for example, may have access to, and be able to trade against and on the basis of, retail customer orders for multiply traded options classes and, in the event that complete segregation of stock and options trading is not required in the OTC markets, their underlying securities. In addition, these marketmakers may be able to trade with their customers without exposing their customer orders to other market participants and without being subject to exchanges auction trading rules affording limit order protection. 388/ Moreover, OTC options marketmakers may not be subject to the obligations that Commission and exchange rules impose upon options exchange marketmakers. 389/ Permitting dual market-making in the OTC markets without allowing comparable integration on exchange floors for multiply traded classes and their underlying securities may, of course, disadvantage options exchange marketmakers still further.

On the other hand, Congress considered a "healthy, highly competitive system of marketmakers" to be "essential to an efficient national market system" and stated that "encouragement should be given to all dealers to make simultaneous markets within the new national system." 390/

388/ See discussion at 168-173, supra.


390/ Senate Report, supra, n.17, at 14.
In addition, the 1975 Amendments require the Commission to assure "fair competition * * * between exchange markets and markets other than exchange markets" 391/ and "to refrain from imposing, or permitting to be imposed, any new regulatory burden on competition 'not necessary or appropriate in furtherance of the purposes' of the Exchange Act." 392/

3. The Integration of Trading of Options and Their Underlying Securities in the Over-the-Counter Markets

Dual marketmaking may be the only method of integrating the trading of options and their underlying securities in an over-the-counter environment. Accordingly, degrees of improvements in market quality or efficiency and the extent of trading integration may be less relevant when evaluating integration proposals pertaining to OTC markets than when evaluating exchange integration plans. 393/ Because the OTC markets are composed of numerous competing dealers, each of whom has exclusive access to, and knowledge of, some portion of any limit orders that may be present in the marketplace and each of whom may attract a significant portion of the orders for securities he is trading, considerations concerning the competitive position and the marketmaking system of the market

392/ Conference Report, supra. n.18, at 94.
393/ See discussion at 99-102, 122-125, supra.
center making a proposal to permit integration in the OTC markets may be less relevant. In all other respects, analysis of OTC market integration plans may be conducted within the same framework as those suggested for exchange plans: 394/ improvements in the quality of the markets for options and their underlying securities that might be derived from dual marketmaking must be balanced against the market information and competitive advantages that dual marketmakers may have over other market participants, additional incentives and opportunities for engaging in manipulative and other improper trading practices that may be created, and increased difficulties in conducting adequate market surveillance that may result.

Three more specific points should be kept in mind when evaluating OTC integration proposals. First, the absence of real-time last sale reporting for underlying securities traded exclusively in the OTC markets, the use of representative bid and ask quotations for underlying securities and their related options, and the ability to trade with, and on the basis of, customer stock and option orders and inquiries may provide OTC dual marketmakers with market information and competitive advantages and opportunities to engage in improper trading activities that exceed those of other OTC market participants. Second, the fact that market

394/ See discussion at 139-142, supra.
surveillance in the OTC markets is, of necessity, based exclusively upon accurate time-stamping and reporting of transactions by NASDAQ marketmakers may make OTC market surveillance difficult. Because trading takes place in the offices of market professionals and transaction reports may not be subject to independent verification by a self-regulatory organization employee or official, the members of a trading crowd, or a price reporting system controlled by the NASD or an exchange, the precision needed to identify the times that stock and options transactions occurred may not be obtainable, and it may be relatively simple to disguise improper trading to avoid detection. Finally, the extent and nature of any marketmaking obligations and the ease with which NASDAQ dual marketmakers may enter and suspend quotations should be considered in connection with any OTC dual marketmaking proposal.

While the 1975 Amendments contemplated that the "competitive structure and incentives" to engage in marketmaking activities in a national market system "should supplement, and ultimately may be able to replace, most affirmative requirements to deal imposed by regulation" 395/ and directed the Commission "to refrain from imposing * * * any new regulatory burden on competition 'not necessary or appropriate in furtherance of the purposes' of the Exchange Act," 396/ the Commission

396/ Conference Report, supra, n.18, at 94.
may wish to satisfy itself that an OTC options market will be sufficiently liquid on a regular basis so that it "does not 'fold up' when the pressure on dealers becomes too heavy." 397/

