processed in NSCC's Continuous Net Settlement (''CNS'') system.

When NSCC revised and updated CNS in 2004 (referred to as the ''CNS Rewrite''), it provided the capability on any settlement day to take in and process transactions due for settlement that day provided the trades are recorded or compared prior to an established cut-off time in the morning.[3] This capability is currently provided for as-of equity transactions but has not yet been expanded to as-of fixed income transactions.[4] Rather, settlement of as-of fixed income corporate debt, municipal, and unit investment trust (''UIT'') trades (corporate debt, municipal, and UIT trades are collectively referred to as ''CMU'' trades) compared on or after their designated settlement date currently occurs on the business day following the day they are compared. Given that settlement risks associated with CMU trades would be reduced if they settled on an accelerated basis in the same manner that as-of equity trades are settled, NSCC is enhancing its fixed income processing to permit same day settlement of as-of fixed income transactions.[5] To accomplish this, NSCC is amending Procedure II (Trade Comparison and Recording Service) so that CNS-eligible as-of CMU trades matched on or after their originally designated settlement date will be processed in CNS on the day they are submitted for comparison so long as they compare prior to the cut-off time established for same day settlement, which currently is 11:30 a.m.[6] As-of trades not eligible for CNS processing will settle on a trade-for-trade basis. Trades that match after the designated cut-off time will continue to be assigned a settlement date of the next business day.

In addition, because these trades are effectively guaranteed upon comparison, risk associated with the trades will be mitigated through the existing component of the Clearing Fund formula, as set forth in Procedure XV (Clearing Fund Formula and Other Matters), that is designed to mitigate the risk to NSCC associated with trades that are processed on a settlement cycle shorter than three days. Under this component, activity specified for a shortened settlement cycle is isolated, and a charge is calculated.[7]

III. Discussion

Section 19(b) of the Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. Section 17A(b)(3)(F) of the Act requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions.[8] The Commission believes that NSCC's rule change is consistent with this Section because it should facilitate the prompt and accurate clearance and settlement of securities by increasing automated trade processing and by expanding the types of trades eligible for CNS netting and NSCC settlement.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular Section 17A of the Act and the rules and regulations thereunder. In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR–NSCC–2007–11) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.[9]

Florence E. Harmon,

Deputy Secretary.

[FR Doc. E7–18825 Filed 9–24–07; 8:45 am]

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[3] Securities Exchange Act Release No. 50026 (July15, 2004), 69 FR 43650 [File No. SR–NSCC–2004–01].

[4] NSCC's systems did not have the capacity forsame day settling trades for fixed income transactions in 2004.

[5] The settlement of cash and next day CMU tradeswhich are compared by NSCC will continue to be the responsibility of the parties to the trades.

[6] In addition, references in Procedure VII (CNSAccounting Operation) that currently note that debt securities are not eligible for such accelerated settlement will be removed.

[7] The component calculates a charge based on theaverage of a member's charges for the specified activity on the three days with the highest charges calculated for the specified activity over the most recent twenty day period. Securities Exchange Act Release No. 54816 (November 27, 2006), 71 FR 69604 [File No. SR–NSCC–2006–09].

[8] 15 U.S.C. 78q–1(b)(3)(F).

[9] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–56455; File No. SR–NYSE–2007–83]

Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Proposed Rule Change Relating to NYSE Rule 104.10 (''Dealings by Specialists'')

September 18, 2007.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on September 14, 2007 the New York Stock Exchange LLC (''NYSE'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'' or ''SEC'') the proposed rule change as described in Items I, II, and III below, which Items have been substantially 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 is proposing to amend NYSE Rule 104.10 to: (i) Extend the duration of the pilot program applicable to Conditional Transactions as defined in Rule 104.10(6)(iv) to March 31, 2008; (ii) remove the ''active securities'' limitation on Conditional Transactions that establish or increase a specialist's position and reach across the market to transact with the NYSE's published quote; and (iii) make certain conforming changes to Rule 104.10(5). The text of the proposed rule change is available at NYSE, the Commission's Public Reference Room, and *http://www.nyse.com.*

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 NYSE 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 NYSE has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

[1] 15 U.S.C 78s(b)(1).

