

[shall] be placed upon the order slip or other *similar* record of the member[, or [his] member organization the name or designation of the account for which such order is to be executed. No change in such account name (*including related accounts*) or designation (*including error accounts*) shall be made unless the change has been authorized by [the] a member, [or another member,] allied member, or a person or persons designated under the provisions of Rule 342(b)(1). [in his organization who shall,] *Such person must*, prior to giving his or her approval of [such] the account designation change, be personally informed of the essential facts relative thereto and [shall] indicate his or her approval of such change in writing on the order or other similar record of the member or member organization. *The essential facts relied upon by the person approving the change must be documented in writing and maintained with the order or other similar record for at least three years, the first two in an easily accessible place as that term is used in Securities Exchange Act Rule 17a-4.*

Exceptions

Under exceptional circumstances, the Exchange may upon written request waive the requirements contained in (1), (2) and (3) above.

(b) Every order in any manner transmitted or carried to the Floor and [covered by (1) or (2) above to be] executed pursuant to Section 11(a)(1)(G) of the Act and Rule 11a1-1(T) thereunder *must* [shall] be identified in a manner that will enable the executing member to disclose to other members that the order is subject to those provisions.

(See also Rules 112A.10 and 123A.45.)

10 For purposes of this Rule, a person designated under the provisions of Rule 342(b)(1) to approve account name or designation changes must pass an examination acceptable to the Exchange.

INTERPRETATION

Rule 342 OFFICES—APPROVAL, SUPERVISION AND CONTROL

(a)(b)

.03 Annual Branch Office Inspection

[At least annual b]Branch office inspections by members and member organizations are expected to be conducted at least annually pursuant to this Rule, unless it has been demonstrated to the satisfaction of the Exchange that because of proximity, special reporting or supervisory practice, other arrangements[, may

satisfy the Rule's requirements. [certain offices may not warrant an annual inspection.] *All required inspections must be conducted by a person who is independent of the direct supervision or control of the branch office (i.e., not the Branch Office Manager, or any person who reports to such Manager, or any person to whom such Manager directly reports).* Written reports of these inspections, or the written authorization of an alternative arrangement, are to be kept on file by the organization for a minimum period of three years.

An annual branch office inspection program must include, but is not limited to, testing and independent verification of internal controls related to the following areas:

- 1) Safeguarding of customer funds and securities,*
- 2) Maintaining books and records,*
- 3) Supervision of customer accounts serviced by Branch Office Managers,*
- 4) Transmittal of funds between customers and registered representatives and between customers and third parties,*
- 5) Validation of customer address changes, and*
- 6) Validation of changes in customer account information.*

For purposes of this interpretation, "annually" means once in a calendar year.

* * * * *

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

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

1. Purpose

On August 15, 2002, the Exchange submitted to the Commission File No. SR-NYSE-2002-36, which proposed several rule amendments intended to strengthen members' and member organizations' supervisory procedures and internal controls. Included are amendments to NYSE Rule 342 ("Offices—Approval, Supervision and

Control") and the Interpretation to that Rule, NYSE Rule 401 ("Business Conduct"), NYSE Rule 408 ("Discretionary Power in Customers' Accounts"), and NYSE Rule 410 ("Records of Orders").

On November 18, 2002, Amendment No. 1 was submitted to the SEC, which added paragraph (b)(3) to NYSE Rule 401 to include "customer changes of investment objectives" with the enumeration of business activities subject to written policies and procedures.

The filing was published in the **Federal Register** for comment on November 27, 2002.⁷ The comment period, which ended January 17, 2003, resulted in letters from two NYSE member organizations (A.G. Edwards & Sons, Inc. and Charles Schwab & Co.), a letter from a non-NYSE member organization (Cadaret, Grant & Co.),⁸ and a letter from the Securities Industry Association ("SIA").⁹ Proposed rule text amendments representing the Exchange's response to industry comments were submitted to the Commission on April 25, 2003 as Amendment No. 2. Amendment No. 3 subsumes Amendment No. 2 and includes additional amendments requested by Commission staff. Several comments and concerns expressed in the A.G. Edwards, Schwab, and SIA letters are very similar and thus will be addressed collectively in this filing as remarks from the "Commenters." When an issue is unique to a particular letter, it will be noted. Amendments to SR-NYSE-2002-36 proposed by the Exchange in response to this collective commentary, as well as discussion of the issues raised, follow:

General Issue

The SIA suggests that, given implementation costs and business model differences, the proposed rule amendments should be adopted in the form of "principles for effective

⁷ See note 4 *supra*.

⁸ While this letter references the NYSE filing, its comments substantively address the comparable NASD filing (SR-NASD-2002-162), and therefore the comments made in this letter will not be discussed herein.

⁹ See letters from Brian Underwood, Senior Vice President, Director of Compliance, A.G. Edwards & Sons, Inc., dated December 18, 2002 ("A.G. Edwards Letter"); Christopher R. Franke, Chairman, Self-Regulation and Supervisory Practices Committee, Securities Industry Association, dated December 18, 2002 ("SIA Letter"); Selwyn J. Noteovitz, Senior Vice President, Global Compliance, Charles Schwab & Co., Inc., dated February 25, 2003 ("Schwab Letter"), collectively ("Commenters"); and Arthur Grant, President, Cadaret, Grant & Co ("Cadaret Letter"), dated December 17, 2002, to Jonathan G. Katz, Secretary, Commission.