VI. THE NEW YORK STOCK EXCHANGE AND STANDARDIZED OPTIONS TRADING

The New York Stock Exchange submitted a plan in June, 1977 to permit the trading of standardized options on the NYSE floor. 398/ NYSE proposed to implement an options trading system which would be similar to that of the CBOE. Under the NYSE Plan, OCC would be the issuer and primary obligor of option contracts listed on NYSE. The marketmaking function on the NYSE floor would be performed by competing options marketmakers. As on all options exchanges utilizing a competing marketmaker system, the transactions of each marketmaker would be required to be "reasonably calculated to contribute to the maintenance of a fair and orderly market," and no marketmaker would be permitted to "enter into transactions or make bids of offers that [would be] inconsistent with such a course of dealings." 399/ The marketmakers also would be subject to trading

397/ Special Study, supra, n.63, at 15.
398/ NYSE Plan, supra, n.5.
399/ NYSE Plan, Proposed Rule 757(f). See also, CBOE Rule 8.7(a); MSE Article XLVII, Rule 6(a); PSE Rule VI, Section 79(a). In addition, with respect to each class of options in which he would have been (footnote continued on next page)
rules analogous to those on other options exchanges utilizing a competing
marketmaker system. Limit orders would be handled and executed by
Order Book Officials employed by the exchange, and such Officials
would not be permitted to trade for their own accounts.

NYSE proposed to commence its options program by listing options on
twenty-five underlying securities. NYSE indicated that many of these
underlying securities are listed and traded on NYSE and that it intends
to list classes and series of options, including puts, that are already
listed and traded on one or more option exchanges. In fact, NYSE has
stated:

[A]ny new entrant into the options business must be able
to list and trade existing options classes if it is to
attract sufficient investor interest to justify the cost

(footnote continued)

registered, each NYSE options marketmaker would have had "a continuous
obligation to engage, to a reasonable degree under the existing
circumstances, in dealings for his own account when there exists,
or it is reasonably anticipated that there will exist, a lack of
price continuity, a temporary disparity between the supply of and
demand for a particular option contract, or a temporary distortion
of the price relationship between option contracts of the same class."
NYSE Plan, Proposed Rule 757(f). See also CBOE Rule 8.7(b); MSE
Article XLVII, Rule 6(b); PSE Rule VI, Section 79(b). The NYSE
Plan also would permit "competitive traders" to trade options for
their own accounts on the NYSE floor. When present in a trading
crowd or called upon by a floor official of the NYSE, a competitive
trader would have marketmaking obligations identical to those of
an NYSE options marketmaker. NYSE Plan, supra, n.5, Proposed
Rule 758(c).
of establishing and maintaining an efficient, effectively regulated options market. ** Apart from the obvious inequity in any approach that would exclude the NYSE from listing and trading standardized options that are traded on one or more other exchanges, it would not be economically feasible for the NYSE to limit its options trading program exclusively to options on securities which are not subject to options trading elsewhere. The most attractive securities for options trading have already been selected by the existing options exchanges. 400/

Most of the NYSE options would be traded in a room physically separated from the NYSE equity trading floor by a ceiling-high solid wall. Since the options room, however, would not have contained sufficient space for the trading of options on all twenty-five underlying securities, NYSE planned to convert one post in the main equity trading room to an options trading post. NYSE represented that no option would be assigned to the options post in the main equity trading room if the underlying stock would also be traded in that room. The NYSE Plan, however, did not contain provisions which would restrict NYSE stock specialist and registered stock marketmaker access to the NYSE options trading floor, or NYSE options marketmaker access to the NYSE stock floor. Moreover, the Plan did not contain provisions which would restrict NYSE stock specialists and registered stock marketmakers from trading options on the NYSE floor. 401/

400/ NYSE Letter, supra, n. 85, at 7.