[2] 17 CFR 240.19b–4.

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

1. Purpose

(1) *Rule Filing History.*

On October 5, 2006, to coincide with the Exchange's implementation of Phase III of the NYSE HYBRID MARKET℠, the NYSE began operating on a pilot basis, among other rules, changes to Rule 104.10 (''Stabilization Rule'').[3] The Stabilization Rule governs specialists' dealings in assigned stocks including restrictions on specialists' ability to trade as a dealer in their assigned stocks. As will be described in greater detail below, the Stabilization Proposal provided additional opportunities for specialists to trade on a proprietary basis. On December 1, 2006, the Commission approved the Stabilization Proposal but required that subsection 104.10(6) of the Rule continue to operate as a pilot (''Conditional Transactions'') through June 30, 2007.[4]

(2) *Summary of the Stabilization Proposal.*

Rule 104 governs specialist dealings in the market. Specialists' transactions for their own accounts are subject to specific expectations of performance. These include a specialist's affirmative and negative obligations. Pursuant to these obligations specialists have a duty to ensure that his or her principal transactions are designed to contribute to the maintenance of price continuity with reasonable depth.

The affirmative obligation requires a registered specialist to maintain adequate minimum capital based on his or her registered securities and use said capital to engage in a course of dealings for his or her own account to assist in the maintenance, so far as practicable, of a fair and orderly market.[5] Thus, pursuant to the affirmative obligations, registered dealers on primary exchanges are required to commit the dealer's capital in their registered securities in order to maintain a fair and orderly market.

The negative obligation, which is part of Exchange Rule 104 requires that specialists allow public orders to be executed against each other without undue dealer intervention and that specialists not deal in a manner that is inconsistent with the overall objective of maintaining a fair and orderly market. Specifically, Rule 104(a) provides:

> No specialist shall effect on the Exchange purchases or sales of any security in which such specialist is registered, for any account in which he, his member organization or any other member, allied member, or approved person, (unless an exemption with respect to such approved person is in effect pursuant to Rule 98) in such organization or officer or employee thereof is directly or indirectly interested, unless such dealings are reasonably necessary to permit such specialist to maintain a fair and orderly market, or to act as an odd-lot dealer in such security.

Thus, prior to the Stabilization Proposal, NYSE Rule 104.10(5) required that specialist proprietary transactions be effected in a reasonable and orderly manner in relation to the general market, the market in their assigned stocks, and the adequacy of the specialist's position to the immediate and reasonably anticipated needs of the market. For example, a specialist was not permitted to effect a transaction that would acquire or increase a position unless it was necessary to render the specialist's position adequate for the immediate or anticipated needs of the market. Specialists were precluded from purchasing stock at a price above the last sale (in the same trading session) or from purchasing more than 50% of the stock offered on a ''zero plus tick'' (*i.e.* at the same price as the last sale, when such last sale was higher than the previous, differently priced sale of stock on the Exchange). Rule 104.10(6) applied similar standards when a specialist was liquidating or reducing a position. A specialist could, however, effect these types of transactions with the approval of a floor official.

The Stabilization Proposal retained the basic standard that a specialist's dealings must be reasonably necessary for the maintenance of a fair and orderly market, and that transactions that are with the trend of the market may have to be accompanied by appropriate re-entry on the opposite side of the market. In place of the then existing last transaction or ''tick'' test, the Exchange proposed to identify four types of transactions: ''Neutral,'' ''Non-Conditional'' ''Conditional'' and ''Prohibited.''

Neutral Transactions are purchases or sales that liquidate or decrease a specialist's position. These transactions must be effected in a fair and orderly manner to render the specialist position adequate to the market's needs, consistent with the specialist's negative obligations, but are not subject to price restrictions or to floor official approval. The obligation to maintain a fair and orderly market may require the specialist to enter the market on the opposite side, which could be the case if market conditions required the specialist to meet his affirmative obligations. The NYSE's rationale for this change was based in part on the recognition that position-reducing transactions are beneficial to the market because the specialists are adding liquidity to the market.

