

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- 53277; File No. SR-NYSE-2006-03)

February 13, 2006

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Extend for an Additional Six Months the Pilot Program Permitting a Floor Broker and an RCMM to Use an Exchange Authorized and Provided Portable Telephone on the Exchange Floor

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 31, 2006, the New York Stock Exchange, Inc. (“NYSE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange seeks to extend its pilot program that amends NYSE Rule 36 (Communication Between Exchange and Members’ Offices) to allow Floor brokers and Registered Competitive Market Makers (“RCMMs”) to use Exchange authorized and provided portable telephones on the Exchange Floor upon approval by the Exchange (“Pilot”) for an additional six months, until July 31, 2006. The last extension of the Pilot was in effect on a six-month pilot basis expiring on January 31, 2006.<sup>3</sup> The text of the proposed rule change is available on the Exchange’s Web site (<http://www.nyse.com>), at the Exchange’s principal office, and at the Commission’s Public Reference Room.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 52188 (August 1, 2005), 70 FR 46252 (August 9, 2005) (SR-NYSE-2005-53).

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 Exchange 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

Background

The Commission originally approved the Pilot to be implemented as a six-month pilot<sup>4</sup> beginning no later than June 23, 2003.<sup>5</sup> Since the inception of the Pilot, the Exchange has extended the Pilot five times, with the current Pilot expiring on January 31, 2006.<sup>6</sup> Most recently, the Exchange incorporated RCMMs into the Pilot and clarified the conditions under

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<sup>4</sup> See Securities Exchange Act Release No. 47671 (April 11, 2003), 68 FR 19048 (April 17, 2003) (SR-NYSE-2002-11) ("Original Order").

<sup>5</sup> See Securities Exchange Act Release No. 47992 (June 5, 2003), 68 FR 35047 (June 11, 2003) (SR-NYSE-2003-19) (delaying the implementation date for portable phones from on or about May 1, 2003 to no later than June 23, 2003).

<sup>6</sup> See Securities Exchange Act Release Nos. 48919 (December 12, 2003), 68 FR 70853 (December 19, 2003) (SR-NYSE-2003-38) (extending the Pilot for an additional six months ending on June 16, 2004); 49954 (July 1, 2004), 69 FR 41323 (July 8, 2004) (SR-NYSE-2004-30) (extending the Pilot for an additional five months ending on November 30, 2004); 50777 (December 1, 2004), 69 FR 71090 (December 8, 2004) (SR-NYSE-2004-67) (extending the Pilot for an additional four months ending March 31, 2005); 51464 (March 31, 2005), 70 FR 17746 (April 7, 2005) (SR-NYSE-2005-20) (extending the Pilot for additional four months ending July 31, 2005); and 52188, supra note 3.

which a Floor broker may use an Exchange authorized and provided portable phone.<sup>7</sup> The Exchange has also filed for permanent approval of NYSE Rule 36, as amended.<sup>8</sup>

With respect to regulatory actions concerning the Pilot, there is an open investigation into possible insider trading in an NYSE listed security in which the trading activity of two RCMMs has been identified and is under review. The use of an Exchange authorized and provided portable phone by one of the RCMMs in or about January 2005 is under review as part of the investigation. No administrative or technical problems, other than routine telephone maintenance issues, have resulted from the Pilot over the past few months.<sup>9</sup> Therefore, the Exchange seeks to extend the Pilot for an additional six months, until July 31, 2006.

#### NYSE Rule 36

NYSE Rule 36 governs the establishment of telephone or electronic communications between the Exchange Floor and any other location. Prior to the Pilot, NYSE Rule 36.20 prohibited the use of portable telephone communications between the Exchange Floor and any off-Floor location. The only way that voice communication could be conducted by Floor brokers between the Exchange Floor and an off-Floor location prior to the Pilot was by means of a telephone located at a broker's booth. These communications often involved a customer calling a broker at the booth for "market look" information. Prior to the Pilot, a broker could not use a portable phone at the point of sale in the trading crowd to speak with a person located off the Exchange Floor.

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<sup>7</sup> See Securities Exchange Act Release No. 53213 (February 2, 2006) (SR-NYSE-2005-80).

<sup>8</sup> See SR-NYSE-2004-52 (September 7, 2004).

<sup>9</sup> The Exchange notes that it has received incoming telephone records for Floor brokers for the period of July 4, 2005 through January 31, 2006, and for RCMMs for the period of November 22, 2005 through January 31, 2006, and will continue to receive monthly updates.