401/ Proposed NYSE Rule 757 would prohibit a registered NYSE options marketmaker from trading other securities on the NYSE floor. Proposed NYSE Rules 105 and 758, however, would permit NYSE stock specialists

(footnote continued on next page)
Since the NYSE Plan contemplated an expansion of multiple trading of standardized options and a greater degree of integration of trading of options and their underlying securities than presently exists, the concerns and considerations previously set forth with respect to these two subjects should be taken into account when evaluating this, or any similar, proposal. 402/ The predominant position of NYSE in the markets for underlying securities, however, may intensify some of these concerns and place some of these considerations in different perspective than multiple trading and integration proposals that other exchanges may submit. This section will discuss the extent and nature of NYSE dominance in the markets for underlying securities and the impact that this dominance may have upon the factors that should (footnote continued)

to trade options with respect to their specialty stocks and NYSE registered stock marketmakers to trade options for their own account. See Securities Exchange Act Release No. 12924, supra, n.224, and discussion at 144-148, supra. See also Letter to George A. Fitzsimmons, Secretary, Securities and Exchange Commission, from James E. Buck, Secretary, NYSE, dated July 13, 1978. More specifically, the NYSE Plan did not contain provisions prohibiting (i) the partners or associates of an NYSE options marketmaker from trading underlying securities, or being a stock specialist on the NYSE floor, (ii) the partners or associates of a registered stock specialist from becoming a "competitive trader" and trading options with respect to a specialty stock, or (iii) a registered stock marketmaker, or his partners or associates, from acting as an options marketmaker or competitive options trader.

402/ See Parts III and IV of this chapter, supra.
be considered in connection with an evaluation of an NYSE proposal to begin standardized options trading.

A. The Predominant Position of the New York Stock Exchange in the Markets for Underlying Securities

1. NYSE Market Share

In 1977, NYSE accounted for 79 per cent of the share volume and 84 per cent of the dollar volume for securities traded on exchanges. 403/ AMEX, by contrast, was responsible for 9.3 per cent of share volume and 4.6 per cent of the dollar volume during the same year. 404/ In addition, NYSE accounted for 85.8 per cent of the volume of all trading in stocks listed on NYSE in that year. 405/ By comparison, NYSE's nearest competitor for multiply listed stocks captured less than 5 per cent of the consolidated share volume for these stocks. 406/

All but two of the 218 stocks that are currently subject to standardized options trading are listed on NYSE. Further, "NYSE is considered

   404/ Id.
   405/ Id., at 35.
   406/ NYSE, 1977 Annual Report of the Quality of Markets Committee, Exhibit E. See also CBOE Letter, supra, n.87, at Table A. A copy of this table is provided as Table 22.
the 'primary market' for each of them," 407/ and accounts for a mean of 86.4 per cent of the consolidated share volume in these stocks. 408/ CBOE also estimates that "approximately 440 stocks currently meet Commission-approved criteria for standardized options trading" and that NYSE is the "primary market for all but two of them," attracting more than 80 per cent of the mean proportion of dollar and share volume and number of trades on each of these stocks. 409/

In light of these data, there is little doubt that NYSE is "by far the dominant market in the securities industry and has achieved an overwhelming concentration of trading in practically all of the underlying stocks which are eligible for exchange options trading." 410/

2. NYSE Financial Resources

As a result of this predominant position among exchange markets and markets for NYSE-listed stocks, NYSE has revenues and resources at its disposal which exceed those available to other exchanges. Total NYSE

408/ Letter to Richard Weingarten from James W. Fuller, supra, n.293.
409/ CBOE Letter, supra, n.87, at 30 and Table B. A copy of CBOE's Table B is provided as Table 23. See also AMEX Letter, supra, n.90, at 12.
410/ AMEX Letter, supra, n.90, at 3.
revenues in 1977, for example, were $118,962,000 and pre-tax income was $10,747,000. 411/ Total AMEX revenues were $36,801,000 and pre-tax income was $1,246,000 during the same year. 412/ CBOE, by contrast, had total revenues of $12,295,000 during 1977 and a pre-tax loss of $580,000. 413/ PHLX, on the other hand, the smallest of the options exchanges in terms of revenues had $4,978,000 in total revenues and $132,000 in pre-tax income in that year. 414/ Similarly, NYSE had total assets of $107,465,000 in 1977 whereas AMEX had total assets of $26,996,000, CBOE of $23,331,000, and PHLX of $30,514,000. 415/

Thus, it is clear that NYSE has "vastly superior financial resources" relative to all other exchanges. 416/

411/ Staff Report on the Securities Industry in 1977, Directorate of Economic and Policy Research, Securities and Exchange Commission, (May 22, 1978), Exhibit 22. It should be noted that NYSE maintains that its total revenues are $87,132,000 and that its revenues before taxes are $9,451,000. NYSE Letter, supra, n.85, at 14. See also CBOE Letter, supra, n.87 at Table C. This table contains comparative financial information for selected self-regulatory organizations and is provided as Table 24.