Non-Conditional Transactions are seven enumerated types of trades which increase or establish a position other than transactions that reach across the market.[6] Specialists are permitted to effect these transactions without regard to price and without floor official approval. The NYSE believes that these transactions, because they reflect instances where an independent source establishes the price, are unlikely to create a conflict of interest or to ''lead the market.'' Even though these transactions may establish the bid or offer, they are initiated by other market participants and not by the specialist. The NYSE also believes that, in the Hybrid Market where trading is substantially electronic, the speed and frequency of executions and quote changes preclude the specialist from being able to track accurately price ticks or to allow for floor official involvement. Re-entry on the opposite side of the market may be required for

[3] *See* Securities Exchange Act Release No. 54578 (October 5, 2006), 71 FR 60216 (October 12, 2006) (SR–NYSE–2006–82). On October 6, 2006, NYSE specialist firms LaBranche & Co. and Kellogg Specialist Group commenced operating pursuant to the Stabilization Rule in two NYSE-listed securities, American Express Company (AXP) and Equity Office Property Trust (EOP), respectively.

The operation of the Pilot implemented pursuant to SR–NYSE–2006–82 was later modified on October 13, 2006 to, among other things, clarify that Rule 104.10(6) was included in the operation of the Pilot. *See* Securities Exchange Act Release No. 54610 (October 16, 2006), 71 FR 62142 (October 23, 2006) (SR–NYSE–2006–84).

The proposed amendments to the Stabilization Rule (collectively referred to herein as ''Stabilization Proposal'') were filed on September 22, 2006 in SR–NYSE–2006–76. On October 25, 2006, the Exchange amended SR–NYSE–2006–76 to clarify certain provisions of the proposal, which was ultimately approved by the Commission on December 1, 2006. *See* Securities Exchange Act Release No. 54860 (December 1, 2006), 71 FR 71221 (December 8, 2006) (SR–NYSE–2006–76).

[4] *See* Securities Exchange Act Release No. 54860, *supra* note 3. On June 28, 2007 the Exchange filed with the Commission to extend the operation of the Stabilization Pilot until September 30, 2007. *See* Securities Exchange Act Release No. 55995 (June 29, 2007), 72 FR 37288 (July 9, 2007) (SR–NYSE–2007–58).

[5] *See* 17 CFR 240.11b–1.

[6] NYSE Rule 104.10(5)(i)(a)(II)(b) states that the transactions without regard to price may be made in order to: (i) Match another market's better bid or offer price; (ii) bring the price of a security into parity with an underlying or related security or asset; (iii) add size to an independently established bid or offer on the exchange; (iv) purchase at the published bid price on the Exchange; (v) sell at the published offer price on the Exchange (vi) purchase or sell at a price between the Exchange published bid and published offer; and (vii) purchase below the published bid or sell below the published offer on the Exchange.

the specialist to meet its affirmative obligations or to maintain a fair and orderly market.

Prohibited Transactions are certain transactions during the last 10 minutes of trading and are designed to prevent the specialist from setting the closing price.

Conditional Transactions are specialists' transactions in an active security that establishes or increases a position and reaches across the market to trade as the contra-side to the Exchange published bid or offer. Conditional transactions may only be executed in an ''active security.'' Active securities include those securities that are part of the S&P 500 Stock Index(c), securities trading on the Exchange during the first 5 trading days following their initial public offering, and securities declared to be active securities by a floor official.[7]

Conditional Transactions may have additional re-entry obligations pursuant to the rule. Specifically, pursuant to NYSE Rule 104.10(6)(iii) ''Appropriate'' re-entry means ''re-entry on the opposite side of the market at or before the price participation point or the ''PPP'').[8] Depending on the type of Conditional Transaction a specialist's obligation to re-enter may be immediate or subject to the same re-entry conditions of Non-Conditional Transactions.[9] In any event, Conditional Transactions remain subject to a specialist's overall negative obligation as discussed above.

