

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-55496; File No. SR-NYSE-2006-37)

March 20, 2007

Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Amendment No. 3 to and Order Granting Accelerated Approval of Proposed Rule Change, as Amended, Relating to the Establishment of NYSE Bonds

I. Introduction

On May 16, 2006, the New York Stock Exchange LLC (“NYSE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> to establish a new bond trading platform, NYSE Bonds, to replace its existing bond trading system, the Automated Bond System (“ABS”). The Exchange filed Amendments No. 1 and 2 to the proposed rule change on August 4, 2006 and October 10, 2006, respectively. The proposed rule change, as amended, was published for comment in the Federal Register on October 24, 2006.<sup>3</sup> The Commission received two comments on the proposal.<sup>4</sup> On March 15, 2007, the Exchange filed Amendment No. 3 to the proposal.<sup>5</sup> On March 16, 2007, the NYSE submitted a response to the comment letters.<sup>6</sup> This order provides notice of Amendment No. 3 to

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 54615 (October 17, 2006), 71 FR 62338.

<sup>4</sup> See Letters from Mary C.M. Kuan, Vice President and Assistant General Counsel, Securities Industry and Financial Markets Association (“SIFMA”) to Nancy Morris, Secretary, Commission, dated November 14, 2006 (“SIFMA Letter”) and from Ron L. Klein, Chairman and CEO, General Associates, Inc., dated December 13, 2006 (“Klein Letter”).

<sup>5</sup> For a discussion of Amendment No. 3, see Section V, infra. Amendment No. 3 replaced and superseded Amendment No. 2 in its entirety.

<sup>6</sup> See Letter from Mary Yeager, Assistant Secretary, NYSE, to Nancy M. Morris, Secretary, Commission, dated March 16, 2007 (“NYSE Response Letter”).

the proposed rule change and approves the proposed rule change as amended on an accelerated basis.

## II. Description of the Proposal

NYSE proposes to amend its Rule 86 to replace its existing bond trading system, ABS, with a bond trading platform based on technology used to operate the NYSE Arca Marketplace.<sup>7</sup> The new name of the NYSE bond trading platform would be “NYSE Bonds.” NYSE also proposes to amend other Exchange rules to conform to revised NYSE Rule 86.

Any security traded on NYSE Bonds would have to be listed, or otherwise admitted to dealing, on the Exchange. NYSE has represented that all debt securities currently trading on ABS would be transferred to NYSE Bonds.<sup>8</sup> Additional debt securities that meet the listing standards in NYSE Listed Company Manual Sections 102.03, 103.05, 703.19, or 703.21, or that are deemed “exempted securities” under Section 3(a)(12) of the Exchange Act,<sup>9</sup> could trade on NYSE Bonds. In addition, NYSE intends to trade unregistered corporate bonds pursuant to an exemption from Section 12(a) of the Exchange Act and a related rule change recently approved by the Commission.<sup>10</sup>

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<sup>7</sup> The NYSE Arca Marketplace is the successor to the Archipelago Exchange. See Securities Exchange Act Release No. 53615 (April 7, 2006), 71 FR 19226 (April 13, 2006) (SR-PCX-2006-24).

<sup>8</sup> Such debt securities include, but are not limited to the following: corporate bonds (including convertible bonds), international bank bonds, foreign government bonds, U.S. government bonds, government agency bonds, municipal bonds, and debt-based structured products. Any security that would trade on NYSE Bonds is referred to as a “bond” for the purposes of NYSE rules.

<sup>9</sup> 15 U.S.C. 78c(a)(12).