412/ Id.

413/ Id.

414/ Id.

415/ Id.

416/ AMEX Letter, supra, n.90, at 20.
3. NYSE Marketmaking Resources

NYSE specialists have accumulated resources which exceed those of marketmakers on other exchanges. While the exact amount of capital available to such firms "is rather difficult to pinpoint because it may change significantly within rather short periods of time and because many of such firms may employ their capital in different lines of business," NYSE has estimated that the combined buying power of its 62 specialist units at December 31, 1977 was $738,000,000. Further, the total equity capital of 61 NYSE firms classified as primarily engaged in marketmaking and trading was between $430,000,000 and $520,000,000 during most of 1976 and 1977.

Although such figures are not precisely comparable, equity figures that the Options Study derived with respect to the cleared accounts of options marketmakers provide a basis for placing these NYSE marketmaking resources in perspective. For example, the equity in such accounts on all exchanges was $81,172,000 and $84,310,000 on December 31, 1976 and 1977 respectively. More specifically, the equity in such accounts on

417/ AMEX Letter, supra, n.90, at 22.
420/ See Chapter VII, Exhibit E, Table 1.
CBOE was $53,963,000 and $45,784,000 and on AMEX was $23,301,000 and $34,524,000 on these dates. 421/

Additional resources are also available to NYSE specialists. As CBOE has observed:

The power of NYSE's specialists is compounded by the fact that some of them control a large number of books. For example, the largest NYSE specialist firm makes markets in 132 common stocks (8% of the total number listed on the NYSE) and the next largest makes markets in 72 common stocks. Further, many of the larger specialist firms clear books other than their own. This control over numerous books gives the NYSE specialist firm a further competitive advantage in any multiple trading contest in a particular security, since it is in a position to attract order flow in the multiply-traded security by offering discounts on brokerage in its other securities and/or in the multiply-traded security itself. 422/

4. Additional NYSE Resources

NYSE has other resources that may contribute to, be responsible for, and result from its position as the nation's predominant securities market. AMEX, for example, has pointed out:

To fully appreciate the significance of the NYSE's dominance of the securities markets it is necessary to understand *** the relationship between the NYSE and its member firms, its listed companies and ultimately the nation's investors.

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421/ Id., at Tables 2 and 3.

422/ CBOE Letter, supra, n.87, at 34-35 (footnote omitted).
Most brokerage firms of any significant size have their execution capability centered on the NYSE. This involves more than just personnel, although clearly most firms do have their largest complement of brokers and support personnel located on the floor of the NYSE. Internal communications networks and sophisticated order routing systems have largely been designed with an eye to transmitting orders to and obtaining information from the NYSE floor. Operational and post-trade procedures of brokerage firms are largely oriented to NYSE requirements and systems. The NYSE has attracted to its floor the largest and by far the most highly capitalized corps of market makers.

Nearly 450 of the "Fortune 500" industrial companies are listed on the NYSE. The prominence of the NYSE has been attractive to many companies that have grown and sought to achieve greater national recognition. Over the past forty years, in excess of 60 companies traded on the Amex have transferred to the NYSE. It has been the Amex's experience that such transfers were not normally motivated by dissatisfaction with the market for their securities on the Amex but rather that they expected to gain added recognition through the broader exposure given by the financial press to NYSE companies and to achieve greater prestige by being listed on the nation's most prominent exchange.

The prominence of the NYSE market and its listed securities serves to sustain and strengthen its dominance of the securities markets. NYSE stock tables receive much broader exposure in the financial press than those of any other exchange. Its securities have a much greater following among registered representatives and analysts. Many investors, particularly institutions, focus their investment interest exclusively on NYSE listed
securities and often invest all or substantially all of their funds in such securities. * * *

Perhaps no private institution in this country plays as influential a role in its particular area of the economy as that of the NYSE in relation to the securities industry. 423/

Similarly, CBOE has pointed out that NYSE "possesses various intangible resources" which it has developed over the years, 424/ stating:

[T]he NYSE is the prime beneficiary of the "primary market" concept. This term is not merely descriptive of the dominance in stock trading that the NYSE has achieved; it also contributes heavily to that dominance, since, * * * in the absence of the facilities and rules of a truly competitive national market system, customer order flow is generally directed to the market that is regarded as "primary" and thereby reinforces that status.

