

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53840; File No. SR-NYSE-2005-58)

May 19, 2006

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change Relating to Exchange Rule 312(f) Regarding Changes Within Member Organizations

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934 (the “Exchange Act”), and Rule 19b-4 thereunder,² notice is hereby given that on August 15, 2005, the New York Stock Exchange, Inc. (“NYSE” or the “Exchange”) filed with the Securities and Exchange Commission (“SEC” or the “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. On May 5, 2006, NYSE filed Amendment No. 1 to the proposed rule change.³ 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 NYSE is filing with the SEC the proposed amendment to Exchange Rule 312(f) to, among other changes, permit the recommendation of purchases and sales of shares of companies controlled and under common control with member organizations

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 1 replaces the rule text in the original filing in its entirety and proposes to clarify that Rule 312(f) applies only to non-investment grade debt and equity securities. Amendment No. 1 also adds Material Associated Persons (“MAPs”), as that term is used in Rule 17h-1T of the Exchange Act, to the class of persons for whose securities the solicitation of trades is prohibited.

(other than MAPs),⁴ subject to appropriate customer disclosure of the relationship.

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

Changes Within Member Organizations

Rule 312(a) to (e) no changes.

(f) (1) After the completion of a distribution of its equity or non-investment grade debt securities or those of any organization controlling the member organization or of any Material Associated Person (as used in Rule 17h-1T of the Securities Exchange Act of 1934, as amended) of the member organization, no member [corporation] organization [which has any publicly held security outstanding] shall effect any transaction (except on an unsolicited basis) for the account of any customer in, or make any recommendation with respect to, any such security [issued by such member corporation]. [or]

(2) Any member organization that makes any recommendation of any [such] equity or non-investment grade debt security issued by any [corporation controlling] person controlled by or under common control with such member [corporation] organization (other than a Material Associated Person) [.], shall promptly disclose to such

⁴ Exchange Act Rule 17h-1T describes certain indicia of MAP status: i) legal relationship between the broker or dealer and the associated person; ii) overall financing requirements of the broker or dealer and the associated person, and the degree, if any, to which the broker or dealer and the associated person are financially dependent on each other; iii) degree, if any, to which the broker or dealer or its customers rely on the associated person for operational support or services in connection with the broker's or dealer's business; iv) level of risk present in the activities of the broker's or dealer's associated persons; and v) extent to which the associated person has the authority or the ability to cause a withdrawal of capital from the broker or dealer.

customer the existence and nature of such control at the time of recommendation and, if this disclosure is not made in writing, shall provide this disclosure in writing prior to the completion of the transaction.

(3) No corporation which has any publicly held security outstanding shall, without the prior written approval of the Exchange, dispose of any such security for its own account and no member corporation shall acquire any such security for its own account or for the account of any corporation controlling, controlled by or under common control with such member corporation except with the prior written approval of the Exchange or pursuant to the terms and provisions of such security or of any agreement between the member corporation and the holder of such security, which agreement has previously been filed with and approved by the Exchange. The Exchange will approve such a disposition or acquisition of securities unless it determines that such action will impair the financial responsibility or operational capability of the member corporation.

Remainder of Rule 312 unchanged.

A. Self-Regulatory Organization's Statement of Purpose of, and Statutory Basis for, the Proposed Rule Change

(1) Purpose

a. Background

Rule 312(f) (the "Rule") was adopted in 1970 when public ownership of member corporations was first permitted in order to address what were perceived to be potential conflicts in such transactions. Experience during the intervening 35

years⁵ has indicated that certain potential conflicts can be effectively addressed by way of disclosure, rather than prohibition. Further, fundamental and wide-ranging changes in the securities industry since the Rule's introduction also contributed to rendering aspects of the Rule unnecessary, outdated and unnecessarily burdensome to member organizations.

In the course of responding to Rule 312(f) interpretive requests over time, the Exchange has noted changes in the business and regulatory environment that warrant reconsideration of the scope of Rule 312(f)'s application. These changes include:

- (i) The wide diversification of business conducted by member organizations and other entities in the same control family; and
- (ii) The nature of new products that are created for investors.