<sup>10</sup> See Securities Exchange Act Release No. 54766 (November 16, 2006), 71 FR 67657 (November 22, 2006) (File No. S7-06-05) (permitting NYSE member organizations to trade bonds on the Exchange that are not registered under Section 12(b) of the Exchange Act, but are issued by NYSE-listed companies or their wholly owned subsidiaries and that meet other conditions); Securities Exchange Act Release No. 54767 (November 16,

NYSE Bonds would be an electronic order-driven matching system. Initially, the System would allow limit orders and reserve orders. Visible interest would be executed on a price/time priority basis. However, undisplayed reserve interest in NYSE Bonds would always yield to displayed interest at a particular price.<sup>11</sup> Outside of an auction (described below), orders marketable at the time of entry would be matched and executed, except if the price exceeded the “price collar” established for the bond at the time of entry. An order that is priced beyond the price collar threshold would be rejected by the system; an order that is not marketable at the time of entry would post to the NYSE Bonds order “book.”<sup>12</sup> If an order were entered at a better price than the then-best priced contra-side order on the NYSE Bonds book, the system would match the incoming order against the booked order at the booked order’s price, thereby providing price improvement to the incoming order. Bonds generally would be traded in denominations of \$1,000.<sup>13</sup>

NYSE Bonds would have three trading sessions: (1) the Opening Bond Trading Session (4:00 a.m. until 9:30 a.m. Eastern Time (“ET”)); (2) the Core Bond Trading Session (9:30 a.m. until 4:00 p.m. ET); and (3) the Late Bond Trading Session (4:00 p.m. until 8:00 p.m. ET). A User<sup>14</sup> entering an order into NYSE Bonds would be required to designate the time in force of the order. A day order, if not executed, would expire at the end of any of the three daily trading sessions for which it was designated. A good-‘til-cancelled order would remain in effect until it

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2006), 71 FR 67680 (November 22, 2006) (SR-NYSE-2004-69) (collectively, the “Unlisted Corporate Bonds Orders”).

<sup>11</sup> See proposed NYSE Rule 86(j)(3)(B).

<sup>12</sup> See proposed NYSE Rule 86(e).

<sup>13</sup> A User submitting an order priced in a denomination less than \$1,000 would be required to specify the original principal amount of the bond. See proposed Rule 86(d).

<sup>14</sup> See proposed NYSE Rule 86(b)(2)(M) (defining “User” as any Subscriber, Sponsored Participant, or Authorized Trader that is authorized to obtain access to NYSE Bonds).

was either cancelled or executed, but would be available for execution only during the Core Bond Trading Session. Unless the User indicated otherwise, the system's default assumption would be that all orders are day orders.

At the commencement of both the Opening Bond Trading Session and the Core Bond Trading Session, the Exchange would conduct a bond auction. Users would be able to submit orders for execution Opening Bond Auction and the Core Bond Auction beginning at 3:30 a.m. ET. Orders designated for the Opening Bond Trading Session would queue until 4:00 a.m. ET, at which time the Opening Bond Auction would take place and orders designated for the Core Bond Trading Session would queue until 9:30 a.m. ET, at which time the Core Bond Auction would take place.<sup>15</sup> During a bond auction, the system would attempt to match and execute orders at the Indicative Match Price ("IMP"). The IMP is defined as: (1) the price at which the maximum volume of bonds are executable; (2) if there are two or more prices at which the maximum volume of bonds are executable, the price that is closest to the closing price in that bond on the previous trading day, or if the bond did not trade on the previous day, the price that is closest to the closing price on the last day that the bond traded; (3) if bond orders to buy and bond orders to sell are not marketable, the highest priced bid; or (4) if there were no bids but only offers, the lowest offer price.<sup>16</sup> Beginning at 3:30 a.m. ET and various times thereafter, the IMP of the Opening Bond Auction and/or the Core Bond Auction and any Imbalance<sup>17</sup> associated therewith would be disseminated by the Exchange.

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<sup>15</sup> See proposed NYSE Rule 86(i).

<sup>16</sup> See proposed NYSE Rule (b)(2)(G).

<sup>17</sup> See proposed NYSE Rule 86(b)(2)(F) (defining "Imbalance" as the number of buy or sell orders that cannot be matched with other orders at the IMP at any given time).

A single order to sell coupled with a single order to buy would be sufficient to establish a bond auction, provided the orders were marketable.<sup>18</sup> If no marketable orders were entered into the system prior to the commencement of a bond auction, the auction would not occur, and the existing orders would be available only for ordinary trading in the designated bond trading session(s). Orders that were designated for a particular bond trading session and eligible to participate in the related bond auction, but not executed in such bond auction, would also be available for ordinary trading in the trading session. Orders designated for but not executed in the Opening Bond Trading Session would be eligible to be matched and executed in the Core Bond Auction at the IMP. Orders eligible for the Opening Bond Auction or the Core Bond Auction could be cancelled at any point until two minutes prior to the commencement of the respective bond auction.