Specialist transactions in securities not within the definition of ''active'' securities continue to be governed by the ''tick test'' and floor official approval requirements described above that are now set forth in Rule 104.10(5)(i)(B)(I).

In the Stabilization Proposal, the Exchange asserted that it believed the types of transactions described above were suitable for all securities. While the Commission acknowledged the considerable changes in the national market system, it stated that it believed that the Stabilization Proposal represented a significant change in the roles and obligations of specialist at the Exchange and thus required that the NYSE to implement the proposed Conditional Transactions only for active securities as a pilot.[10] The Commission further stated that, before it decided whether to extend the operation of the rule or to approve the rule on a permanent basis, it would require the NYSE to provide data and analysis on the impact of the rule change.[11]

(3) *The Exchange's Analysis of the Conditional Transaction Pilot.*

The Exchange has closely monitored its market quality as it made changes to its operations, including the implementation of the Hybrid Market and the pilot that allowed specialists to effect Conditional Transactions. The Exchange has performed a review [12] of the market quality for the period July 1, 2006 to September 30, 2006, compared to the market quality for the period from April 1, 2007 through June 30, 2007 and the NYSE states that its review shows that overall there has been a narrowing of the effective spread for marketable orders and a lowering of volatility. The percentage of trades executed automatically substantially increased. Other indicators remained generally the same except for the percentage of times that the NYSE set the National Best Bid or Offer.

In addition, the Exchange reviewed data related to the specialists' re-entry requirement. Specifically, the Exchange reviewed the specialist's re-entry quote and execution activity on the opposite side of the market at 30-second and one-minute intervals for the month of April 2007. The Exchange states that the data showed that specialists effected Conditional Transactions sparingly and that, in those instances where specialists effected Conditional Transactions, the data showed that specialist overall complied with their obligations to re-enter liquidity on the opposite side of the market.

The Exchange further compared the 84 securities that are listed on the NYSE and are included in the S&P 500 index (''S&P 500'') operating in the Conditional Transaction Pilot that that had the lowest consolidated volume for the months of March and April 2007. The 84 securities were divided into two deciles containing 42 securities per decile. The Exchange created a matched sample for these two deciles by finding other NYSE-listed securities not included in the S&P 500 (''non-S&P 500'') that had comparable consolidated volumes, Volume Weighted Average Price (''VWAP'') and market capital.[13] The Exchange believes that its review showed that there was no discernible difference between the change in market quality in the lowest two deciles of the S&P 500 securities operating pursuant to the Conditional Transaction Pilot as compared to similar securities in the non-S&P 500 securities. The Exchange noted a difference in the market quality statistics for the S&P 500 securities as compared to the non-S&P 500 matched sample. However, upon further review, the Exchange noted that the differences were present both before and after the Conditional Transaction Pilot, which suggests that a factor other than the Conditional Transaction Pilot was the cause of the noted difference. The Exchange believes that the most probable cause of the noted difference was the inclusion in the S&P 500. The

[7] Pursuant to current NYSE Rule 104.10(6)(c), a Floor Official may designate a security active when such security has exhibited substantially greater than normal trading volume and is, in the Floor Official's judgment likely to continue to sustain such higher volume during the remainder of the current trading session.

[8] NYSE Rule 104.10(6)(iv)(a) provides that the PPP identifies the price at or before which a specialist is expected to re-enter the market after effecting a Conditional Transaction. PPPs are only minimum guidelines and compliance with them does not guarantee that a specialist is meeting its obligations. The Exchange issued guidance regarding PPPs in January 2007. *See* NYSE Member Education Bulletin 2007–1.

[9] NYSE Rule 104.10(6)(iv)(c) requires immediate re-entry following Conditional Transactions that is:

(I) A purchase that (1) reaches across the market to trade with an Exchange published offer that is above the last differently priced trade on the Exchange and above the last differently priced published offer on the Exchange, (2) is 10,000 shares or more or has a market value of $200,000 or more, and (3) exceeds 50% of the published offer size.

