price will be used. Once all of the component stocks have opened for trading, the value of the Index will be determined and that value will be used as the final settlement value for expiring Index options contracts. If any of the component stocks do not open for trading on the last trading day before expiration, then the prior trading day's (*i.e.*, Thursday's) last sale price will be used in the Index calculation. In this regard, before deciding to use Thursday's closing value of a component stock for purposes of determining the settlement value of the Index, the Amex will wait until the end of the trading day on expiration Friday.23

G. Contract Specifications

The proposed options on the Index will be cash-settled, European-style options.24 Standard options trading hours (9:30 a.m. to 4:10 p.m. New York time) will apply to the contracts. The options on the Index will expire on the Saturday following the third Friday of the expiration month. Under Amex Rule 903C, the Exchange intends to list up to three near-term calendar months and two additional calendar months in three month intervals in the March cycle.²⁵ The Exchange also intends to list Index LEAPS having up to thirty-six months to expiration. Pursuant to the Amex's rules, strike price interval, bid/ask differential and price continuity rules will not apply to the trading of Index LEAPS until their time to expiration is less than twelve months.

The options on the Index will expire on the Saturday following Expiration Friday. Because options on the Index will settle based upon the opening prices of the component stocks on the last trading day before expiration (normally a Friday), the last trading day for an expiring Index option series will normally be the second to the last business day before expiration (normally a Thursday).

H. Listing of Long-Term Options on the Full Value or Reduced Value Broker/ Dealer Index

The proposal provides that the Exchange may list long-term index

options that expire from 12 to 36 months from listing on the full-value Tech 35 Index or a reduced-value Index that will be computed at one-tenth the value of the full-value Index. The current and closing Index value for reduced-value Tech 35 LEAPS will be computed by dividing the value of the full-value Index by 10 and rounding the resulting figure to the nearest onehundredth. The reduced-value Index LEAPS will also have a European-style exercise and will be subject to the same rules that govern the trading of all the Exchange's index options, including sales practice rules, margin requirements and floor trading procedures. The strike price interval for the reduced-value Index LEAPS will be no less than \$2.50 instead of \$5.00.

In addition, the Amex's rules provide that full-value or reduced-value Index LEAPS will be issued at no less than six month intervals and that new strike prices will either be near or bracketing the current Index value.

I. Position and Exercise Limits, Margin Requirements, and Trading Halts

Because the Index is a Stock Index Option under Amex Rule 901C(a) and a Stock Index Industry Group under Rule 900C(b)(1), the proposal provides that Exchange rules that are applicable to the trading of narrow-based index options will apply to the trading of options on the Index. Specifically, Exchange rules governing margin requirements,²⁶ position and exercise limits,²⁷ and trading halt procedures 28 that are applicable to the trading of narrowbased index options will apply to options traded on the Index. The proposal further provides that positions in full and reduced-value Index LEAPS will be aggregated with positions in regular Index options. For aggregation purposes, ten reduced-value contracts will equal one full-value contract.

J. Surveillance

Surveillance procedures currently used to monitor trading in each of the

²⁷ Pursuant to Amex Rules 904C and 905C, respectively, the position and exercise limits for the Index options will be 10,500 contracts, unless the Exchange determines, pursuant to Rules 904C and 905C, that a lower limit is warranted.

²⁸ Pursuant to Amex Rule 918C, the trading of Index options will be halted or suspended whenever trading in underlying securities whose weighted value represents more than 20% of the Index value are halted or suspended. Exchange's other index options will also be used to monitor trading in Index options and full-value and reducedvalue Index LEAPS. These procedures include complete access to trading activity in the underlying securities. Further, the Intermarket Surveillance Group ("ISG") Agreement, dated July 14, 1983, as amended on January 29, 1990, will be applicable to the trading of options on the Index.²⁹

Morgan Stanley has also adopted special procedures to prevent the potential misuse of material, non-public information by the research, sales and trading divisions of the firm in connection with the maintenance of the Index.³⁰ As discussed above, the stocks on each Replacement List are not eligible to be added to the Index by the Amex for a period of three months after receipt of the Replacement List by the Exchange. Moreover, the Amex has agreed to publicly disseminate each Replacement List by issuing information circulars so that investors will know in advance which securities will be considered as replacements for the Index.31

In addition, Morgan Stanley will have a limited role in the stock replacement selection and substitution process. First, when a stock in the Index no longer meets the published criteria as determined following a quarterly review of the components by the Exchange, the Amex will determine, without consultation with Morgan Stanley, which security from the applicable Replacement List will be selected for addition to the Index. Second, the Amex will also make adjustments as a result of stock splits, spin-offs, and otherwise, without consultation with Morgan Stanley. Finally, even in those situations where the Amex consults

³⁰ See Morgan Stanley Letter, supra note 18.
³¹ See Amendment No. 3, supra, note 6.

²³ For purposes of the daily dissemination of the Index value, if a stock included in the Index has not opened for trading, the Amex will use the closing value of that stock in its primary market on the prior trading day when calculating the value of the Index, until the stock opens for trading.

²⁴ A European-style option can be exercised only during a specified period before the option expires.

 $^{^{25}}$ See Amendment No. 3, supra note 6. With respect to Amex Rule 903C(b), the Exchange proposes to list near-the-money option series on the Index at $2^{1/2}$ point strike price intervals when the value of the Index is below 200.

 $^{^{26}}$ Pursuant to Amex Rule 462(d)(2)(D)(iv), the margin requirements for the Index options will be: (1) For each short options positions, 100% of the current market value of the options contract plus 20% of the underlying aggregate Index value, less any out-of-the-money amount, with a minimum requirement of the options premium plus 10% of the underlying Index value; and (2) for long options positions, 100% of the options premium paid.

²⁹ ISG was formed on July 14, 1983 to, among other things, coordinate more effectively surveillance and investigative information sharing arrangements in the stock and options markets. See Intermarket Surveillance Group Agreement, July 14, 1983. The most recent amendment to the ISG Agreement, which incorporates the original agreement and all amendments made thereafter, was signed by ISG members on January 29, 1990. See Second Amendment to the Intermarket Surveillance Group Agreement, January 29, 1990. The members of the ISG are: the Amex; the Boston Stock Exchange, Inc.; the Chicago Board Options Exchange, Inc.; the Chicago Stock Exchange, Inc.; the National Association of Securities Dealers, Inc.; the NYSE; the Pacific Stock Exchange, Inc.; and the Philadelphia Stock Exchange, Inc. Because of potential opportunities for trading abuses involving stock index futures, stock options, and the underlying stock; and the need for greater sharing of surveillance information for these potential intermarket trading abuses, the major stock index futures exchanges (e.g., the Chicago Mercantile Exchange and the Chicago Board of Trade) joined the ISG as affiliate members in 1990.