To post an order on NYSE Bonds, a User would be required to enter the following information: CUSIP number; quantity; order type (i.e., limit or reserve); price (up to three decimals); account type indicator (“P” for principle or “A” for agent); time in force; and whether the order is buy, sell, or sell/short.<sup>19</sup> An order could not be modified but could be cancelled at any time before it is executed, except that a User could not cancel an order eligible for execution in a regularly scheduled bond auction inside of two minutes prior to the beginning of the bond auction.

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<sup>18</sup> See proposed NYSE Rule 86(l) (prescribing procedures NYSE Bonds Bond Auctions).

<sup>19</sup> The staff of the Division of Market Regulation of the Commission previously has stated that it would not recommend that the Commission take enforcement action if short sales in exchange-listed bonds and debentures are effected without complying with Rule 10a-1 under the Exchange Act, 17 CFR 240.10a-1. See Securities Exchange Act Release No. 30772 (June 3, 1992), 57 FR 24415 (June 9, 1992) (File No. S7-13-92) (“Bond Short Sale No-Action Position”). The Exchange deems this determination by the Commission Staff to apply to Exchange Rule 440B (Short Sales).

The proposal contemplates the halting, suspension, and closing of bond trading on NYSE Bonds (a “Bond Halt”) in certain circumstances.<sup>20</sup> During a Bond Halt, orders could enter the system and queue according to price/time priority but would not execute. When the Bond Halt is concluded, trading would resume with a Bond Halt Auction, at which time orders would match and execute at the IMP under similar terms to the other bond auctions. Like the other bond auctions, no executions would occur unless marketable orders were available prior to the commencement of the Bond Halt Auction. Orders eligible for execution in the Bond Halt Auction could be cancelled at any point prior to the beginning of the Bond Halt Auction. At the conclusion of the Bond Halt Auction, ordinary trading would resume in the trading session in progress at the conclusion of the halt.

A member organization wishing to trade on NYSE Bonds (“Subscriber”) would be required to enter into a written agreement with the Exchange.<sup>21</sup> A non-member (“Sponsored Participant”)<sup>22</sup> could gain access to NYSE Bonds only by entering into a written agreement with a Subscriber (*i.e.*, a “Sponsoring Member Organization”)<sup>23</sup> and the Exchange. In the sponsorship agreement, the Sponsoring Member Organization would acknowledge, among other things, that any order entered by the Sponsored Participant and any execution resulting from such order would be binding in all respects on the Sponsoring Member Organization.<sup>24</sup> The Sponsoring Member Organization would be responsible for any and all actions taken by its Sponsored Participant. The Sponsored Participant, in turn, would agree, among other things, to comply

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<sup>20</sup> See proposed NYSE Rule 86(k).

<sup>21</sup> See proposed NYSE Rule 86(o)(a).

<sup>22</sup> See proposed NYSE Rule 86(b)(2)(K).

<sup>23</sup> See proposed NYSE Rule 86(b)(2)(J).

<sup>24</sup> See proposed NYSE Rule 86(o)(b)(2)(B)(i).

with the rules of the Exchange and the rules and procedures with regard to NYSE Bonds, as if it were a member of the Exchange.<sup>25</sup> The Sponsored Participant also would be required to: (1) take reasonable security precautions to prevent unauthorized access to NYSE Bonds; (2) establish and maintain an up-to-date list of persons permitted to access NYSE Bonds on behalf of the Sponsored Participant (i.e., “Authorized Traders”<sup>26</sup>); and (3) provide that list to the Sponsoring Member Organization. Moreover, the Sponsoring Member Organization would be required to undertake certain responsibilities related to a Sponsored Participant’s Authorized Traders, including: (1) maintaining a list of Authorized Traders; (2) establishing procedures to ensure that Authorized Traders comply with Exchange rules and to ensure the safety of and access to the equipment used to access NYSE Bonds; and (3) suspending an individual’s status as an Authorized Trader when such individual’s action has caused the Sponsoring Member Organization to fail to comply with Exchange rules.<sup>27</sup>