(II) A sale that (1) reaches across the market to trade with an Exchange published bid that is below the last differently priced trade on the Exchange and below the last differently priced published bid on the Exchange, (2) is 10,000 shares or more or has a market value of $200,000 or more, and (3) exceeds 50% of the published bid size.

Pursuant to current NYSE Rule 104.10(6)(v) Conditional Transactions that involve:

(a) A specialist's purchase from the Exchange published offer that is priced above the last differently-priced trade on the Exchange or above the last differently-priced published offer on the Exchange; and

(b) A specialist's sale to the Exchange published bid that is priced below the last differently-priced trade on the Exchange or below the last differently-priced published bid on the Exchange are subject to the re-entry requirements for Non-Conditional Transactions pursuant to NYSE Rule 104.10(5)(i)(a)(II)(c).

Rule 104.10(5)(i)(a)(II)(c) provides:

Re-entry Obligation Following Non-Conditional Transactions—The specialist's obligation to maintain a fair and orderly market may require re-entry on the opposite side of the market trend after effecting one or more Non-Conditional Transactions. Such re-entry transactions should be commensurate with the size of the Non-Conditional Transactions and the immediate and anticipated needs of the market.

[10] *See* Securities Exchange Act Release No. 54860, *supra* note 3, at 71230.

[11] *Id.*

[12] *See* Appendix 3A, which is available on the NYSE Web site at the following link: *http://www.nyse.com/Frameset.html?displayPage=http://apps.nyse.com/commdata/pub19b4.nsf/rulefilings?openview.*

Appendix 3A is also available on the Commission Web site at *http://www.sec.gov/rules/sro/nyse.shtml.*

[13] *See* Appendices 3B and 3C, which are available on the NYSE Web site at the following link: *http://www.nyse.com/Frameset.html?displayPage=http://apps.nyse.com/commdata/pub19b4.nsf/rulefilings?openview.*

Appendices 3B and 3C are also available on the Commission Web site at *http://www.sec.gov/rules/sro/nyse.shtml.*

stocks in the S&P 500 appear to have inherently different market quality characteristics from those not in the S&P 500. The changes in market quality were similar for both groups. The Exchange therefore believes that the Conditional Transaction Pilot was not the cause of the market quality differences in the samples. Therefore, the Exchange believes that the data supports the conclusion that the Conditional Transaction Pilot has not had a detrimental effect on market quality.

Thus, in analyzing the data related to the Conditional Transaction Pilot, the Exchange believes that it is clear that specialists have acted appropriately in regard to Conditional Transactions and have re-entered the market as required, with no discernable adverse impact on liquidity or market quality. The Exchange therefore believes that Conditional Transaction Pilot should be modified to include all stocks traded on the NYSE.

(4) *Inclusion of All NYSE Traded Securities in the Conditional Transaction Pilot.*

The NYSE now seeks approval to extend the term of the Conditional Transaction Pilot to March 31, 2008 and to make it applicable to all securities traded on the NYSE. As explained more fully below, the Exchange believes that it is appropriate to provide specialists the same ability to effect Conditional Transactions in all securities traded on the Exchange.

(5) *Importance of the Specialist Role to the NYSE's Hybrid Market Model.*

The Exchange states that the specialist is critical to the NYSE's Hybrid Market model. Advances in technology have virtually obviated the specialists' time and place advantage. The rate of trading participation by specialists in specialist stocks has been significantly reduced. Therefore, the Exchange believes that the basis for concern over specialist conflicts of interest (and the consequent ability to trade to the detriment of the public) is also diminished. The NYSE believes that these factors and specialist re-entry obligations support the expansion of specialists trading opportunities in all of the securities traded on the NYSE.

The amendments to NYSE Rule 104.10(5) and (6) in this filing should be seen as part of the NYSE's goal of providing the market with the ability to seek the best price by submitting orders to a traditional floor-based auction process or by obtaining virtually instantaneous execution in an electronic platform. The NYSE believes that specialists play a critical role in achieving this goal, but it is in many ways a different role from the ''traditional'' function of specialists prior to implementation of the NYSE's current market structure. The Exchange states that, most importantly, it has attempted to balance concerns over the potential conflict of interest between specialists' agency function in the auction process and the specialists' ability (and need) to trade for their own account as a dealer.

