period applicable to the listing and trading of options on the iShares MSCI Emerging Markets Index Fund ("Fund Options"). The Amex is not proposing any changes to the rule text. 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, 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, 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 the places specified in Item IV below. The Amex 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 Statutory Basis for, the Proposed Rule Change

##### 1. Purpose

On May 17, 2006, the Commission approved the Amex's proposal to list and trade the Fund Options.<sup>6</sup> On June 30, 2006 the Commission approved a 90-day extension to the Pilot that is due to expire October 1, 2006.<sup>7</sup> The Fund Options will continue to meet substantially all of the listing and maintenance standards in Commentary .06 to Amex Rule 915 and Commentary .07 to Amex Rule 916. For the requirements that are not satisfied, the Exchange continues to represent that sufficient mechanisms exist that would provide the Exchange with adequate surveillance and regulatory information with respect to the Fund Options. Continuation of the Pilot would permit the Exchange to continue to work with the Bolsa Mexicana de Valores ("Bolsa") to develop a surveillance sharing agreement.

Accordingly, the Exchange proposes to extend the Pilot for an additional ninety days, until December 30, 2006.<sup>8</sup>

##### 2. Statutory Basis

The Amex believes the proposed rule change is consistent with Section 6(b) of the Act<sup>9</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>10</sup> in particular, in that it is 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; and is not designed to permit unfair discrimination between customers,

<sup>6</sup> See Securities Exchange Act Release No. 53824 (May 17, 2006), 71 FR 30003 (May 24, 2006) (SR-Amex-2006-43).

<sup>7</sup> See Securities Exchange Act Release No. 54081 (June 30, 2006), 71 FR 38911 (July 10, 2006) (SR-Amex-2006-60).

<sup>8</sup> Given that December 30, 2006 is a Saturday, the Commission notes that the Pilot will in effect be extended until January 2, 2007, the first business day after December 30, 2006.

<sup>9</sup> 15 U.S.C. 78f(b).

<sup>10</sup> 15 U.S.C. 78f(b)(5).

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

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

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

<sup>5</sup> The Exchange requested the Commission to waive the five-day pre-filing notice requirement and the 30-day operative delay, as specified in Rule 19b(f)(6)(iii). 17 CFR 240.19b-4(f)(6)(iii).

<sup>160</sup> U.S.C. 78f(b)(5) and 78f(b)(8).

<sup>161</sup> 15 U.S.C. 78s(b)(2).

<sup>162</sup> 17 CFR 200.30-3(a)(12).