

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-53791; File No. SR-NYSE-2006-33)

May 11, 2006

Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to a Pilot Program beginning on May 12, 2006 and ending on October 31, 2006 or sooner, to implement certain Hybrid Market changes and amend certain changes to approved Hybrid Market rules

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 May 10, 2006, the New York Stock Exchange LLC (“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 Exchange filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposed rule change effective upon filing with the Commission. 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 proposed rule change consists of amendments to NYSE rules governing trading in pilot securities (“Pilot Securities”) pursuant to a pilot program (the “Pilot”).

The text of the proposed rule change is available on the Exchange’s Web site (<http://www.nyse.com>), at the Exchange’s Office of the Secretary, 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> 15 U.S.C. 78s(b)(3)(A).

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

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

The NYSE HYBRID MARKET<sup>SM</sup> was proposed in SR-NYSE-2004-05 and Amendment Nos. 1, 2, 3, 5, 6, 7, and 8<sup>5</sup> thereto and approved on March 22, 2006<sup>6</sup> (“Hybrid Market filings” or “Hybrid”). The Hybrid Market filings, as approved, set forth the Exchange’s plan to provide mechanisms for more electronic trading via NYSE Direct+<sup>®</sup> (“Direct +”), while retaining the benefits of the auction market. Phase 1 of the Hybrid Market is in the process of being implemented Floor-wide. Other Hybrid Market changes will be implemented in several phases over the next few months.

As a result of a merger between Lucent Technologies Inc. (“Lucent”) and Alcatel, announced on or about March 23, 2006, there has been increased activity in Lucent, a listed security on the Exchange. Much of this activity has been routed to other market centers that

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<sup>5</sup> See Securities Exchange Act Release Nos. 50173 (August 10, 2004), 69 FR 50407 (August 16, 2004); 50667 (November 15, 2004), 69 FR 67980 (November 22, 2004); and 51906 (June 22, 2005), 70 FR 37463 (June 29, 2005). The Exchange withdrew Amendment No. 4 and replaced it with Amendment No. 5. See also Amendment No. 6 filed on September 16, 2005, Amendment No. 7 filed on October 11, 2005, and Amendment No. 8 filed on March 14, 2006.

<sup>6</sup> See Securities Exchange Act Release No. 53539 (March 22, 2006), 71 FR 16353 (March 31, 2006) (“Hybrid Market approval order”).

have automatic execution facilities with no size and frequency restrictions.<sup>7</sup> In order to remain competitive with other market centers in Lucent, the Exchange proposes a Pilot that would implement immediately certain of the Hybrid Market changes approved but scheduled for implementation in later phases. In addition, the Exchange proposes certain amendments, as outlined below, to other approved rules for the purposes of the Pilot.

This Pilot would include only Lucent. The Exchange may seek to include other securities in the Pilot for similar reasons. In the event the Exchange seeks to do so, the Exchange will amend the Pilot by filing a proposed rule change with the Commission indicating the proposed additions and notify its membership of such additions, if approved.

The Pilot would commence on May 12, 2006, and would terminate on October 31, 2006 or earlier, upon notice to the Commission and Exchange membership. An Information Memo would be issued and posted on the Exchange's Web site announcing the Pilot.

Moreover, the Exchange intends to have available at all times during the Pilot two versions of the operating settings – the new version that would be operational and the original, pre-Pilot version. If a problem develops during the Pilot, the Exchange will be able to revert to the pre-Pilot settings within an average time of two minutes or less.

In the event systems or other problems arise with the Pilot that adversely impact investors or impede the Exchange's ability to maintain a fair and orderly market, the Exchange will immediately terminate the Pilot in whole or in part, as appropriate, and return trading to operations under NYSE rules applicable at the time of such termination.

#### Rules Applicable to the Pilot

The following rules are applicable during the Pilot. The Exchange has designated these

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<sup>7</sup> See Exchange Rules 1000 and 1005, as in effect today.

rules with a “P” in the proposed rule text.<sup>8</sup> In addition, during the Pilot, all other Exchange rules will apply as they do to other securities traded on the Exchange.<sup>9</sup> Furthermore, functions and rules to be implemented in future phases of Hybrid, as described in the Hybrid Market filings and approval order, will apply to the Pilot when implemented in the normal course of business. For this reason, the Exchange has kept the numbering of these Pilot rules consistent with and parallel to the Hybrid Market approved rules, except for the addition of the “P” designation. Where the Pilot rules are different from the Hybrid Market rules, the Pilot rules shall govern with respect to the Pilot securities.

