THE INTERACTIVE BROKERS GROUP

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Via Electronic Mail and Hand Delivery

Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: Proposed Rule Change and Amendment No. 1 Thereto by the New York Stock Exchange, Inc. Relating to Enhancements to the Exchange's Existing Automatic Execution Facility (NYSE Direct+); SR-NYSE-2004-05

Dear Mr. Katz:

The Interactive Brokers Group, on behalf of its affiliates Timber Hill LLC and Interactive Brokers LLC[1], respectfully submits these comments on the proposed rules of the New York Stock Exchange ("NYSE" or the "Exchange") for changes to its Direct+ platform. The proposed rules would create a hybrid market featuring elements of electronic trading and elements of open outcry trading.

While we strongly support any effort by the Exchange more fully to automate its trading system, the rules as proposed cannot be approved because they are too cursory and leave critical questions about the operation of the proposed hybrid market unanswered. It is no exaggeration to say that this proposal is among the most important SRO rule changes that the Commission has had to evaluate for quite some time. Yet on many key operational elements, the proposed rules are essentially a *tabula rasa* – interpreted and implemented one way they might bring great improvement to the Exchange's market structure, but interpreted another way they might offer

[1] We are interested in the speed, certainty and cost of executing U.S. stock trades both on behalf of our customers and also as very large proprietary traders ourselves. Through our Interactive Brokers subsidiary we provide direct access online brokerage services to thousands of institutions and sophisticated individual customers, connecting them to virtually every major U.S. market center using smart routing technology. Our market making affiliate, Timber Hill, is one of the most active market making firms in options and other equity derivatives and we are therefore among the largest users of the U.S. stock exchanges.

little progress toward the fairer, more automated market that the Exchange's users require. In any event, the rule proposal as drafted does not provide the public with a sufficient basis to offer informed comment, nor do the proposed rules provide any assurance to the public or the Commission of exactly how the market would operate if approved. A much more specific and detailed version of the rules, with concrete trading examples, should be published for comment as soon as possible.

In our analysis of the NYSE proposal, we have identified dozens of questions that are left open by the rules as currently drafted. Here are just a few:

Initial Handling of AL and Market Orders:

1. The proposed rules say that an Auction Limit ("AL") Order or market order not designated for automatic execution will be displayed on the book at the minimum variation better than the exchange bid or offer ***"if not executed upon entry."***

   a. Exactly how would such an order be "executed upon entry" rather then booked? Would it be a manual or automated process? Is price improvement required if an AL Order or non-auto-ex-designated market order is "executed upon entry"?
   b. If it is not "executed upon entry", what is the process for posting the AL or non-auto-ex-designated market order in the Display Book? Does it happen manually or automatically?
   c. If it is a manual process to book these types of orders, how long does the specialist have to decide whether to execute such an order before the order will be quoted in the book? Is there a surveillance standard that will be used?
   d. Does the 15 second timer start to run from the time the AL or non-auto-ex-designated market order is received by the Exchange or from the time it is put on the Display Book?
   e. What happens if the market is one penny wide and a non-auto-ex-designated market order or AL order is received by the Exchange?

After AL and Market Orders Hit the Display Book:

2. After an AL or non-auto-ex-designated market order is placed in the Display Book at a minimum tick better than the contra side quote, but before 15 seconds has elapsed, can the specialist or crowd trade with the order at the prevailing offer (*i.e.*, no price improvement for the order)? How? Can orders be manually "marked" for handling or execution by the specialist and thereby removed indefinitely from the system's automatic execution timer?

3. AL Orders and non-auto-ex-designated market orders both will automatically execute if there is ***"a subsequent order on the same side of the market capable of trading at a price better than the [market or auction limit order] is bidding"***. But which trades first -- the AL or market order that was pending on the book, or the incoming order?

4. If the booked order trades first, then the Exchange's quote on the other side of the market from the booked order is not truly automatically executable, because an electronic order sent

to hit that price will simply trigger the booked order to trade and may not get filled itself. For example, assume the NYSE market is \$2.20 - \$2.25, and a non-auto-ex-designated market order to buy is placed on the book as a \$ 2.21 bid. Ten seconds later, another customer sends a buy limit order to pay \$2.25. It would seem that the booked market order, and not the incoming limit order, would trade (assuming there is only sufficient volume at the top of the book to fill one or the other order). Would the Exchange's bid or offer nonetheless be designated as automatically executable in the public quote if there is a booked AL or market order on the other side? Would it depend on the available volume at the top of the book compared to the size of the pending AL or market order(s) on the other side?

5. What happens when multiple AL Orders and non-auto-ex-designated market orders are received by the Exchange within the same 15 second period?

   a. An AL or non-auto-ex-designated market order coming in within 15 seconds of any booked AL or market order would seem to force the prior order to trade immediately (because the second order would seem to be "a subsequent order capable of trading at a better price"). Yet the rule filing says: ***"Multiple AL orders and market orders on the same side of the market would be aggregated at the best price (consistent with the AL order limits), and executions would occur based on time priority."*** What does this mean?
   b. There are many permutations to consider regarding the interactions of AL orders, non-auto-designated market orders, ordinary market orders and ordinary limit orders depending on the relative time of receipt of the orders and the limit price of each order. Yet the proposed rules use very cryptic language to describe the trigger conditions for execution of booked AL and market orders, and do not describe with certainty how executions will happen, with what priority, and at what price, for each scenario. No examples are provided.

<u>Liquidity Replenishment Points ("LRPs")</u>

6. How will LRPs be determined?

7. How will they be disseminated? How often? Real-time? Days, weeks, months?

8. Will the public be able to see LRPs for each stock, or have enough information real time to calculate them (*i.e.*, to know when a LRP will be hit if a large order is sent?

<u>Cancellations</u>

9. The Federal Register release says that where a LRP is reached or autoquote is otherwise suspended, "cancellations of orders would be permitted." This provision does not appear to be in the proposed rules themselves. Is the cancellation electronic and immediate or does it involve manual handling?

Specialist Trading, Specialist Interest File and Broker Agency Interest File

10. How exactly does the specialist ***"systematically supplement the Exchange's published bid or offer?"*** This is referenced in the proposed rules as a separate process from that of the specialist interest file but the process is not described at all.

11. How exactly does the specialist information file work? How is it used to ***"facilitate a single price execution at the bid or offer"?*** How does the specialist know how much stock will be needed to fill the entire order? Are these processes manual or automated?

12. How does priority and parity work with respect to the specialist file and the broker agency interest file? Do orders in those files have any priority or precedence over incoming orders?

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The above questions provide just a small sample of the operational details that are omitted from the Exchange's important hybrid market proposal. It may be that the Exchange and/or the Commission know the answers to these and the other questions surrounding the proposed rules, but the answers have not been provided to the many customers, broker-dealers and member firms that rely on the Exchange. While we hope and expect in the near future to be able to comment favorably on the Exchange's initiative to further automate its markets, the proposed rules as drafted do not allow us to do so at this point.

We thank the Commission and its staff for their time and consideration of our comments. Please contact either of undersigned if you require any additional information or would like to discuss these matters further.

s/ Thomas Peterffy

Thomas Peterffy

David M. Battan

cc: Hon. William H. Donaldson
Hon. Paul S. Atkins
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