The Exchange's regulatory experience relative to Rule 312(f) has generally involved determinations as to the existence, or not, of a control relationship involving a member organization among the complicated interrelationships of, and equity investments by, financial organizations. The sole purpose of determining whether such a control relationship exists is to establish whether Rule 312(f) restrictions on the recommendation of stock issued by entities in the member organization's corporate family apply to the member organization. The term "recommendation" in this context

⁵ NYSE previously proposed the amendment of Rule 312(f) (which, at the time was Rule 312(g)) in 1982 (See File No. SR-NYSE-83-3). Exchange Act Release No. 19462 (January 28, 1983) (notice of filing of SR-NYSE-83-3). In the filing, NYSE stated that the rule created a "burden on competition" by placing "NYSE members and their customers at a competitive disadvantage" to similar organizations subject only to the SEC disclosure requirements. NYSE withdrew the proposal in 1994. That proposal differed from the present proposal in allowing the recommendation of the member organization's own publicly traded securities and those of its parent corporation, subject to appropriate disclosure of the relationship. The present proposal does not permit the recommendation of (or the solicited execution of trades in the shares of) a member organization or its parent following their initial distribution.

has been interpreted by NYSE to include solicited transactions, the issuance of research or market letters, and the use of “active” market making tactics (i.e., actively buying and selling a stock from a proprietary account as opposed to “passively” standing ready to buy or sell).

Typical member organization Rule 312(f) interpretive requests involve submission to the Exchange of intricate factual representations regarding board representation, equity ownership, and/or profit participation and will request concurrence with the opinion that no control relationship exists.⁶ Often, the request will involve one or more investment partnerships, affiliated with a member organization, that hold an interest in a subject security. An officer of the member organization may be a general partner or on the board of directors of the subject security’s issuing company. The analysis to determine control of the subject security involves objective factors as well as consideration of the percentage of member organization personnel represented on the issuing company’s board of directors and/or their ability to influence the issuing company. Such directors, while not participants in day-to-day management of the issuing company, may exercise a degree of control over it resulting either from their voting power, from specially granted powers, or from participation in committees. Ultimately, the determination of control is often, in good measure, a subjective one.

⁶ NYSE Rule 2 creates a presumption of control, in this context, where a person possesses the right to vote 25% or more of the voting securities, receives 25% or more of the net profits or is a director of the other person. Rule 2 defines a “person” as “a natural person, corporation, partnership, association, joint stock company, trust, fund or any organized group of persons whether incorporated or not.”

b. Proposed Amendments

The Rule, in pertinent part, currently prohibits a member organization from soliciting transactions in its own publicly traded securities and from making any recommendations with respect to its publicly traded securities or the securities issued by any corporation controlling, controlled by or under common control with such member corporation (i.e., the securities of any parent, sister, or subsidiary corporation relative to the member organization). The intent of the Rule is to mitigate conflicts of interest that may arise when recommending the public securities of companies in which the member organization may have an interest.

i. Proposed Codification to Exclude Investment Grade Debt from Rule 312(f)

NYSE has interpreted Rule 312(f) to apply only to non-investment grade debt and equity securities.⁷ This proposal would codify that interpretation.

ii. Proposed Expansion to Include All Non-Investment Grade Debt and Equity Securities

The proposed rule change would also broaden the application of the Rule to all non-investment grade debt and equity securities, including privately placed issues. The current Rule's prohibition applies only to publicly traded securities.

⁷ Another common interpretive inquiry with respect to Rule 312(f) involves, and NYSE anticipates would continue to involve, a determination as to whether the security in question has "debt-like characteristics." The Exchange has generally interpreted Rule 312(f) restrictions to not apply to investment grade debt and securities that function as investment grade debt. The interpretation as to whether a security functions as investment grade debt is based on the totality of the circumstances, e.g., 1) whether the shares of stock have fixed dividends; 2) whether the shares of stock are non-participatory in common dividends; 3) whether the shares of stock have limited voting rights; and 4) whether the shares of stock are non-convertible into common stock.

