

currently listed and traded on the Amex.¹⁸ Accordingly, the Commission finds that the listing and trading of the Notes based on the Index is consistent with the Act and will promote, among other things, just and equitable principles of trade and will facilitate transactions in securities, and, in general, protect investors and the public interest consistent with section 6(b)(5) of the Act.¹⁹

As described more fully above, at maturity, the holder of a Note will receive an amount based upon the percentage change of the Biotech Index. Specifically, at maturity, the holder of a Note will be entitled to receive a payment equal to three times the amount of that percentage increase, not to exceed a certain maximum payment, if the value of the Biotech Index has increased over the term of such Note. The Notes will provide investors who are willing to forego market interest payments during the term of the Notes with a means to participate or gain exposure to the Index, subject to a cap.

The Commission notes that the Notes are not-leveraged, non-principal protected instruments. The Notes are debt instruments whose price will be derived and based upon the value of the Biotech Index. The Notes do not have a minimum principal amount that will be repaid at maturity, and the payments of the Notes prior to or at maturity may be less than the original issue price of the Notes. Thus, if the value of the Biotech Index has declined at maturity, the holder of the Note will receive less than the original public offering price of the Note. Accordingly, the level of risk involved in the purchase or sale of the Notes is similar to the risk involved in the purchase or sale of traditional common stock. Because the final rate of return of the Notes is derivatively priced and based upon the performance of an index of securities, because the Notes are debt instruments that do not guarantee a return of principal, and because investors' potential return is limited by the Capped Amount, if the

value of the Biotech Index has increased over the term of such Note, there are several issues regarding the trading of this type of product. However, for the reasons discussed below, the Commission believes that the Exchange's proposal adequately addresses the concerns raised by this type of product.

The Commission notes that the Exchange's rules and procedures that address the special concerns attendant to the trading of hybrid securities will be applicable to the Notes. In particular, by imposing the hybrid listing standards, suitability, disclosure, and compliance requirements noted above, the Commission believes that the Exchange has addressed adequately the potential problems that could arise from the hybrid nature of the Notes. Moreover, the Commission notes that the Exchange will distribute a circular to its membership calling attention to the specific risks associated with the Notes. The Commission also notes that Merrill Lynch will deliver a prospectus in connection with the initial sale of the Notes. In addition, the Commission notes that Amex will incorporate and rely upon its existing surveillance procedure governing equities, which have been deemed adequate under the Act. Moreover, the Commission also notes that the Exchange has a general policy that prohibits the distribution of material, non-public information by its employees, which is necessary given Amex's role in selecting components and maintaining the Index.

In approving this product, the Commission recognizes, that Biotech Index is an equal dollar weighted index listed on Nasdaq, the NYSE and the Amex. The Commission notes that the Biotech Index is determined, calculated, and maintained by Amex. As of June 12, 2003, the market capitalization of the securities included in the Biotech Index ranged from a high of \$84.1 billion to a low of \$556.2 million. The average daily trading volume for these same securities for the last six (6) months, as of the same date, ranged from a high of 11.6 million shares to a low of 349,268 shares.²⁰

Given the relatively large trading volume and capitalization of the compositions of the stocks underlying the Biotech Index, the Commission believes that the listing and trading of the Notes that are linked to the Biotech Index, should not unduly impact the market for the underlying securities comprising the Biotech Index or raise manipulative concerns. As discussed more fully above, the underlying stocks comprising the Biotech Index are well-capitalized, highly liquid stocks. Moreover, the issuers of the underlying securities comprising the Biotech Index, are subject to reporting requirements under the Act, and all of the component stocks are either listed or traded on, or traded through the facilities of, U.S. securities markets. Additionally, the Amex's surveillance procedures will serve to deter as well as detect any potential manipulation.

Furthermore, the Commission notes that the Notes are depending upon the individual credit of the Issuer, Merrill Lynch. To some extent this credit risk is minimized by the Exchange's listing standards in section 107A of the Company Guide which provide the only issuers satisfying substantial asset and equity requirements may issue securities such as the Notes. In addition, the Exchange's "Other Securities" listing standards further require that the Notes have a market value of at least \$4 million.²¹ Furthermore, financial information regarding Merrill Lynch, in addition to the information on the common stocks comprising the Biotech Index, will be publicly available.²²

The Commission also has a systemic concern, however, that a broker-dealer such as Merrill Lynch, or a subsidiary providing a hedge for the issuer will incur position exposure. However, as the Commission has concluded in previous approval orders for other hybrid instruments issued by broker-dealers,²³ the Commission believes that this concern is minimal given the size

¹⁸ See Securities Exchange Act Release Nos. 47983 (June 4, 2003), 68 FR 35032 (June 11, 2003) (approving the listing and trading of non-principal protected notes linked to the S&P 500); 47911 (May 22, 2003), 68 FR 32558 (May 30, 2003) (approving the listing and trading of non-principal protected notes linked to the S&P 500); 46883 (November 21, 2002), 67 FR 71216 (November 29, 2002) (approving the listing and trading of non-principal protected notes linked to the DJIA); and 45305 (January 17, 2002), 67 FR 3753 (January 25, 2002) (approving the listing and trading of non-principal protected exchangeable notes linked to the Biotech-Pharmaceutical Index).

¹⁹ 15 U.S.C. 78f(b)(5). In approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

²⁰ As of June 12, 2003 the Biotech Index was composed of shares of the following companies: Affymetrix, Inc. (AFFX); Amgen Inc. (AMGN); Applera Corporation-Celera Genomics Group (CRA); Biogen, Inc. (BGEN); Cephalon, Inc. (CEPH); Chiron Corporation (CHIR); Enzon, Inc. (ENZN); Genentech, Inc. (DNA); Genzyme Corporation (GENZ); Gilead Sciences, Inc. (GILD); Human Genome Sciences, Inc. (HGSI); IDEC Pharmaceuticals Corporation (IDPH); Invitrogen Corporation (IVGN); Medimmune, Inc. (MEDI); Millennium Pharmaceuticals, Inc. (MLNM); Protein Labs, Inc. (PDLI) and Vertex Pharmaceuticals Incorporated (VRTX).

²¹ See Company Guide Section 107A.

²² The Commission notes that the component stocks that comprise the Biotech Index are reporting companies under the Act, and the Notes will be registered under section 12 of the Act.

²³ See Securities Exchange Act Release Nos. 44913 (October 9, 2001), 66 FR 52469 (October 15, 2001) (order approving the listing and trading of notes whose return is based on the performance of the Nasdaq-100 Index) (File No. SR-NASD-2001-73); 44483 (June 27, 2001), 66 FR 35677 (July 6, 2001) (order approving the listing and trading of notes whose return is based on a portfolio of 20 securities selected from the Amex Institutional Index) (File No. SR-Amex-2001-40); and 37744 (September 27, 1996), 61 FR 52480 (October 7, 1996) (order approving the listing and trading of notes whose return is based on a weighted portfolio of healthcare/biotechnology industry securities) (File No. SR-Amex-96-27).