

Exchange. On December 30, 2002, the Exchange submitted Amendment No. 1 to the proposed rule change.³ The proposed rule change, as amended by Amendment No. 1, was published in the **Federal Register** on January 28, 2003.⁴ One comment was received on the published proposed rule change, as amended by Amendment No. 1.⁵ On March 24, 2003, the Exchange filed Amendment No. 2 to the proposed rule change.⁶ This order approves the proposed rule change, as amended by Amendment Nos. 1 and 2. Amendment No. 2 is being approved on an accelerated basis.

I. Description of the Proposal

NYSE Rule 36 governs the establishment of telephone or electronic communications between the Exchange's Trading Floor and any other location. Rule 36.20 prohibits the use of portable telephone communications between the Trading Floor and any off-Floor location. According to the Exchange, the only way that voice communication can be conducted today by Floor brokers between the Trading Floor and an off-Floor location is by means of a telephone located at a broker's booth. Communications often involve a customer calling a broker at the booth for "market look" information. A broker may not use a portable phone currently in a trading crowd at the point of sale to speak with a person located off the Floor.

The Exchange proposes to amend NYSE Rule 36 to permit a Floor broker

to use an Exchange authorized and issued portable telephone on the Floor with the approval of the Exchange. As noted above, the Exchange currently does not permit the use of portable telephones on its Floor. Thus, a Floor broker would be permitted to engage in direct voice communication from the point of sale to an off-Floor location, such as a member firm's trading desk or the office of one of the broker's customers. Such communications would permit the broker to accept orders consistent with Exchange rules, provide status and oral execution reports as to orders previously received, as well as provide "market look" observations as are routinely transmitted from a broker's booth location today. Only portable telephones authorized and issued by the Exchange would be permitted on the Exchange Floor. Any other type of portable telephone would continue to be prohibited.

Under the proposal, both incoming and outgoing calls, and orders on such calls, would be allowed, provided the requirements of all other Exchange rules have been met. A broker would not be permitted to represent and execute any order received as a result of such voice communication unless the order was first properly recorded by the member and entered into the Exchange's Front End Systemic Capture ("FESC").⁷ In addition, Exchange rules require that any Floor broker receiving orders from the public over portable phones must be properly qualified to do direct access business under Exchange Rules 342 and 345, among others.⁸ As a result, NYSE

Rule 36 would be amended to specifically state that any Floor broker receiving orders from the public over portable phones must be properly qualified to do a public customer business.

Furthermore, the Exchange originally proposed in Amendment No. 1 that it would not permit portable communications at the point of sale for orders in ETFs, because there was an exception to NYSE Rule 123(e) that permitted orders in ETFs to first be executed and then entered into FESC.⁹ In its original filing, the NYSE stated that technical restraints would be developed to implement this policy, thus preventing the use of portable phones where ETFs currently trade. The NYSE, however, determined that technical restraints could not be developed to prevent the use of portable phones in the Expanded Blue Room of the NYSE where ETFs currently trade. As a result, in Amendment No. 2, the Exchange proposed to eliminate the exception to NYSE Rule 123(e) for ETFs¹⁰ and allow the use of portable phones for orders in ETFs.¹¹ Orders in ETFs would thus be subject to the same FESC requirements as orders in any other security listed on the Exchange. The Exchange states that requiring orders in ETFs to be first entered into FESC before execution or representation on the Floor would place them on an equal footing with orders in other securities with respect to order entry and recording procedures. As a result, the Exchange believes that allowing portable phones for orders in ETFs should be permitted. The Exchange also notes that the same surveillance procedures applicable to trading in all other equities would also apply to ETFs.

Although the Exchange originally stated in Amendment No. 1 that the proposal would be implemented on a six-month pilot basis from the date of Commission approval, and contained a

(November 21, 2001), Information Memo 01-18 (July 11, 2001) (available on www.nyse.com/regulation/regulation.html), and Information Memo 91-25 (July 8, 1991).

⁹ See Securities Exchange Act Release No. 45246 (January 7, 2002), 67 FR 1527 (January 11, 2002) (SR-NYSE-2001-52) (discussing an exception to FESC that allowed orders in ETFs to be entered within 90 seconds of execution for a one-year pilot period). See also Securities Exchange Act Release No. 46713 (October 23, 2002), 67 FR 66033 (October 29, 2002) (SR-NYSE-2002-48) (extending the exception until January 5, 2004), and note 7 and accompanying text.

¹⁰ The Exchange stated in Amendment No. 2 that a separate proposed rule change would be filed with the Commission to eliminate the exception in Supplementary Material .23 of NYSE Rule 123(e) for ETF orders. See SR-NYSE-2003-09 which discusses in more detail the rational for eliminating the exception.

¹¹ See Amendment No. 2, *supra* note .

³ See letter from Darla C. Stuckey, Corporate Secretary, NYSE, to Nancy J. Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated December 30, 2002 ("Amendment No. 1"). Amendment No. 1 replaces the filing in its entirety and provides, in the proposed rule text and the purpose section of the filing, clarification and further details on the use of Exchange authorized and issued portable telephones on the Exchange Floor, and also proposes, among others, a pilot program for six months.

⁴ See Securities Exchange Act Release No. 47221 (January 21, 2003), 68 FR 4261.

⁵ See letter from Thomas N. McManus, Executive Director and Counsel, Morgan Stanley & Co. Incorporated, to Jonathan G. Katz, Secretary, Commission, dated March 6, 2003 ("Morgan Stanley Letter").

⁶ See letter from Darla C. Stuckey, Corporate Secretary, NYSE, to Nancy J. Sanow, Assistant Director, Division, Commission, dated March 21, 2003 ("Amendment No. 2"). Amendment No. 2 specifies the timing for the notification and implementation of the six-month pilot program as well as for the completion of a study, and eliminates the proposed prohibition against using Exchange authorized and provided portable telephones for orders in Investment Company Units (as defined in Section 703.16 of the Listed Company Manual), also known as Exchange-Traded Funds ("ETFs"). See notes 11 through 15, and accompanying text. Amendment No. 2 also extends the statutory time for the Commission to take action on the filing for a period of forty-five days.

⁷ See Securities Exchange Act Release No. 43689 (December 7, 2000), 65 FR 79145 (December 18, 2000) (SR-NYSE-98-25). See also Securities Exchange Act Release No. 44943 (October 16, 2001), 66 FR 53820 (October 24, 2001) (SR-NYSE-2001-39) (discussing certain exceptions to FESC, such as orders to offset an error, or a bona fide arbitrage, which may be entered within 60 seconds after a trade is executed). The Exchange believes that the exceptions to FESC for bona fide arbitrage and orders to offset transactions made in error do not raise unique issues with respect to the use of portable telephones on the Floor. The NYSE believes that the purpose of the FESC requirement is to ensure that orders are entered into an Exchange data base before they are executed, thereby minimizing the possibility that orders are being initiated on the Floor in contravention of NYSE and SEC rules. Members may, however, initiate bona fide arbitrage and error offset orders on the Floor, as expressly permitted by NYSE Rule 112 and SEC Rule 11a-1. The Exchange believes that the use of portable telephones, therefore, does not raise on-Floor trading concerns as to these types of orders because these orders are not normally transmitted by phone. Telephone conversation between Jeff Rosenstock, Senior Special Counsel, NYSE, and Cyndi Rodriguez, Special Counsel, Division, Commission, on April 11, 2003.

⁸ For more information regarding Exchange requirements for conducting a public business on the Exchange Floor, see Information Memo 01-41