Furthermore, until recently, NYSE Rule 36.20 only applied to a Floor broker's ability to use an Exchange authorized and provided portable phone.<sup>10</sup> RCMMs are non-specialist members of the Exchange and do not have the same type of information (i.e., access to the Display Book<sup>®</sup>) that a specialist has. As such, the Exchange believes it is appropriate for RCMMs to participate in the Pilot so that they can communicate with their offices in order to, among other things, enter off-Floor orders and better monitor their positions.<sup>11</sup>

The Exchange proposes to extend the Pilot for an additional six months, expiring on July 31, 2006. The Pilot would amend NYSE Rule 36 to permit Floor brokers and RCMMs to use Exchange authorized and issued portable telephones on the Exchange Floor. Thus, with the approval of the Exchange, a Floor broker would be permitted to engage in direct voice communication from the point of sale to an off-Floor location, such as a member firm's trading desk or the office of one of the broker's customers. Such communications would permit the broker to accept orders consistent with Exchange rules<sup>12</sup> and provide status and oral execution reports of orders previously received, as well as "market look" observations as have historically been routinely transmitted from a broker's booth location. Moreover, the Pilot would allow RCMMs to use an Exchange authorized and portable phone solely to communicate with their or their member organizations' off-Floor office and the off-Floor office of their clearing member organization, to enter off-Floor orders, and to discuss matters related to the clearance and

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<sup>10</sup> Telephone conversation between Jeff Rosenstock, Senior Special Counsel, NYSE, and Molly M. Kim, Attorney, Division of Market Regulation, Commission, on February 8, 2006.

<sup>11</sup> The Exchange has developed surveillance and examination procedures to monitor the activities of RCMMs, including their use of Exchange authorized and provided portable phones.

<sup>12</sup> Floor brokers receiving orders from the public over portable phones must be properly qualified to engage in such "direct access" business under NYSE Rules 342 and 345, among others.

settlement of transactions, provided the off-Floor office uses a wired telephone line for these discussions. RCMMs, however, would not be allowed to use a portable phone to conduct any agency business until issues involving the use of portable phones by RCMMs acting in the capacity of agent have been fully reviewed and resolved by NYSE Regulation in consultation with the Commission.<sup>13</sup> For both RCMMs and Floor brokers, use of a portable telephone on the Exchange Floor other than one authorized and issued by the Exchange would continue to be prohibited.

Furthermore, both incoming and outgoing calls would continue to be allowed, provided the requirements of all other Exchange rules have been met. Under NYSE Rule 123(e), a broker would not be permitted to represent and execute any order received as a result of such voice communication unless the order was first properly recorded by the member and entered into the Exchange's Front End Systemic Capture ("FESC") electronic database.<sup>14</sup> In addition, Exchange rules require that any Floor broker receiving orders from the public over portable phones must be properly qualified to engage in such direct access business under NYSE Rules 342 and 345, among others.<sup>15</sup>

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<sup>13</sup> Allowing RCMMs acting as Floor brokers to use Exchange authorized and provided portable phones would involve further discussions with the Commission and would be the subject of a separate filing with the Commission.

<sup>14</sup> See Securities Exchange Act Release No. 43689 (December 7, 2000), 65 FR 79145 (December 18, 2000) (SR-NYSE-98-25). See also Securities Exchange Act Release No. 44943 (October 16, 2001), 66 FR 53820 (October 24, 2001) (SR-NYSE-2001-39) (discussing certain exceptions to FESC, such as orders to offset an error or a bona fide arbitrage, which may be entered within 60 seconds after a trade is executed).

<sup>15</sup> See Information Memos 01-41 (November 21, 2001), 01-18 (July 11, 2001) (available on <http://www.nyse.com>) and 91-25 (July 8, 1991) for more information regarding Exchange requirements for conducting a public business on the Exchange Floor.

In addition, NYSE Rule 36 does not apply to specialists, who are prohibited from speaking from the post to upstairs trading desks or customers.<sup>16</sup> The Exchange notes that specialists are subject to separate restrictions in NYSE Rule 36 on their ability to engage in voice communications from the specialist post to an off-Floor location.<sup>17</sup>

By enabling customers to speak directly to a Floor broker in a trading crowd on an Exchange authorized and issued portable telephone and by allowing RCMMs to communicate with their upstairs office's land line and the land line of their clearing member organization's upstairs office, the Exchange believes that the proposed rule change would expedite and make more direct the free flow of information which, prior to the Pilot, had to be transmitted somewhat more circuitously via the booth. The Exchange believes that an extension of the Pilot for an additional six months would enable the Exchange to provide more direct, efficient access to its trading crowds and customers, increase the speed of transmittal of orders and the execution of trades, and provide an enhanced level of service to customers in an increasingly competitive environment.<sup>18</sup>

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<sup>16</sup> NYSE Rule 36.30 provides that, with the approval of the Exchange, a specialist unit may maintain a telephone line at its stock trading post location to the off-Floor offices of the specialist unit or the unit's clearing firm. Such telephone connection shall not be used for the purpose of transmitting to the Floor orders for the purchase or sale of securities, but may be used to enter options or futures hedging orders through the unit's off-Floor office or the unit's clearing firm, or through a member (on the Exchange Floor) of an options or futures exchange.

<sup>17</sup> See Securities Exchange Act Release No. 46560 (September 26, 2002), 67 FR 62088 (October 3, 2002) (SR-NYSE-00-31) (discussing restrictions on specialists' communications from the post).