#### Definition of Auto Ex Order (Rule 13(P))

In the Hybrid Market filings, the Exchange defined an auto ex order in Rule 13, in part, as “a market order designated for automatic execution or a limit order to buy (sell) priced at or above (below) the Exchange best offer (bid) at the time such order is routed to the Display Book.<sup>®</sup>” In addition, the Commission approved the Exchange’s proposal to eliminate the 1,099 share restriction for auto ex orders. Although the Hybrid Market filings have been approved, this change has not yet been implemented.

For purposes of this Pilot, the Exchange proposes to:

- (i) provide that auto ex orders in Pilot securities may be entered as market and limit orders in an amount greater than 1,099 shares;

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<sup>8</sup> The previous Hybrid Market pilot which put into operation Phase 1 of the Exchange’s Hybrid Market initiative also designated rules with a “P.” This pilot terminated upon Commission approval of the Hybrid Market. Roll out of Phase 1 Floor-wide to all Exchange-listed securities began March 24, 2006. See also Securities Exchange Act Release No. 52954 (December 14, 2005), 70 FR 75519 (December 20, 2005); see also Information Memos 05-98 (December 14, 2005) and 06-14 (March 23, 2006).

<sup>9</sup> Phase 1 was implemented in Lucent on April 5, 2006.

- (ii) add a maximum order size of 3 million shares for auto ex orders;<sup>10</sup> and
- (iii) include that all market orders,<sup>11</sup> not only those market orders specifically designated as such, are eligible for automatic execution.<sup>12</sup>

The Exchange believes that in the case of highly liquid securities, such as Lucent, this proposed change will benefit customers entering market orders, allowing them the opportunity to get a better and faster execution rather than requiring them to wait for a manual execution by a specialist.

Where an incoming auto ex market order that exhausts all liquidity at the best bid (offer) remains unfilled, the specialist will manually handle the remainder of the market order.<sup>13</sup> Where an auto ex limit order or residual thereof cannot be immediately executed, it shall be displayed as a limit order on the Display Book.<sup>14</sup>

As stated above, as other parts of Rule 13 amended by the Hybrid Market filings are implemented in the normal course of business, the Exchange proposes that they will apply to the Pilot.

#### Definition of a Market Order – Rule 13(P)

The Hybrid Market filings provided that “a market order designated for automatic

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<sup>10</sup> This would allow the Exchange to provide for a phased-in raising of order size eligibility, up to a maximum of 3,000,000 shares. Each raising of order size eligibility shall be preceded by advance notice to the Exchange’s membership. The Exchange intends to begin the Pilot with a maximum order size of 1,000,000 shares, which is the same as NYSE Archipelago’s (“Arca”) automatic execution facility’s maximum order size.

<sup>11</sup> In the Hybrid Market filings, market orders need to be designated auto ex in order to be treated so. The Exchange recognizes that a separate 19b-4 filing is required in order for this provision to be applicable beyond the Pilot.

<sup>12</sup> See proposed Exchange Rule 13(a)(i)(P) and (a)(P).

<sup>13</sup> See proposed Exchange Rule 1000(d)(v)(A)(P).

<sup>14</sup> See proposed Exchange Rule 1000(d)(v)(P).

execution is an auto ex order and shall be executed in accordance with, and to the extent provided by, Exchange Rules 1000-1004.” For purposes of the Pilot, and as described above, this definition is proposed to be amended to state that all market orders are auto ex orders, even if they are not designated for automatic execution.

NYSE Direct+ - Automatic Executions – Rules 1000(P) and 1005.10(P)

The Exchange proposes to add Rule 1000.10(P) which describes the unique rules applicable to the Pilot and the Pilot’s start and end dates.

