

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-41682; File No. SR-AMEX-99-13]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 to the Proposed Rule Change by the American Stock Exchange LLC Relating to Specialist Capital Requirements

August 2, 1999.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on April 2, 1999, 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, II, and III below, which Items have been prepared by the Amex. On June 11, 1999, and July 16, 1999, the Amex filed with the Commission Amendment Nos. 1 and 2 to the proposal.³ The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 1 revised the proposal to: (1) provide an example comparing the financial requirements for options specialists under the rules of the Amex, the Pacific Exchange ("PCX"), and the Chicago Board Options Exchange ("CBOE"); and (2) provide examples demonstrating the calculation of the capital requirements for joint equity/options specialists. See letter from Scott G. Van Hatten, Legal Counsel, Derivatives and Securities, Amex, to Richard Strasser, Division of Market Regulation ("Division"), Commission, dated June 10, 1999 ("Amendment No. 1"). Amendment No. 2 to the proposal provides two charts setting forth specialist financial requirements as of two dates in May 1999. See letter from Scott G. Van Hatten, legal Counsel, Derivatives and Securities, Amex, to Richard Strasser, Division, Commission, dated July 23, 1999 ("Amendment No. 2").

In addition, the Amex filed a letter describing financial safeguards applicable to specialists, including the clearing firm guarantee of specialists' transactions (for specialists who are not self-clearing), the Amex's daily review of each specialist's financial condition, and the procedures the Amex follows when the Exchange determines that a specialist is approaching the early warning financial requirements level (120% of the minimum specialist financial requirement). See letter from Scott G. Van Hatten, Legal Counsel, Derivatives and Securities, Amex, to Richard Strasser, Assistant Director, Division, Commission, dated June 10, 1999 ("June 10 Letter").

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

The Amex proposes to amend Amex Rule 950(h) to revise the financial requirements for options specialists. Specifically, the Amex proposes to amend Amex Rule 950(h) to provide that the minimum financial requirement for an options specialist will be \$600,000 plus \$25,000 for each option issue in excess of the initial ten issues in which the specialist is registered. In addition, the Amex proposes to revise Amex Rule 950(h), Commentary .01 to specify that for an option specialist that is also an equity specialist, the minimum financial requirement of \$600,000 specified in Amex Rule 171⁴ will apply to the entirety of the specialist's business, in both equities and options. Under Amex Rule 950(h), Commentary .01, as amended, the minimum financial requirement for an options specialist also serving as an equity specialist will be \$600,000, provided that the financial requirement for either the equity allocation or the options allocation does not exceed \$600,000. If the financial requirement for either the equity allocation or the options allocation exceeds \$600,000, then the specialist's financial requirement will be calculated by combining the financial requirement for equity specialists under Amex Rule 171 and the financial requirement for options specialists under Amex rule 950(h).

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

In its filing with the Commission, the 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.

⁴ Amex Rule 171, "Specialist Financial Requirements," requires every registered specialist to maintain a cash or liquid asset position in the amount of \$600,000 or an amount sufficient to assume a position of 60 trading units of each security in which the specialist is registered, whichever is greater.

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

1. Purpose

The Amex proposes to amend Amex Rule 950(h), which governs options specialist financial requirements. Currently, Amex Rule 950(h), which incorporates by reference the specialist financial requirements set forth in Amex Rule 171, requires that every registered options specialist maintain cash or liquid assets equal to the greater of \$600,000 or an amount sufficient to assume a position of 60 units of the highest priced puts and calls for each option in which the specialist is registered.⁵ Because the financial requirement is in some cases based on current market prices of puts and calls, it generally fluctuates from day to day. The Amex maintains that, with the recent increases in premiums for certain stock options, specialist financial requirements have increased dramatically beyond the level of risk associated with a specialist's market making activities. This situation occurs because the financial requirements for specialists do not take into consideration the extent to which specialists maintain hedged positions in their registered option issues.

The following charts provided in Amendment No. 2 illustrate the fluctuations in the capital requirement for an options specialist as calculated under current Amex Rule 950(h). Both charts are based on actual capital requirements for options traded on the Amex. The calculations in the first chart are based on premiums for six options as of the close of business on May 6, 1999, while the calculations in the second chart show the premiums for the same options as of the close of business on May 13, 1999. The charts demonstrate the effect that premium appreciation has on a specialist's minimum financial requirements. Specifically, because of the rise in premiums, the specialist's minimum capital requirement increased from \$882,750 in Week 1 to \$993,000 in Week 2.

⁵ The "cost to carry" 60 option contracts is determined pursuant to rule 15c3-1a(b)(2)(iii)(C) under the Act, 17 CFR 15c3-1a(b)(2)(iii)(C), which provides that a broker or dealer that is long puts or calls must deduct 50 percent of the market value of the net long put and call positions in the same options series.

