

commitment to complete, within three months of Commission approval, a study of communications on the Exchange Floor pursuant to the recommendation of an Independent Consultant retained by the Exchange,¹² the Exchange now proposes in Amendment No. 2 to provide for Exchange authorized and provided portable phones on the Exchange Floor as a six-month pilot beginning on or about May 1, 2003.¹³ Furthermore, the Exchange has committed to complete the study within three months of implementation of the pilot program, which would be on or about August 1, 2003.¹⁴ The Exchange has also committed to notify the Division, OCIE, and the Exchange's membership within one week prior to the actual implementation date of this proposal.¹⁵

In its filing, the Exchange also noted that specialists are subject to separate restrictions in NYSE Rule 36 on their ability to engage in voice communications from the specialist post to an off-Floor location.¹⁶ The Exchange's proposed amendment to NYSE Rule 36 would not apply to specialists, who would continue to be prohibited from speaking from the post to upstairs trading desks or customers.

II. Discussion

After careful review, the Commission finds that the proposed rule change and Amendment Nos. 1 and 2 are consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.¹⁷ In particular, the Commission finds that the proposal, as amended, is consistent with section 6(b)(5) of the Act,¹⁸ which requires, among other things, that the Exchange's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and

facilitating transactions in securities, 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.

Specifically, the proposal, as amended, would eliminate the requirement that an off-Floor customer must communicate with the Exchange Floor by calling a broker's booth and using the booth clerk as an intermediary to access the trading crowd, which may help to facilitate transactions in securities consistent with section 6(b)(5) of the Act.¹⁹ While the Commission believes that the proposal to permit a Floor broker to use an Exchange authorized and issued portable telephone on the Floor on a six-month pilot basis could provide certain benefits, as stated by the NYSE in its filing, such as more direct access to the Exchange's trading crowds, and increased speed in the transmittal, and execution, of orders, it believes there are certain concerns.

The prohibition on the use of portable telephones in trading crowds on the NYSE was adopted in 1988.²⁰ In approving the prohibition, the Commission noted that the use of portable telephones in the trading crowd was different from such access at a booth phone. In particular, the Commission stated that the ability of a customer to communicate directly with a broker in the trading crowd could provide a significant time and place advantage to the customer, who invariably would be a large or institutional customer. The Commission also noted certain concerns that could result from such advantage.

While the Commission recognized that the NYSE had reasonable concerns for imposing the portable phone prohibition, the Commission noted that the NYSE's decision to prohibit the use of portable telephones on the Floor was not the only approach that could be consistent with the Act. The Commission further stated that its order did not foreclose an exchange from devising a program that would permit the use of portable telephones.

Under NYSE rules, a broker would not be permitted to represent and execute an order unless it was inputted into FESC. In addition, the filing has been amended so that only Exchange authorized and issued portable telephones would be permitted on the Floor. The benefit of this requirement is that the Exchange would have access to all phone records. This ability to track phone calls, along with the data captured in FESC, should aid the Exchange in surveilling for compliance with Exchange rules and address concerns identified in the adoption of the original prohibition. In this regard, the Commission notes that proper surveillance is an essential component of any telephone access policy to an Exchange Trading Floor. Surveillance procedures should help to ensure that Floor brokers who are interacting with the public on portable phones are authorized to do so, as NYSE Rule 36 will require,²¹ and that orders are being handled in compliance with NYSE rules. The six-month pilot approval should provide the NYSE with an opportunity to review these procedures and address any potential concerns that have arisen during the pilot.

The Commission notes that the NYSE is expected to complete within three months of implementation of the portable phones a study of communications on the Exchange Floor, pursuant to a recommendation of an Independent Consultant retained by the Exchange.²² In addition to this study, the Commission requests that the Exchange report any problems, surveillance or enforcement matters associated with the Floor brokers use of an Exchange authorized and issued portable telephone on the Floor. If the NYSE decides to request permanent approval or an extension of the pilot, we would expect, in addition to the report due in three months, that the NYSE submit information documenting the usage of the phones, any problems that have occurred, and any advantages or disadvantages that have resulted.²³

In summary, the Commission notes that the proposal, by enabling customers to speak directly to a Floor broker in a trading crowd on Exchange authorized and issued portable phones, rather than being routed through the Floor broker booth, may help to expedite orders and make more direct the flow of

¹² See *In the Matter of New York Stock Exchange*, 70 S.E.C. Docket 106, Release No. 41574, 1999 WL 430863 (June 29, 1999).

¹³ See Amendment No. 2, *supra* note 6.

¹⁴ See Amendment No. 2, *supra* note 6.

¹⁵ See Amendment No. 2, *supra* note 6. The Commission notes that should the NYSE be unable to implement the filing on or about May 1st, it would have to submit a rule proposal under Section 19(b) of the Act to change the date.

¹⁶ See Securities Exchange Act Release No. 46560 (September 26, 2002), 67 FR 62088 (October 3, 2002) (SR-NYSE-00-31) (discussing restrictions on specialists' communications from the post).

¹⁷ In approving this proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹⁸ 15 U.S.C. 78f(b)(5).

¹⁹ 15 U.S.C. 78f(b)(5).

²⁰ The proposal resulting in the adoption of the prohibition was in response to a Commission order setting aside actions by the Exchange denying two of its members permission to install telephone connections to communicate from the Exchange Floor with non-member customers located off-Floor. See Securities Exchange Act Release No. 24429, May 6, 1987, 38 SEC Doc. 432. The NYSE's proposal that was ultimately approved by the Commission permitted access to non-member customers at the Floor booth, but prohibited such access through portable phones that could be used in the trading crowd.

²¹ See note 8 and accompanying text for other NYSE requirement that Floor brokers be properly qualified before doing a public customer business.

²² See *supra* note 12.

²³ This information along with any proposal to extend, or permanently approve, the pilot should be submitted at least two to three months prior to the expiration of the six-month pilot.