Having grown and prospered over a long period in a monopoly environment, the NYSE has gathered a large and powerful membership, which accounts for the overwhelming preponderance of the brokerage business in equity securities in the United States. * * *

In addition, the NYSE long ago established, and has insisted on maintaining, primary self-regulatory authority over all its member firms, regardless of their size, location, other activities or other self-regulatory memberships. Under Rule 17d-1 and the plans that have been filed under Rule 17d-2, the NYSE is the designated examining authority for virtually all of its member firms, even though many are also members of other exchanges. 425/

423/ AMEX Letter, supra, n.90, at 9-14 (emphasis in original) (footnotes omitted).

424/ CBOE Letter, supra, n.87, at 31.

425/ Id., at 31-32 (footnotes omitted).
B. Potential NYSE Predominance of the Standardized Options Markets

The predominant position of NYSE in the markets for underlying securities may provide it with competitive advantages that the options exchanges do not possess and may substantially assure that NYSE would come to be the predominant options market in the long run. These advantages will be discussed in this section and should be kept in mind in connection with any proposal to permit the trading of options on the NYSE floor that NYSE may submit.

1. NYSE and the Primary Market Designation

NYSE is the primary market for virtually all stocks traded on its floor. In 1977, for instance, NYSE attracted more than 90 per cent of the consolidated share volume in approximately 70 per cent of its multiply traded stocks, and captured more than 70 per cent of the market in all but 4 per cent of its issues. 426/ As a result, NYSE may be "automatically considered by a large part of the exchange community to be the primary market in practically all securities that become listed there, regardless of the quality or depth of market that may be made elsewhere." 427/

In this regard, AMEX has stated:

426/ NYSE, 1977 Annual Report of the Quality of Markets Committee, Exhibit E. See Table 22.

427/ AMEX Letter, supra, n.90, at 17-18 (footnote omitted).
Brokerage firms and investors alike who have traditionally identified the NYSE market with the securities of most major corporations that are the subject of options trading will most likely transfer that primary market identification to the options as well. The great prominence and prestige of the NYSE as well as the vast influence that it exercises over the securities industry will tend to reinforce this strong predilection towards its market. 428/

2. NYSE Facilities Advantage

Because most brokerage firms do a substantially higher volume of business on NYSE than on any other exchange, most of these firms have their execution capability and personnel "centered" on NYSE. 429/ Similarly, their internal communications networks and order routing systems are "oriented to the NYSE market." 430/ This "concentration of personnel and facilities," as AMEX has pointed out, may represent "a very substantial commitment by [NYSE] member firms to the NYSE market and [may] serve as an almost irresistible force in attracting options order flow to that exchange at the expense of other markets." 431/ Along the same lines, CBOE has noted:

The NYSE [may] be likely to obtain order flow benefits from the fact that over the years the securities industry has concentrated resources in New York for stock trading

428/ Id., at 16.
429/ Id., at 18.
430/ Id.
431/ Id.
which also could be used to handle options business; most member firms have more floor members and more staff on the floor of the NYSE than elsewhere; and many firms have developed close relationships with NYSE specialist units and their personnel. Further, many NYSE floor members, who are influential in member firms controlling substantial order flows, would have both the incentive and frequently the power to direct their firms' options order flow to the NYSE. 432/

3. NYSE Advantage With Respect to Combined Orders

As the primary market for virtually all underlying securities, NYSE may have a distinct advantage when competing to attract orders that necessitate the purchase or sale of an option and a simultaneous transaction in its related stock. For example, because the price of the option portion of these "combined orders" will depend in large part upon the price of the underlying stock at the time that the option order is entered, brokers executing such orders may be more likely to obtain the best prices available for both parts of the order if they can evaluate market conditions for both securities on the exchange floor that is likely to determine the price of the underlying stock. In addition, it may be more economical for a brokerage firm to send a combined order to one floor broker and one exchange floor rather than

432/ CBOE Letter, supra, n.87, at 39.