The Rule currently prohibits effecting solicited transactions only as to the securities of member organizations. The proposed rule change would extend that prohibition to the non-investment grade debt and equity securities of companies controlling member organizations (e.g., parent companies) and MAPs. By their nature, MAPs can substantially influence a registered broker-dealer, and the inclusion of such entities along with controlling organizations⁸ acts to limit inevitable conflicts of interest.

iii. Proposed Amendment to Permit Certain Recommendations If Disclosed

The Exchange also proposes to amend the Rule to permit the recommendation of purchases and sales of shares of companies controlled by and under common control with member organizations (other than MAPs), subject to appropriate customer disclosure of the relationship.⁹ Given the varied and numerous sister corporations that a member organization owned by a diversified holding company may have, the Rule 312(f) restrictions on recommendations of securities issued by all such corporations can sometimes be an unnecessary burden to legitimate business activity. The rule has had the unintended impact of affecting the way merger and acquisition deals are structured, in that unnecessarily complex and unwieldy ownership models are developed primarily to avoid the 25% voting or profit presumption of control established by NYSE Rule 2.

⁸ See NYSE Rule 2.

⁹ See proposed Rule 312(f)(2).

To alleviate these unintended burdens, the Exchange proposes amendments to Rule 312(f) that would permit member organizations to recommend equity or non-investment grade debt securities¹⁰ issued by any person controlled by, or under common control with, a member organization (other than a MAP); however, any such recommendation would be subject to a requirement to disclose to the customer the existence and nature of such control at the time of recommendation. If the disclosure at the time of the recommendation is not made in writing, then the member must also provide this disclosure in writing prior to the completion of the transaction.¹¹ This proposal is consistent with and similar to other Exchange regulations such as Rule 472, which addresses the issue of research analysts' conflicts, in part, through disclosure of potential conflicts involving ownership of equity that is the subject of research and market making activity involving the subject equity.

While the Exchange believes that disclosure is adequate to address certain conflicts of interest that could arise with respect to a member's recommendation to buy or sell securities of many affiliated entities, the Exchange believes that it is warranted to retain the prohibition on the solicitation of purchases in the securities of the member organization, any controlling organization or a MAP, given the greater potential for a conflict of interest inherent in such relationships. For instance, an employee of a member organization could act on material non-public information in connection with either the member organization or its parent. Of special concern is stock issued by the member

¹⁰ As previously noted, the proposed change would broaden the application of the Rule to all securities including privately placed issues. The current Rule applies only to publicly traded securities.

¹¹ See proposed Rule 312(f)(2).

organization itself, as a registered representative/employee may attempt to drive up the price to increase the value of his or her company stock plan portfolio. To address these potential abuses, the Exchange is proposing to preserve the prohibition on making a recommendation or otherwise acting on such information in these contexts.

(2) Statutory Basis

The proposed rule change is consistent with the requirements of the Exchange Act, and the rules and regulations thereunder applicable to a national securities exchange, and in particular, with the requirements of Section 6(b)(5)¹² of the Exchange Act. Section 6(b)(5) requires, among other things, that the rules of an exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and national market system, and in general, to protect investors and the public interest. In addition Section 3(f) of the Exchange Act requires, among other things, whenever there is a requirement to consider or determine whether an action is necessary or appropriate in the public interest, to also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. The proposed change in Rule 312(f) will act to assure adequate and continuing protection for investors while promoting efficiency, competition, and capital formation by permitting the recommendation of purchases and sales of shares of companies controlled and under common control with member organizations (other than MAPs), subject to appropriate customer disclosure of the

¹² 15 U.S.C. 78f(b)(5).

relationship, by expanding certain restrictions on effecting solicited transactions, and by codifying NYSE interpretations.

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

The Exchange believes that the proposal does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act.

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

Written comments were neither solicited nor received.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

- (A) by order approve such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Exchange 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. Please include File Number SR-NYSE-2005-58 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NYSE-2005-58. 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, 100 F Street, NE, Washington, DC 20549. Copies of such filing will also 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 the File Number SR-NYSE-2005-58 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.¹³

Nancy M. Morris
Secretary

¹³ 17 CFR 200.30-3(a)(12).