<sup>18</sup> See, e.g., Securities Exchange Act Release Nos. 43493 (October 30, 2000), 65 FR 67022 (November 8, 2000) (SR-CBOE-00-04) (expanding the Chicago Board Options Exchange, Inc.'s existing policy and rules governing the use of telephones at equity option trading posts by allowing for the receipt of orders over outside telephone lines from any source, directly at equity trading posts) and 43836 (January 11, 2001), 66 FR 6727 (January 22, 2001) (SR-PCX-00-33) (discussing and approving the Pacific

## Pilot Program Results

Since the Pilot's inception, the Exchange represents that there have been approximately 800 portable phone subscribers.<sup>19</sup> In addition, with regard to portable phone usage, for a sample week of December 5, 2005 through December 9, 2005, an average of 10,951 calls per day were originated from portable phones, and an average of 4,932 calls per day were received on portable phones. Of the calls originated from portable phones, an average of 7,216 calls per day was internal calls to the booth, and 3,735 calls per day were external calls. Thus, approximately 66% of the calls originated from portable phones were internal calls to the booth. With regard to received calls, of the 4,932 average calls per days received, an average of 2,472 calls per day was external calls and an average of 2,460 calls per day was internal calls received from the booth. Thus, approximately 50% of all received calls were internally generated and 50% were calls from the outside.

Therefore, the Exchange believes that the Pilot appears to be successful in that there is a reasonable degree of usage of portable phones. Furthermore, except as noted above, there have been no other regulatory, administrative, or other technical problems identified with their usage. The Exchange also believes that the Pilot appears to facilitate communication on the Exchange Floor for both Floor brokers and RCMMs without any corresponding drawbacks. Therefore, the Exchange believes it is appropriate to extend the Pilot for an additional six months, expiring on July 31, 2006.

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Exchange's proposal to remove current prohibitions against Floor brokers' use of cellular or cordless phones to make calls to persons located off the trading floor).

<sup>19</sup> The data includes both Floor brokers' and RCMMs' usage of Exchange authorized and provided phones. Telephone conversation between Jeff Rosenstock, Senior Special Counsel, NYSE, and Molly M. Kim, Attorney, Division of Market Regulation, Commission, on February 7, 2006.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>20</sup> in general, and further the objectives of Section 6(b)(5) of the Act<sup>21</sup> in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The Exchange believes that the amendment to NYSE Rule 36 would support the mechanism of free and open markets by providing for increased means by which communications to and from the Exchange Floor could take place.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

The Exchange has neither solicited nor received written comments on the proposed rule change.

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

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>22</sup> and Rule 19b-

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<sup>20</sup> 15 U.S.C. 78f(b).

<sup>21</sup> 15 U.S.C. 78f(b)(5).

<sup>22</sup> 15 U.S.C. 78s(b)(3)(A).

4(f)(6) thereunder.<sup>23</sup> At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

The Exchange requests that the Commission waive the 30-day operative period under Rule 19b-4(f)(6)(iii).<sup>24</sup> The Exchange believes that the continuation of the Pilot is in the public interest as it will avoid inconvenience and interruption to the public. The Commission believes that it is consistent with the protection of investors and the public interest to waive the 30-day operative delay and make this proposed rule change immediately effective upon filing on January 31, 2006.<sup>25</sup> The Commission believes that the waiver of the 30-day operative delay will allow the Exchange to continue, without interruption, the existing operation of its Pilot until July 31, 2006.

The Commission notes that proper surveillance is an essential component of any telephone access policy to an exchange trading floor. Surveillance procedures should help to ensure that Floor brokers and RCMs use portable phones as authorized by NYSE Rule 36<sup>26</sup> and that orders are being handled in compliance with NYSE rules. The Commission expects the Exchange to actively review these procedures and address any potential concerns that have arisen during the Pilot. In this regard, the Commission notes that the Exchange should address whether telephone records are adequate for surveillance purposes.

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<sup>23</sup> 17 CFR 240.19b-4(f)(6).

<sup>24</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>25</sup> For purposes only of waiving the 30-day operative delay of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>26</sup> See note 11 *supra* and accompanying text for other NYSE requirements that Floor brokers be properly qualified before doing public customer business.

The Commission also requests that the Exchange report any problems, surveillance, or enforcement matters associated with the Floor brokers' and RCMs' use of an Exchange authorized and provided portable telephone on the Exchange Floor. As stated in the Original Order, the NYSE should also address whether additional surveillance would be needed because of the derivative nature of the ETFs. Furthermore, in any future additional filings on the Pilot, the Commission would expect that the NYSE submit information documenting the usage of the phones, any problems that have occurred, including, among other things, any regulatory actions or concerns, and any advantages or disadvantages that have resulted.<sup>27</sup>

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSE-2006-03 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSE-2006-03. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all

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<sup>27</sup> In the future, the Commission expects the information to distinguish between Floor brokers' and RCMs' usage of the phones.

comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 in the Commission's Public Reference Room. Copies of such filing also will be available for inspection and copying at the principal office of the NYSE. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-NYSE-2006-03 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>28</sup>

Nancy M. Morris  
Secretary

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<sup>28</sup> 17 CFR 200.30-3(a)(12).