The proposed NYSE Bonds rules also include provisions for the handling of a “Clearly Erroneous Execution,” defined as an execution involving an obvious error in any term of an order participating in such execution, such as price, unit of trading, or identification of the bond.<sup>28</sup> Subject to the approval of the Exchange, a Clearly Erroneous Execution could be nullified if no party to the trade objects.<sup>29</sup> The Exchange also has proposed to establish procedures for reviewing a transaction if one of the parties does not agree to the cancellation. A User could request a review via telephone, facsimile, or e-mail. Upon receipt of such request,

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<sup>25</sup> See proposed NYSE Rule 86(o)(b)(2)(C).

<sup>26</sup> See proposed NYSE Rule 86(b)(2)(L).

<sup>27</sup> See proposed NYSE Rule 86(o)(b)(4).

<sup>28</sup> See proposed NYSE Rule 86(b)(2)(H).

<sup>29</sup> See proposed NYSE Rule 86(m)(1).

the Exchange would notify the counterparty as soon as practicable. Any request for review would generally be required to be submitted within 30 minutes of the trade; however, the Exchange could consider a request after 30 minutes on a case-by-case basis in a manner that promotes a fair and orderly market and does not unfairly discriminate against Users of NYSE Bonds. Each party to the transaction would be required to provide, within 30 minutes of the request for review, any supporting written information as may be reasonably requested by the Exchange to aid in the resolution of the matter.

Unless both parties to the disputed transaction agreed to withdraw the initial request for review, an Officer of the Exchange or a designee (the “Reviewer”) would review the transaction and determine whether it were clearly erroneous, with a view towards maintaining a fair and orderly market and the protection of investors and the public interest. In Amendment No. 3, the Exchange proposed factors that the Reviewer could consider in the determination of a Clearly Erroneous Execution.<sup>30</sup> If the Reviewer determines that the transaction in dispute is erroneous, the transaction would be declared null and void, or one or more of the terms of the transaction would be modified. The parties would be promptly notified of the determination.

A request for review of the initial determination by the Clearly Erroneous Execution Panel (“CEE Panel”)<sup>31</sup> may be made within 30 minutes after the party making the appeal is given

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<sup>30</sup> Such factors include execution price(s); volume and volatility of a bond; news released for the issuer or the bond and/or the related security; the existence of trading halts; corporate action(s); general market conditions; rating of the bond; interest and or coupon rate; maturity date; yield curves; last sale, if available within a reasonable time frame; executions inconsistent with the trading pattern of a bond; current day’s trading high/low; recent day’s and week’s trading high/low; executions outside the 52 week high/low; effect of a single large order creating several prints at various prices; and quotes and executions of other market centers. See proposed NYSE Rule 86(m)(2)(E).

<sup>31</sup> The CEE Panel would be comprised of the Chief Executive Officer of NYSE Regulation or a designee, and representatives from two Subscribers to NYSE Bonds. The Exchange



notice of the determination. However, the CEE Panel would not review a determination of the Reviewer if the Reviewer determined that the number of affected transactions was such that immediate finality would be necessary to maintain a fair and orderly market and to protect investors and the public interest. All determinations by the CEE Panel would constitute final action by the Exchange.

In addition, the proposal would allow the Exchange to review transactions affected by a system disruption, system malfunction, or equipment changeover to decide if any such transactions were erroneous.<sup>32</sup> In the event of any system disruption, system malfunction, or equipment changeover in the use or operation of any electronic communications and trading facilities of the Exchange, an Officer of the Exchange or a designee, on his or her own initiative, could review a transaction arising out of the use or operation of such facilities during such period and declare it unchanged, nullify it, or modify the terms of the trade. Absent extraordinary circumstances, any such action of the Exchange would need to be taken within 30 minutes of detection of the system disruption, system malfunction, equipment changeover, or an erroneous transaction resulting from such system problem. If an erroneous transaction occurred as a result of a system problem and the Exchange determines to revise the trade, the counterparties to the erroneous transaction would be notified of the action as soon as practicable. A User aggrieved by such action could appeal such action to the CEE Panel in accordance with the provisions described above.

