

registered options trader to “engage \* \* \* in dealings for his own account when there exists a lack of price continuity, a temporary disparity between the supply of and demand for option contracts of a particular series, or a temporary distortion of the price relationships between option contracts of the same class.”<sup>10</sup> In addition, the Exchange has a proposal pending with the Commission to provide that specialists and registered options traders may not have priority over or be on parity with a public customer order.<sup>11</sup>

The Exchange believes the expansion of the EE Device for direct use by registered options traders and the adoption of rules requiring the allocation of trades to quote-improving registered options traders will substantially enhance incentives for registered options traders to quote competitively by providing for a means to by-pass the Auto-Ex system and the Auto-Ex allocation algorithm that may not reward the improving registered options trader and allow the allocation of trades to such registered options traders against quotes they caused to be disseminated.

#### **Integration of Automated Quote Dissemination and Trade Allocation**

The Exchange is in the process of developing a new integrated trading system that will replace many of its existing floor trading systems. Current systems, which include order routing, automated quotation calculation and dissemination, specialist “book” functions including limit order display, automatic order execution and allocation of trades are to be replaced by a fully integrated and automated system. The system will continue to have an “auto-quote” function similar to XTOPS, which would be made available to both the specialist and registered options traders for the inputting of competitive quotes. The auto-quote function would be available to registered options traders through their hand-held devices. Unlike XTOPS, the specialist’s auto-quote in a given option series would represent only the specialist’s trading interest. In order to enter quotes for dissemination through the Exchange’s Market Data System to the Options Price Reporting Authority, the registered options trader would be required to: (i) Be physically present in the trading crowd;<sup>12</sup> and (ii) disseminate

a quote for at least the minimum quote size. The required minimum size of the improved bid or offer would not be less than 10 contracts. The improved quotes would have an identifier so that orders executed against such quotes could be allocated automatically to the appropriate registered options trader.

The system, which would include algorithms established according to Exchange rules of priority and parity for customers, and the participation rights of registered options traders and specialists then in effect as set forth in Rule 950(d), Commentary .06, would automatically allocate executed trades to each market participant. It is anticipated that these algorithms together with Exchange rules would provide that: (i) When the specialist or registered options trader (price improver) is quoting alone at the best bid or offer, he would be automatically allocated 100% of incoming orders for as long as he is alone at the best bid or offer and up to his disseminated size; and (ii) if any other trading crowd participants subsequently join or match the initial price improver’s best bid or offer, contracts executed at that price would be allocated in accordance with rules of priority and parity then in effect.

It is currently anticipated that the Exchange will be able to begin its rollout of the new trading system during November 2003. In addition, it is anticipated that the rollout period could be a lengthy one. Since the system would not only be replacing systems in use today, different elements of the system would be used by every trading floor participant—specialists, registered options traders and floor brokers. The Exchange anticipates that the rollout will be completed by the first quarter of 2005. Once rolled out, the new system would be used for all option classes traded on the Exchange.

The Exchange believes that its initial step of expanding the use of the EE Device and its method for ensuring that trades executed at a registered options trader disseminated quote are properly allocated together with the development and implementation of a new integrated trading system that would automate and integrate all of these processes, would

the same side of the market. If the registered options trader leaves the trading crowd, he would be required to remove his quotes in all series. If the registered options fails to remove his quotes and an incoming order executes against one or more of those quotes, the registered options trader would not be able to participate in the trade. Unless, however, the system is unable to otherwise allocate the trade to other market participants at the same price, the registered options trader responsible for causing the quote to be disseminated would be assigned as contra-party to the incoming trade.

substantially enhance incentives to quote competitively and substantially reduce disincentives for market participants to act competitively. The Exchange believes that its customers would continue to benefit from instantaneous, automatic executions at the best available prices for option classes traded on the Exchange.

#### **2. Statutory Basis**

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act<sup>13</sup> in general and furthers the objectives of section 6(b)(5) of the Act<sup>14</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices and to promote just and equitable principles of trade.

#### **B. Self-Regulatory Organization’s Statement on Burden on Competition**

The Amex does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

#### **C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others**

No written comments were solicited or received with respect to the proposed rule change.

#### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Amex consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549—

<sup>10</sup> Amex Rule 958(c).

<sup>11</sup> See SR-Amex-2003-07.

<sup>12</sup> To reduce the possibility of remote market making, registered options traders would only be allowed to place one order or quote per series on

<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> 15 U.S.C. 78f(b)(5).