The Exchange believes that specialists provide an extraordinary benefit to the NYSE market by using their capital to cushion market volatility. Specialists' capital commitment provides depth, and lowers volatility and overall execution costs for investors. Furthermore, specialists add liquidity to the market when there is little or no liquidity, bridging the gap between supply and demand by purchasing when no one else is buying and by overall maintaining a fair and orderly market. In order for specialists to continue providing that benefit, they must be allowed greater flexibility in trading for their dealer accounts to be competitive with other market participants in times of market stability so that they may be adequately positioned to step in during times of market instability. The Exchange believes that the ability of the specialists to effect Conditional Transactions allows specialists, to a greater degree, to manage the inventory of the dealer account to provide more liquidity against the market trend and thus moderate volatility.

Moreover, the NYSE believes human judgment is particularly valuable in less liquid securities because the service provided by specialists is even more critical during the opening and closing of trading in such securities, particularly in times of uncertainty such as when an earnings surprise, news, or an outside event leads to market volatility and/or instability. In these cases, the specialists' trading judgment, exercised in carrying out their affirmative obligations, results in reduced volatility and more stable prices.

But while the Hybrid Market is intended to combine the benefits of specialist and floor broker expertise with the speed, certainty and anonymity of electronic executions, implementation of this system has created a significantly different trading environment for specialists. Historically, the NYSE specialist's unique dual role as broker and dealer afforded him or her an informational advantage over other market participants because, in that role, the specialists served as the main conduit of the order flow information in his or her subject security. As a result of this information advantage, specialists trading for their own account were constrained by affirmative and negative obligations.

Today, the Exchange believes that there is a virtual elimination of the informational advantage of the specialist. Certain order types that previously required specialist intervention for execution are now handled systemically and automatically. For example, in December 2006 the Exchange changed its stop order handling process to make stop orders no longer visible to the part of the Display Book that the specialist ''sees.'' [14] Currently, when a transaction on the Exchange results in the election of a stop order that had been received prior to such transaction, the elected stop order is sent as a market order to the Display Book and the specialist's system employing algorithms where it is handled in the same way as any other market order. The specialist therefore has no information regarding the status of stop orders.

Moreover, the quantity and quality of information that is available solely to the specialist has decreased. In the auction market, the specialist had information about all orders on the Display Book and also received information from the Crowd. Floor Brokers, Registered Competitive Market Makers (''RCMMs'') and Competitive Traders (''CTs'') all interacted verbally with the specialists and each other in the Crowd at the trading post for each security. Through this interaction and the proximity of the other market participants, the specialist was in possession of information not readily available to all other market participants. In his or her position, the specialist had information directly from the Crowd and the Display Book. Additionally, the specialist was able to glean incidental information based on his or her observation of the communication between other market participants.

Currently, the Hybrid Market provides Floor brokers with electronic trading tools that have resulted in less personal and verbal interaction between Floor brokers and specialists.[15] A Floor broker is now able to electronically represent his or her customer's interest through the use of e-quotes and d-quotes.

[14] *See* Securities Exchange Act Release No. 54820 (November 27, 2006), 71 FR 70824 (December 6, 2006) (SR–NYSE–2006–65) (clarifying certain definitions and the systematic processing of certain orders in the Hybrid Market).

[15] Currently, approximately 90% of the transactions executed on the Exchange are done through electronic executions.

Moreover, the electronic representation need not take place directly in front of the post and panel where the security is traded as the Exchange definition of Crowd has expanded the physical area encompassed in a Crowd. Today, a Crowd is one of three trading zones which is one of the three trading rooms operating as part of the NYSE Floor. The verbal information the specialist was once able to obtain from Floor broker's expressed interest is greatly reduced. Moreover, the Exchange believes that the observations of Crowd to Crowd transactions offer little if any information to the specialists. A specialist at a trading post is unable to know with any degree of certainty the security being traded by Floor brokers electronically bidding and offering in front of him or her.