433/ See discussion at 209-210, 216, supra.
to two, as is now the case. Should such economies exist, the most likely floor to receive the order may be the primary stock exchange floor because stock prices, and, as a result, options prices, are likely to be most accurately assessed there. In this connection, AMEX has observed:

If the market center which is considered the primary market for the underlying stock is also able to provide a market for the option as well, it will have a very significant advantage in attracting both sides of the order. This will not only give the NYSE an added edge over any competing market center in seeking options order flow but also will help to further entrench its already overwhelming position of dominance in the area of equities trading. Other exchanges will be unable to effectively compete for this type of order even if they do provide a market in both the option and the underlying stock because experience demonstrates that most firms send the equity order to the primary market (the NYSE) and, therefore, the option order is likely to be sent there as well. 434/

4. NYSE Financial Resources

NYSE's superior financial resources and revenue flow 435/ may also provide NYSE with a competitive advantage over other options exchanges. Its accumulated capital may enable NYSE "to far out-spend other exchanges in an effort to initiate and promote its options program." 436/

434/ AMEX Letter, supra, n.90, at 19-20.
435/ See discussion at 210-212, supra.
436/ AMEX Letter, supra, n.90, at 20.
addition, NYSE’s income flow from stocks and other securities may
"provide the means for subsidizing the operation of its options market
and permit the charging of fees below those of other exchanges in an
effort to win order flow." 437/

AMEX and CBOE have noted the competitive advantages that NYSE’s sub-
stantial financial resources may provide. AMEX illustrated these advantages
with the following example:

["The NYSE plan provides for the use of "order book
officials" who will be exchange employees and who
will be responsible for maintaining the limit order
books in options, executing agency orders left on
the books by brokers, quoting the markets, and in
general controlling the trading crowds. The NYSE
can, if it chooses, compensate its order book
officials out of funds derived from existing
sources of revenue and charge minimal fees (or
no fees at all) for the services which they
perform. These services on most other exchanges
are performed by members who must charge a fee
to cover their expenses and make a reasonable
profit. Even if other options exchanges were
to adopt the "order book official" concept, few,
if any, would have existing revenue sources which
could be used to subsidize the providing of such
services, and would, therefore, have to impose
fees sufficient to cover the cost of providing
the services. If the NYSE determined to adopt
this competitive scheme, the lower cost of executing
options transactions (particularly limit orders)
on its floor would provide it with a formidable
advantage over other exchanges, an advantage
which would surely result in the re-direction
of order flow to its floor. 438/"

437/ Id.

438/ Id., at 20-21.
Similarly, the CBOE has stated:

[T]he NYSE would start an options program with a capital base and revenue flow derived from its dominant position in stock trading that competing exchanges could not hope to match. The increasing importance of very costly automated systems in order handling and market surveillance would be likely to make this great disparity in resources decisive in any future competitive struggle. For example, the NYSE might well be able to avoid assessing a user charge for any new order handling system (or to impose a much lower charge) by directly or indirectly subsidizing the capital and operational costs with revenues derived from its stock market. In contrast, competing options exchanges, which depend on transaction fees as their major source of revenue, would likely have to impose charges for the use of such systems.

The NYSE could also use its unmatched financial resources in a variety of less obvious but equally anticompetitive ways. For example, the NYSE and its floor members would undoubtedly seek *** to obtain experienced options personnel, trained at the expense of other options exchanges and their floor members, by offering inducements that the latter would be financially unable to match. 439/

5. NYSE Marketmaking Resources and Advantages

The financial resources of NYSE stock specialists and market-makers 440/ may contribute to, and ultimately become, the competitive

439/ CBOE Letter, supra, n.87, at 38. See also discussion at 227-229, infra.

440/ See discussion at 212-213, supra.
advantage of an NYSE options market. To the extent that NYSE stock
marketmaking resources are allowed to be used in connection with NYSE
options marketmaking activities, \textsuperscript{441} NYSE options marketmakers may
have access to financial resources which would exceed those available
to options marketmakers on other exchanges.

In this regard, AMEX has observed:

The vast financial resources of NYSE floor-oriented firms could be used in several ways to
wage competitive warfare. For example, substantial amounts of capital and marketmaking talent could
be concentrated in specific options where the competitive battle was most intense. Once the
redirection of order flow had resulted in the NYSE floor being recognized as the primary market
for those particular options, the capital and marketmaking capability could be focused on another
group of options. One by one, or group by group, the NYSE floor would become the dominant market in the
options it chose to list, and once it achieved primary market designation in an option, experience demonstrates
it would be nearly impossible for any other exchange to dislodge it.