In the Hybrid Market filings, the Exchange deleted the first three sentences of Exchange Rule 1000 and added (a) as a paragraph designation. The Exchange proposes to implement these amendments for purposes of the Pilot. In addition, the Exchange added language to reflect that automatic executions may take place with respect to reserve interest, orders on the Display Book outside the Exchange published quotation during sweeps and with floor broker agency file interest and specialist interest. The Exchange is not proposing to implement this change to Rule 1000 at this time. Accordingly, automatic executions will continue to be executed against only displayed interest.<sup>15</sup>

In addition, the Exchange proposes to implement Exchange Rule 1000(d) to set forth how auto ex market and limit orders would be handled during the Pilot; auto ex orders would trade with all liquidity at the best bid (offer). Where there is residual, it shall trade with available contra-side interest.<sup>16</sup> In addition, as noted above, where an incoming auto ex market order that exhausts all liquidity at the best bid (offer) remains unfilled, the specialist will manually handle the remainder of the market order.<sup>17</sup>

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<sup>15</sup> See proposed Exchange Rule 1000(a)(P).

<sup>16</sup> See proposed Exchange Rules 1000(d)(i)-(ii)(P).

<sup>17</sup> See proposed Exchange Rule 1000(d)(v)(A)(P).

Finally, the Exchange is not seeking to implement as part of the Pilot at this time the amendments to Hybrid Market Rules 1000(a)(i)-(vi). The current NYSE Direct+ rules will continue to govern when automatic executions are not available. As noted above, the approved amendments to these rules will be implemented in a later phase. Should the Pilot still be active at the time of their implementation, the amended Hybrid Market version of these rules will apply to the Pilot, upon notice to the Exchange membership.

In the Hybrid Market filings, the Exchange proposed to rescind Rule 1005. This amendment has been approved by the Commission, but has not yet been implemented. Exchange Rule 1005 provides that “an auto ex order for any account in which the same person is directly or indirectly interested may only be entered at intervals of no less than 30 seconds between entry of each such order in a stock,” unless certain conditions are met. The Exchange proposes to implement this rescission with respect to the Pilot.<sup>18</sup>

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>19</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>20</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 the proposed rule change is also designed to support the principles of Section 11A(a)(1) of the Act<sup>21</sup> in that it seeks to assure economically efficient execution of securities transactions, make it practicable for

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<sup>18</sup> See proposed Exchange Rule 1005.10(P).

<sup>19</sup> 15 U.S.C. 78f(b).

<sup>20</sup> 15 U.S.C. 78f(b)(5).

<sup>21</sup> 15 U.S.C. 78k-1(a)(1).

brokers to execute investors' orders in the best market, and provide an opportunity for investors' orders to be executed without the participation of a dealer.

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) by its terms, 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-4(f)(6) thereunder.<sup>23</sup>

A proposed rule change filed under Rule 19b-4(f)(6) normally may not become operative prior to 30 days after the date of filing. However, Rule 19b-4(f)(6)(iii)<sup>24</sup> permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has requested that the Commission waive the 30-day operative delay and designate the proposed rule change immediately operative upon filing. The Commission believes that waiver of the 30-day operative delay is consistent with the

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

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

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

protection of investors and the public interest because the Pilot may enhance competition in this highly liquid security by allowing NYSE to modify its automatic execution system for this security.<sup>25</sup> Accordingly, the Commission designates the proposal to be effective and operative upon filing with the Commission.<sup>26</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.

#### 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-2006-33 on the subject line.

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<sup>25</sup> The Exchange represented that it would not implement the specialist algorithmic function in the Pilot until the Exchange develops guidance to clarify how it expects specialists to comply with NYSE Rule 104. Telephone conversation between Nancy Reich, Vice President, NYSE, and Kelly M. Riley, Assistant Director, Division of Market Regulation, Commission, on May 10, 2006. See also footnote 382 of the Hybrid Market approval order, supra note 6.

<sup>26</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

Paper Comments:

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

All submissions should refer to File Number SR-NYSE-2006-33. 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 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 Exchange. 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-2006-33 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>27</sup>

Nancy M. Morris  
Secretary

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<sup>27</sup> 17 CFR 200.30-3(a)(12).