The Exchange believes that the reduced ability of a specialist to glean market information because a specialist's intervention is no longer required to receive an execution, the specialist's inability to see stop orders and the dramatic increase in transparency with respect to the Display Book through, among other things, Exchange initiatives like Exchange OPENBOOK™ make it clear that the specialist no longer possesses an information advantage over other market participants. In fact, it may be argued that the specialist has less information than some market participants with the increased internalization of orders. Often prior, to orders being sent to an exchange for execution, the broker-dealer will ''shop'' the order. In some instances, the broker-dealer will execute all or part the customer order against its principal account with any residual being sent to an exchange for execution. Internalization of order flow limits price discovery and does not result in transparency. As such, the specialist can be said, in certain instances, to be at an informational disadvantage to other market participants.

The Exchange states that in approving the Stabilization Proposal, the Commission agreed with the Exchange that trade-by-trade negative compliance obligations previously embodied in the so-called Saperstein Interpretation[16] established seventy years ago no longer address the realities of the modern market. The Commission's approval order stated:

> The Commission believes that eliminating the trade-by-trade standard with respect to the negative obligation should enhance the specialists' ability to fulfill its obligation to maintain a fair and orderly market. The Commission believes that increased automation and competition—both within the Hybrid Market and in the markets generally—are significant factors, among others, that affect the ability of specialists to make trade-by-trade analysis regarding their negative obligations. The Commission finds that permitting specialists to consider the reasonable necessity of their transactions under negative obligations without a transaction-by-transaction test, is appropriate and consistent with the Act. The Commission emphasizes that it is not eliminating the negative obligation (footnote omitted). Therefore, specialists must continue to assess their need to trade and limit their proprietary trades to those reasonably necessary to allow the specialists to maintain a fair and orderly market.[17]

The re-interpretation of the Saperstein letter thus moved away from defining stabilization in terms of the last sale to focus on market conditions, the type of trade in question and the specialists' existing position.

The Exchange's proposal to allow specialists to effect Conditional Transactions in all securities is a request to further address the realities of the current market. The Exchange states that it does not in any way reduce the obligations imposed on them pursuant to NYSE Rule 104 to re-enter a transaction on the opposite side of the market and their negative obligation. The Exchange believes that these critically distinguishing obligations imposed on NYSE specialists, coupled with the empirical evidence that, when given the opportunity to effect Conditional Transactions in less liquid securities there is no discernable diminishment of market quality, justifies the extension of the specialist ability to effect Conditional Transactions in all securities.

For the reasons stated above, the Exchange believes that extending the ability of the specialist to effect Conditional Transactions to all securities will allow specialists to more effectively meet their affirmative and negative obligations by giving them the tools to better manage the inventory of the dealer account.

(6) *Exchange Continued Data Provision to the Commission.*

The Exchange represents that it will continue to provide the Division of Market Regulation and the Office of Economic Analysis with statistics related to market quality, specialist trading activity and sample statistics. The sample statistics include the daily Consolidated Tape volume in shares, daily number of trades, daily high-low volatility in basis points, and daily close price in dollars.

The Exchange will also calculate the specialist profit on round-trip Hit Bid and Take Offer (''HB/TO'') executions. This will be accomplished by measuring the specialist profit on HB/TO activity by taking the round-trip trading profits for all HB/TO trades where the specialist executes an offsetting trade within 30 seconds. In cases where the volume of the offsetting execution is less than the size of the HB/TO execution, the calculation will only include profits realized within the 30-second window.

The Exchange will further calculate the quote-based specialist re-entry ratio. Each re-entry price level will be categorized and reported separately. For example, if the specialist buys from the offer at $50.00 and then re-enters at $50.01, then this is categorized as a one cent re-entry. Similarly, if the specialist buys from the offer at $50.00 and then re-enters at $50.02, then this is categorized as a two cent re-entry. The categories will be in cent intervals at 0, 1, 2, 3, 4, and 5 or more cents. The time window for these calculations will also be in 30 seconds.