WEEK 1

Option	CALL		PUT		Total
	Premium	Requirement	Premium	Requirement	
1	56 $\frac{3}{8}$	\$5,687.50 \times 60 / 2	67 $\frac{1}{4}$	\$6,725.00 \times 60 / 2	\$372,375
2	14 $\frac{1}{2}$	1,450.00 \times 60 / 2	7 $\frac{5}{8}$	762.30 \times 60 / 2	66,375
3	4 $\frac{1}{8}$	412.50 \times 60 / 2	17	1,700 \times 60 / 2	63,375
4	9	900.00 \times 60 / 2	5 $\frac{1}{4}$	525.00 \times 60 / 2	42,750
5	15 $\frac{1}{4}$	1,525.00 \times 60 / 2	5 $\frac{1}{4}$	525.00 \times 60 / 2	61,500
6	58 $\frac{1}{2}$	5,850.00 \times 60 / 2	33 $\frac{5}{8}$	3,362.50 \times 60 / 2	276,375
Total .....	.....	.....	.....	.....	882,750

WEEK 2

Option	CALL		PUT		Total
	Premium	Requirement	Premium	Requirement	
1	75 $\frac{3}{8}$	\$7,537.50 \times 60 / 2	55 $\frac{3}{4}$	\$5,575.00 \times 60 / 2	\$393,375
2	13 $\frac{7}{8}$	1,387.50 \times 60 / 2	16 $\frac{1}{8}$	1,612.50 \times 60 / 2	90,000
3	5 $\frac{1}{4}$	525.00 \times 60 / 2	22 $\frac{1}{4}$	2,225.00 \times 60 / 2	82,500
4	9 $\frac{1}{8}$	912.50 \times 60 / 2	8 $\frac{3}{8}$	837.50 \times 60 / 2	52,500
5	14 $\frac{7}{8}$	1,487.50 \times 60 / 2	8 $\frac{3}{8}$	837.50 \times 60 / 2	69,750
6	61 $\frac{3}{4}$	6,175.00 \times 60 / 2	39 $\frac{7}{8}$	3,987.50 \times 60 / 2	304,875
Total .....	.....	.....	.....	.....	993,000

Before the Amex's current specialist financial requirements took effect in June 1988, Amex rules required specialists to maintain cash or net liquid assets equal to the greater of \$100,000 or an amount sufficient to assume a position of 20 trading units of each speciality issue. As noted above, the Amex proposes to amend Amex Rule 950(h) to require every registered options specialist to maintain cash or liquid assets in the amount of \$600,000 plus \$25,000 for each option issue in excess of ten option issues in which such specialist is registered. Under the proposal, a specialist's financial requirement would not fluctuate with the premiums of the highest priced option series, but would change only when the specialist unit voluntarily changes the number of option issues it trades. The equity specialist financial requirements will remain at their current levels as set forth in Amex Rule 171.

The Exchange notes the existence of additional safeguards, such as circuit breakers, which became operative since the Exchange's last revision to Amex Rule 171.⁶ In addition, the Exchange's

daily review of specialist capital reserves and the Exchange's early warning signals, which trigger a more intense level of surveillance of exchange specialists during volatile market situations, continue to remain in place. Further, the proposal will permit options specialists to maintain relative control over their level of financial requirements by determining their respective number of options allocations.

As noted above, under the Amex's current rules, financial requirements for options specialists do not take into consideration the extent to which the specialists maintain hedged positions in their registered option issues. The Amex recently compared its financial requirements for options specialists to similar capital requirements maintained by other exchanges. In contrast to the Amex's capital requirements, the Exchange notes that a Lead Market Maker ("LMM") on the Pacific Exchange ("PCX") that performs the function of an

each day and contacts the specialist's principal(s) to request the deposit of additional funds on any day when the specialist approaches the early warning financial requirement level (120% of the minimum specialist financial requirement). If the specialist is unable to deposit additional capital, the Amex obtains a written guarantee from the specialist's clearing firm stating that the clearing firm will guarantee the specialist's transactions. The process of obtaining a written guarantee serves to notify the clearing firm of the specialist's current financial condition. Finally, the Amex notes that the Exchange may reallocate the specialist's allocation to another specialist unit if the specialist fails to satisfy the Amex's financial requirements. See June 10 Letter, *supra* note 3.

Order Book Official ("OBO") must maintain minimum net capital of \$500,000 plus \$25,000 for each issue over five issues for which the LMM performs the function of an OBO.⁷ An LMM that does not perform the function of an OBO must maintain minimum net capital of \$350,000 plus \$25,000 for each issue over eight issues that has been allocated to the LMM.⁸ Accordingly, to carry the same options book noted in the Amex's example above, an LMM that functions as an OBO in each of his options allocations would be required to maintain minimum net capital of \$525,000, while an LMM that does not function as an OBO would be required to maintain minimum net capital of \$350,000. The Exchange has also compared its current financial requirements for option specialists with those of the Chicago Board Options Exchange and the Philadelphia Stock Exchange. These comparisons have led the Amex to conclude that revisions to Amex Rule 950(h) are necessary.

