prior to maturity only by selling the Notes in the secondary market. The Exchange anticipates that the trading value of the Notes in the secondary market will depend in large part on the value of the securities comprising the Index and such other factors as the level of interest rates, the volatility of the value of the Index, the time remaining to maturity, dividend rates, and the credit of the issuer.

The Notes will be subject to the equity margin rules of the Exchange. The Exchange will also distribute a circular to its membership prior to trading the Notes providing guidance with regard to member firm compliance responsibilities (including suitability recommendations) when handling transactions in the notes and highlighting the special risks and characteristics of the Notes.<sup>4</sup>

## The Index

The Notes will be linked to the Real Estate Index, a new index designed to reflect general movements in the underlying market for commercial real estate. The Index is calculated as a combination of the performance of two separate equity indexes: the REIT50 Index, which is a total return index comprised of 50 large, actively traded REITS; <sup>5</sup> and the Russell 2000 Index, which is a well-established capitalization-weighted broad-based index designed to track the performance of the small capitalization segment of the stock market.<sup>6</sup>

The Exchange represents that the method for calculating the value of the Index was developed based upon research that has demonstrated that the performance associated with an index of REITs may be attributed partly to movements in the underlying real estate market, and partly to the small capitalization nature of REIT stocks. Therefore, by subtracting a portion of the returns associated with a broadbased small capitalization stock index (such as the Russell 2000) from the returns generated by an index of REITs, the Exchange believes that an index can be generated that more closely reflects the performance of the underlying real estate market. Based on historical research and for purposes of simplicity,

$$I_{t} = 100 * \left( 1 + \left| \frac{(\text{RE50}_{t} - \text{RE50}_{\text{init}})}{\text{RE50}_{\text{init}}} - 50\% * \frac{(\text{R2000}_{t} - \text{R2000}_{\text{init}})}{\text{R2000}_{\text{init}}} \right| \right)$$

Where:

- RE50=REIT50 Index.
- R2000=Russell 2000 Index.
- Init=Indicates the level of the designated index as of the market close on the day prior to the start of trading of the Notes.
- t=Indicates the current level of the designated index.

The Index will be calculated continuously based on the most recently reported values of the REIT50 Index and the Russell 2000 and disseminated every 15 seconds over the Consolidated Tape Association Network B.

## Russell 2000 Index

The Russell 2000 is a well established benchmark index of the smallcapitalization segment of the U.S. equity market. Options on the Russell 2000 trade at the Chicago Board Options Exchange and futures trade at the Chicago Mercantile Exchange. The Russell 2000 is capitalization-weighted, and values are disseminated every 15 seconds to market vendors through the Option Price Reporting Authority. The value of the Russell 2000 does not reflect reinvestment of dividends paid on component stocks in the Index.

## **REIT50** Index

The REIT50 Index is a new capitalization-weighted index and, as discussed below, is a total return index. The Exchange represents that the REIT50 Index conforms with Exchange Rule 901C, which specifies criteria for inclusion of stocks in an index on which standardized options will be traded. The REIT50 Index is composed of the 50 largest publicly-traded equity REITs, as measured by market capitalization. The REIT50 Index will be maintained so that at each quarterly review, as discussed below, over the prior six-month period, the components of the Index will have had an average monthly trading volume of at least 400,000 shares with share prices greater than or equal to \$5 for the majority of business days during the preceding three calendar months.7 The REIT50 Index also does not and will not include health care REITs or REITs that invest

the Exchange has determined that the portion of small capitalization stock returns to be subtracted from the returns of the REIT50 Index will be set at a fixed level of 50% of the value of the Russell 2000.

The Index will initially be set at a level of 100 as of the market close on the day prior to the start of trading of the Notes. At any point in time, the Index value is calculated by multiplying the initial Index level (i.e., 100) by a factor determined as follows: First, the percentage change in the REIT50 Index from the market close on the day prior to the start of trading of the Notes is determined. Next, the percentage change of the Russell 2000 from the market close on the day prior to the start of trading of the Notes is determined. One half of the calculated percent change in the Russell 2000 is then subtracted from the calculated percent change in the REIG50 Index. This differential is added to the number one to yield the factor by which the initial Index level is multiplied to determine the current Index level. The following formula summarizes this calculation:

primarily in real estate mortgages or debt securities.<sup>8</sup> The REIT50 Index also will exclude real estate operating companies and partnerships.<sup>9</sup>

The Exchange will review the component securities on a quarterly basis to ensure that the REIT50 Index continues to represent only the largest and most actively traded REITs. After the close of trading on the last business day of December, March, June, and September, all eligible REITs will be ranked by descending market capitalization, and the 50 largest, subject to the maintenance criteria discussed above, will comprise the **REIT50** Index until the next quarterly review. Only REITs that have been trading for at least three calendar months will be considered for inclusion in the REIT50 Index. Resulting composition changes will be made after the close of trading on the third Friday of January, April, July, and October. The divisor of the REIT50 Index will be adjusted as necessary to ensure that there is no discontinuity in the value of

<sup>&</sup>lt;sup>4</sup> The Commission notes that the Amex will be required to submit a draft of the circular to the Commission staff for approval prior to distribution to members.

<sup>&</sup>lt;sup>5</sup> See Discussion of the REIT50 Index, *infra*.

<sup>&</sup>lt;sup>6</sup> See Discussion of the Russell 200 Index, infra.

<sup>&</sup>lt;sup>7</sup>Telephone conversation between Claire McGrath, Managing Director and Special Counsel,

Amex, and Brad Ritter, Senior Counsel, OMS, Division, Commission, on April 5, 1995.

<sup>&</sup>lt;sup>8</sup> Id.

<sup>9</sup> Id.