In addition, the Exchange will provide the Commission with data related to the average realized spread on specialist HB/TO executions. These calculations will be done using the same formula as Rule 605 of Regulation NMS under the Act.[18] Specifically, the average realized spread should be a share-weighted average of realized spreads. For specialist buys, it is double the amount of difference between the execution price and the midpoint of the consolidated best bid and offer five minutes after the time of HB/TO execution. For specialist sells, it is double the amount of difference between the midpoint of the consolidated best bid and offer five minutes after the time of HB/TO execution and the execution price.

All of the aforementioned information will be provided to the Commission on a monthly basis. The Exchange represents that it will also maintain average measures for each stock-day during a particular month in order to provide such information to the Commission upon request.

(7) *Surveillance.*

As noted in the NYSE's original Stabilization Rule filing, NYSE Regulation (''NYSER'') believes that it has appropriate surveillance procedures in place to surveil for compliance with the negative obligations of specialists. NYSER monitors, using a pattern and

[16] Securities Exchange Act Release No. 1117, 1937 SEC LEXIS 357 (March 30, 1937).

[17] *See* Securities Exchange Act Release No. 54860, *supra* note 3.

[18] 17 CFR 242.605.

practice and/or outlier approach, specialist activity that appears to cause or exacerbate excessive price movement in the market (since such transactions would appear to be in violation of a specialist's negative obligation). In this connection, NYSER surveils for specialist compliance with the PPP re-entry requirements and, based on its preliminary reviews of surveillance data, has not identified significant compliance issues to date. The Division of Market Surveillance of NYSER also monitors specialist trading to cushion such price movements.

(8) *Conclusion.*

The Exchange seeks to be able to modify and change its business model in order to continue to improve market quality. If the Exchange is to do this then it must be allowed to provide the specialists that operate on the Exchange with the flexibility to compete. The Exchange believes that this flexibility can be achieved by extending the specialists ability to effect Conditional Transactions in all securities.

The Exchange believes that its current stabilization rules do not afford specialists trading on the NYSE the necessary flexibility to manage the dealer account inventory. The Exchange believes that these rules are antiquated and inconsistent with the electronic trading environment that has virtually eliminated the specialists' agency role and information advantage. The Exchange believes that the proposed amendments regarding specialists' ability to effect Conditional Transactions will allow specialists on the Exchange to efficiently and systematically trade and quote in their securities and thus be in a position to fluidly manage their risk. Providing the specialists with the required flexibility to compete will add value to the Exchange market by encouraging them to continue to commit capital, thus benefiting the marketplace by increasing liquidity at prices outside the best bid and offer, bridging temporary gaps in supply and demand, and dampening volatility.

Given all the above, the NYSE believes that allowing specialists to effect Conditional Transactions in all securities on pilot basis until March 31, 2008 is appropriate at this time.

2. Statutory Basis

The Exchange believes that the basis under the Act for this proposed rule change is the requirement under Section 6(b)(5) [19] of the Act that an Exchange have rules that are 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 proposed rule change also is designed to support the principles of Section 11A(a)(1) [20] under the Act in that it seeks to assure economically efficient execution of securities transactions.

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 states that the proposed rule change was developed in response to concerns expressed by certain member organizations. During the drafting of the rule filing and proposed rule, those member organizations reviewed an initial draft and provided the Exchange with written comments relating to specialists' obligations and actions during periods of instability. The Exchange states that it has incorporated these comments into the final rule proposal, but the Exchange has neither solicited nor received written comments on the final proposed rule change.

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 NYSE 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 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.* Please include File Number SR–NYSE–2007–83 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 20549–1090.

All submissions should refer to File Number SR–NYSE–2007–83. 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, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of 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–2007–83 and should be submitted on or before October 16, 2007.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[21]

Florence E. Harmon,

Deputy Secretary.

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[19] 15 U.S.C. 78f(b)(5).

[20] 15 U.S.C. 78k–1(a)(1).

[21] 17 CFR 200.30–3(a)(12).