The "flocking" of market makers to the areas where
competition is the most intense would not require formal agreements or even oral understandings. It would be
very apparent to the NYSE market makers that by concentrating their efforts and sacrificing immediate
rewards, the resulting flow of business once that market had been established as dominant in options
would be immensely rewarding to all. If individual market makers on different exchanges had roughly
comparable amounts of financial resources and no

\textsuperscript{441} See discussion at 207, and n.401, supra.
exchange had any overriding advantages such as those described above, then this kind of "pull and tug" would be considered the very essence of competition. However, given the magnitude of the resources available on the NYSE floor, combined with the many other advantages which can be brought to bear by the NYSE in the competitive fray, it is very likely that the countermeasures by market makers on other exchanges to retain order flow would prove in the long run to be largely ineffectual. 442/

More generally, CBOE has pointed out that revenues that NYSE stock market-makers generate from their stock trading may be used to "temporarily [subsidize NYSE options marketmaking] at below-cost pricing levels or to maintain minimal spreads between bid and offer so as to enable the NYSE to attract order flow," 443/ and that NYSE stock specialists who also perform clearing functions may be able to provide capital and credit resources to NYSE options marketmakers whose accounts they clear exceeding those available to other options marketmakers. 444/

It must also be kept in mind that virtually every stock traded on NYSE is assigned to a unitary specialist who has combined dealer and agency functions and essentially exclusive control of and access to the limit order book for that stock. Further, specialist firms may control the limit

442/ AMEX Letter, supra, n.90, at 24-25.
443/ CBOE letter, supra, n.87, at 38.
444/ Id., at 39.
order books for numerous stocks. 445/ Accordingly, there may be "temptations and opportunities" for NYSE stock specialists and other market participants to engage in "reciprocal practices" designed to attract options order flow to the NYSE floor. 446/ NYSE stock specialists, for example, may be able to "give brokerage discounts with respect to their specialty stocks to induce customers to bring their options orders to the NYSE's options floor." 447/

Finally, two other significant marketmaking advantages may accrue to NYSE marketmakers in an NYSE options market as a result of NYSE's predominant position in the markets for underlying securities. CBOE described these advantages as follows:

Effective market-making in options depends on the use of stock positions to hedge options positions. An options market-maker who has access to the stock

445/ See n.422 and accompanying test, supra.
446/ CBOE Letter, supra, n.87, at 40.
447/ Id., at 38-39. In this connection, CBOE stated:

For example, according to published reports, during recent competition between the NYSE and the AMEX concerning a particular stock, the NYSE specialist discounted its brokerage fee by 25% in that stock and all 29 of the other stocks in which it made markets, and a number of brokerage firms directed their order flow to the NYSE rather than the AMEX (on which the stock had previously been solely listed) as a result.

Id., at 35.
market on a cheaper or more efficient basis than a competing market-maker enjoys a substantial competitive advantage. Further, information as to market activity and developments on the NYSE stock floor is of much greater utility in options trading than is comparable information as to any other stock floor. As NYSE market-makers or other traders move back and forth between its options and stock floors—a practice which does not appear to have been prohibited in the withdrawn NYSE proposal 448/—and as they otherwise develop communications to both

448/ Regarding NYSE's representation that NYSE listed options and their underlying securities would be traded in separate rooms, AMEX has observed:

The NYSE proposed to trade most of these original twenty-five options in a room adjacent to but "physically separated from the equity trading floor by a ceiling-high solid wall." However, since this room does not contain sufficient space for trading all of the original twenty-five options, one post in the equity trading area is also to be converted to an option trading post. The NYSE has represented to the Commission that no option would be assigned to the option post in the "main equity trading room" if the underlying stock is also traded in that room. As to exactly where these underlying stocks are to be traded is unclear, but presumably they would be traded in a space adjacent and accessible to the "main equity trading room". Actually, the trading floor of the NYSE consists of several contiguous areas, all of which are completely open to one another (without walls or barriers in between) and all such areas are fully accessible to all floor members and support personnel. It would therefore appear that purported distinctions between a "main equity trading room" and other trading areas are meaningless and that all of the NYSE's trading areas combined (including the so-called "options room") must be considered a single trading floor.

In any event, it is clear that the NYSE does not intend to limit its options trading program to twenty-five options. As it adds more options it will presumably

(footnote continued on next page)