

Number of trades signed on to quick trade	Approximate number of trades allocated to the specialist	Approximate number of trades signed on to quick trade (as a group)
2	40%	60%
3-7	30%	70%
8 or more	25%	75%

(ii) Notwithstanding the foregoing, in the event the Exchange establishes a payment for order flow program, in which it collects a fee from the registered options traders, the rotation is designed to provide that the allocation of trades between the specialist and traders signed on to Quick Trade in a given option class is as follows:

Number of traders signed on to quick trade	Approximate [percentage] number of trades allocated to the specialist	Approximate [percentage] number of trades allocated to the traders signed on to quick trade (as a group)
1	60%	40%
2-4	40%	60%
5-7	30%	70%
8-15	25%	75%
16 or more	20%	80%

(e) through (p) No change.

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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 Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

On April 24, 2003, the Commission approved amendments to Amex Rules 933 and 950(d), codifying longstanding practices regarding the allocation of options contracts executed on the Exchange and, among other things, setting forth in Commentary .06 to Amex Rule 950(d) allocation ratios by which contracts are divided between registered options traders and

specialists on parity.⁴ In addition, on May 22, 2002, the Commission approved the implementation of Quick Trade, an automated allocation system activated for particular kinds of transactions that allocates trades between specialists and registered options traders using specific allocation ratios set forth in Amex Rule 950(d), Commentary .07.⁵ The Exchange is now proposing to revise the allocation ratios set forth in Amex Rule 933 and in Commentaries .06 and .07 of Amex Rule 950(d), as discussed below, in connection with the re-institution of an exchange-sponsored payment for order flow program.⁶

Recently, the Exchange re-instituted an exchange-sponsored payment for order flow program. The Exchange has traditionally opposed payment for order flow, believing, among other things, that it can create serious conflicts of interest and can compromise a broker's fiduciary obligation to achieve best execution of the broker's customers' orders. However, given the institution of payment for order flow programs at other options exchanges and the continuation of payment for order flow programs by some specialist and market making organizations, the Exchange believes that the re-institution of payment for order flow is necessary to respond to these competitive pressures. Amex represents that most specialists and registered options traders are fundamentally against the practice of payment for order flow, but they recognize its necessity, especially when specialists and market makers at other exchanges engage in the practice using either their own funds or funds provided by their exchange.

The Exchange's re-instituted payment for order flow program collects a marketing fee of \$0.40 per contract from both specialists and registered options traders. The Exchange represents that the marketing fee, however, will only be collected on those specialist and registered options trader transactions involving customer orders from firms that accept payment for directing their orders to the Exchange ("payment-accepting firms"). The Exchange also represents that the specialist is solely responsible for negotiating payment for order flow arrangements with payment-

accepting firms. Amex asserts that specialists would not be required to negotiate with any payment-accepting firms. Accordingly, the marketing fee would be assessed only on those specialist and registered options trader transactions resulting from orders from customers of payment-accepting firms with whom a specialist has negotiated a payment for order flow arrangement. Amex represents that the current payment for order flow program in place at the Exchange also allows registered options traders to vote to eliminate the program in select classes.⁷ The Exchange asserts that a vote to eliminate the marketing fee will result in registered options traders not contributing to the payment for order flow program in some option classes, which in turn will require the specialists in those classes to pay for order flow using their own funds. Amex represents that one issue of concern to the specialists is that, while they pay for order flow out of their own funds, the order flow that is received by the Exchange is shared with the registered options traders who will not be contributing to the payment for order flow program.

While specialists generally receive a larger share of order flow when on parity with registered options traders, the percentages and practices codified in Amex Rule 933 and Commentaries .06 and .07 of Rule 950(d) were established many years ago, and current payment for order flow practices had not been taken into consideration. Given the specialists' concerns, the Exchange has determined that a revision to the percentages set forth in these rules for those options classes in which the Exchange does not collect a payment for order flow marketing fee is appropriate. The Exchange has also determined that the percentages will vary depending on the type of option, whether equity option or option on an Exchange Traded Fund, Trust Issued Receipt, or index. The proposed revised percentages for equity options are set forth below:⁸

⁴ See Securities Exchange Act Release No. 47729 (April 24, 2003) 68 FR 23344 (May 1, 2003) (approving File No. SR-Amex-00-30).

⁵ See Securities Exchange Act Release No. 45974 (May 22, 2002) 67 FR 37886 (May 30, 2002) (approving File No. SR-Amex-2001-65). The allocation ratios in Commentary .07 to Amex Rule 950(d) are the same as those in Commentary .06.

⁶ See Securities Exchange Act Release No. 48053 (June 17, 2003), 68 FR 37880 (June 25, 2003) (File No. SR-Amex-2003-50).

⁷ See Securities Exchange Act Release No. 48577 (September 30, 2003), 68 FR 57943 (October 7, 2003) (File No. SR-Amex-2003-80). The Commission notes that Amex instituted the procedures by which specialists and registered options traders may determine whether to continue to participate in the payment for order flow program on a six-month pilot basis.

⁸ Amex is also proposing comparable revisions to the percentages for traders signed on to Quick Trade.