In the Exchange's view, the cost for options specialists to maintain financial reserves sufficient to satisfy the Exchange's financial requirements has been increasing for Amex options specialists relative to competing options specialists or market makers at other exchanges. These financial requirements effectively reduce the number of option

⁶ The Amex's June 10 Letter describes additional safeguards relating to specialists' financial requirements. Among other things, the June 10 Letter notes that a specialist unit that is not self-clearing maintains an agreement with a clearing firm that guarantees the specialist's transactions. A specialist that is self-clearing guarantees the transactions effected by its specialists on the Amex floor. In addition, the June 10 Letter states that the Amex reviews all specialist financial requirements

⁷ See PCX Rule 6.82(h), Commentary .04.

⁸ See PCX Rule 6.82(c)(11).

issues that may be allocated to an Amex options specialist and provide an incentive for Amex members to consider moving their business operations to exchanges with less restrictive financial requirements. The Exchange believes that the proposed change is necessary to address any potential and significant increase in the number of option issues traded on the Exchange that may occur as a result of competitive marketplace conditions. The Exchange believes that the proposed change in the specialist financial requirements will help to ensure that Amex options specialists continue to maintain adequate capital reserves while remaining competitive with their counterparts at other exchanges.

The Amex also proposes to amend Amex Rule 950(h), Commentary .01, to specify the minimum capital requirement for a specialist that maintains a book in both equity securities and options ("an equity/option book"). Specifically, Amex Rule 950(h), Commentary .01, as amended, will provide that, for an options specialist also serving as an equity specialist, the minimum \$600,000 requirement specified in Amex Rule 171 will apply to the entirety of the specialist's business in both equities and options. The minimum financial requirement for a specialist with an equity/option book will be \$600,000, provided that the financial requirement for neither the equity allocation nor the option allocation exceeds \$600,000. Thus, under Commentary .01, the minimum financial requirement for a specialist who is allocated one equity issue and one option issue would be \$600,000, provided that the financial requirement for neither the equity allocation nor the options allocation exceeds \$600,000.⁹

For an equity/option book where the financial requirement of either the equity allocation or the options allocation exceeds \$600,000, the minimum financial requirement will be calculated by combining the equity and optional financial requirement (i.e., the financial requirements for equity specialists under Amex Rule 171 and the financial requirements for options specialists under Amex Rule 950(h)). For example, a specialist with three equity allocations and two options allocations, where the financial requirement for the three equity allocations exceeds \$600,000, would be required to maintain capital sufficient to assume a position of 60 trading units of each equity allocation plus \$50,000 for the two options allocations. Similarly, a

specialist allocated 11 options and one equity security would be required to maintain capital of \$625,000 for the 11 option allocations plus the amount required to assume a position of 60 trading units of the equity security.¹⁰ The Amex indicated that Commentary .01 is designed to encourage new specialist books.

2. Statutory Basis

The Amex believes that the proposed rule change is consistent with Section 6(b)(5) of the Act¹¹ 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 facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Amex does not believe that the proposed rule change will impose any inappropriate burden on competition.

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

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule change and Timing for Commission Action

Within 35 days of the 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 self-regulatory organization consents, the Commission will:

(A) By order approve the 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 proposal, as amended, is consistent with the act. Persons making written submission should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. 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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. SR-Amex-99-13 and should be submitted by August 30, 1999.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹²

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 99-20414 Filed 8-6-99; 8:45 am]

BILLING CODE 8010-01-M

DEPARTMENT OF TRANSPORTATION

Office of the Secretary

Aviation Proceedings, Agreements Filed During the Week Ending July 30, 1999

The following Agreements were filed with the Department of Transportation under the provisions of 49 U.S.C. 412 and 414. Answers may be filed within 21 days of date of filing.

Docket Number: OST-99-6027

Date Filed: July 27, 1999

Parties: Members of the International Air Transport Association

Subject:

PTC12 USA-EUR 0080 dated 2 July 1999

PTC12 USA-EUR 0085 dated 27 July 1999

Mail Vote 020—TC12 North Atlantic USA—Austria, Belgium, Germany, Netherlands, Scandinavia, Switzerland

Minutes—PTC12 USA-EUR 0084 dated 9 July 1999

Tables—PTC12 USA-EUR Fares 0037 dated 27 July 1999

Intended for effective date: 1 November 1999.

Docket Number: OST-99-6037

Date Filed: July 30, 1999

Parties: Members of the International Air Transport Association

Subject:

PTC COMP 0486 dated 30 July 1999
Composite Expedited Resolution 017d

⁹ See Amendment No. 1, *surpa* note 3.

¹⁰ *Id.*

¹¹ 15 U.S.C. 78f(b)(5).

¹² 17 CFR 200.30-3(a)(12).