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would designate at least ten Subscribers to NYSE Bonds to act as representatives to be called upon to serve on the CEE Panel, as needed. In no case would a CEE Panel include a person related to a party to the trade in question. To the extent reasonably possible, the Exchange would call upon the designated representatives to participate on a CEE Panel on an equally frequent basis. See proposed NYSE Rule 86(m)(4)(A) and (B).

<sup>32</sup> See proposed NYSE Rule 86(m)(5).

Most orders matched on NYSE Bonds would be locked-in trades and would be submitted to a registered clearing agency with accrued interest calculated according to the defined eligibility characteristics of the particular bond.<sup>33</sup> Settlement of corporate bond trades would be “regular way,” *i.e.*, three-day settlement. At a later date, the Exchange intends to publish a real-time bond data feed, and intends to make such data available for purchase by non-subscribing market participants, third-party data vendors, and other interested parties who agree to the Exchange’s terms. In addition to disseminating the NYSE Bonds order book, the data feed would also include the last sale price and size as executions occur. The Exchange also proposed several technical changes to other NYSE rules to remove certain obsolete references and otherwise conform the terms of certain other rules to revised NYSE Rule 86.

### III. Summary of Comments and NYSE’s Response

As noted above, the Commission received two comment letters on the proposal. The Klein Letter expressed support for the NYSE's proposal. The other commenter, SIFMA, expressed some support for NYSE’s proposal but also raised certain concerns. The Exchange responded to the concerns raised in the SIFMA Letter.

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<sup>33</sup> The Exchange submits completed trades to one of the subsidiaries of the Depository Trust Clearing Corporation (“DTCC”) for clearance and settlement. The National Securities Clearing Corporation (“NSCC”), a subsidiary of DTCC, provides clearance and settlement services for government agency, corporate, and municipal bonds that trade on ABS. While the Government Securities Division of the Fixed Income Clearing Corporation (“FICC”), another subsidiary of DTCC, provides clearance and settlement services for transactions in U.S. government bonds, the Exchange does not currently have an agreement with FICC for such settlement and clearance. Presently, U.S. government bonds that trade on ABS are traded *ex-clearing* (*i.e.*, the parties to the transaction arrange for manual clearing and settlement). The Exchange plans to submit trades on a locked-in basis to FICC for clearance and settlement in 2007. Until such time as the Exchange has established such an agreement with the FICC, the U.S. government bonds that trade on NYSE Bonds would continue to trade *ex-clearing* as they do today on ABS. Trades that would not be locked-in would be those in bonds that are not set up for the Exchange’s registered clearing agency, or bonds having a face value other than \$1,000.

SIFMA questioned whether the Exchange's plans to assess a fee for the market data generated by NYSE Bonds would confer an unfair competitive advantage as the exclusive processor of quote and trade data of NYSE Bonds, which it believed may lead to unreasonable prices for such data.<sup>34</sup> In addition, SIFMA raised concern regarding the Exchange's intention to limit the use and redistribution of its market data.<sup>35</sup> NYSE responded that SIFMA's concerns were premature in that the Exchange has not yet filed a proposal with the Commission under Rule 19b-4 under the Exchange Act to modify the fees that it charges for NYSE Bonds data.<sup>36</sup>

SIFMA also expressed concerns relating to the jurisdiction of NASD for transactions on NYSE Bonds.<sup>37</sup> Specifically, SIFMA requested clarity on whether Users of NYSE Bonds would have any trade reporting obligations to NASD for bonds that trade on NYSE pursuant to Exchange Rules 1400 and 1401. SIFMA also raised a more general concern that NASD may assert jurisdiction over trading activities effected on a national securities exchange, including NYSE Bonds. NYSE argued that the concerns were without merit because NASD recently established a two-year pilot program<sup>38</sup> that exempted unlisted bonds trading on the NYSE subject to the Exchange's trade reporting requirements from TRACE reporting requirements.<sup>39</sup> Moreover, NYSE clarified that NYSE Regulation will undertake primary responsibility for regulating NYSE Bonds and that NASD will retain responsibility for regulating the over-the-counter corporate bond market.

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<sup>34</sup> See SIFMA Letter at 2-3.

<sup>35</sup> Id.

<sup>36</sup> See NYSE Response Letter at 2.

<sup>37</sup> See SIFMA Letter at 3-4.

<sup>38</sup> See Securities Exchange Act Release No. 54678 (November 16, 2006), 71 FR 67673 (November 22, 2006) (SR-NASD-2006-110).

<sup>39</sup> See NYSE Response Letter at 3.

Finally, SIFMA expressed concern about the lack of definitive quantitative standards in the proposed trade nullification rule for NYSE Bonds.<sup>40</sup> The Exchange included in Amendment No. 3 relevant factors that may be considered when the Exchange determines whether an execution is clearly erroneous.<sup>41</sup>

#### IV. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the Exchange Act and the rules and regulations promulgated thereunder applicable to a national securities exchange.<sup>42</sup> Specifically, the Commission finds that approval of the proposal is consistent with Section 6(b)(5) of the Exchange Act<sup>43</sup> in that it is designed to facilitate transactions in securities; 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.

NYSE Bonds will replace ABS as the facility for trading bonds on the Exchange. The Commission believes that an exchange's determination to implement new trading technology is generally consistent with the Exchange Act. As described above, the proposal includes provisions regarding order entry, priority, trading sessions and auctions, manner of execution, clearing, trade halt procedures, and trade nullification. The Commission finds that these

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<sup>40</sup> See SIFMA Letter at 4.

<sup>41</sup> See proposed NYSE Rule 86(m)(2)(E).

<sup>42</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>43</sup> 15 U.S.C. 78f(b)(5).

provisions are reasonably designed to promote the efficient functioning of NYSE Bonds and are generally consistent with the Exchange Act.<sup>44</sup> Other aspects of the proposal are described in more detail below.

#### Sponsored Access to NYSE Bonds

Only members that enter into a service agreement with the Exchange may access NYSE Bonds. In addition, the Exchange would permit a non-member that enters into an agreement with a subscribing member and the Exchange to access NYSE Bonds as a “Sponsored Participant.” These sponsored access provisions are substantially similar to those that have been adopted by other national securities exchanges and previously approved by the Commission.<sup>45</sup>

#### Price Collars

The Exchange would reject an incoming order that is otherwise marketable if the price of the order violated the price collar for that bond. The Commission believes that the proposed price collars are reasonably designed to protect investors and promote the public interest by preventing executions that are substantially away from the prevailing market price. These provisions are similar to others employed by NYSE Arca and Nasdaq, which previously have been approved by the Commission.<sup>46</sup>

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<sup>44</sup> However, the Commission notes that the Exchange did not in this filing propose any fee changes in connection with the NYSE Bonds system. Therefore, the Commission in this order is not making any findings regarding any fee that the Exchange charges or may in the future propose to charge in connection with the use of the NYSE Bonds system.

<sup>45</sup> See NYSE Arca Equities, Inc. (“NYSE Arca Equities”) Rule 7.29(b); Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (SR-PCX-00-25) (establishing sponsored participant provision for equity trading on the NYSE Arca Marketplace).

<sup>46</sup> See, e.g., NYSE Arca Equities Rule 1.1(r)(A) (NYSE Arca Market Order Auction and Closing Auction), Securities Exchange Act Release No. 52361 (August 30, 2005), 70 FR 53704 (September 9, 2005) (SR-PCX-2005-58); Nasdaq Rule 4752(d)(2)(E) (Nasdaq Opening Process), Securities Exchange Act Release No. 50405 (September 16, 2004), 69 FR 57118 (September 23, 2004) (SR-NASD-2004-071); and Nasdaq Rule 4754(b)(2)(E)

Applicability of Section 11(a) and (b) of the Exchange Act

Section 11(a) of the Exchange Act<sup>47</sup> prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises investment discretion, unless an exception applies. The Commission notes that this general prohibition would not generally impact trading on NYSE Bonds because Rule 11a1-4(T) under the Exchange Act<sup>48</sup> deems transactions in bonds on a national securities exchange for a member's own account to be consistent with Section 11(a). However, for those securities trading on NYSE Bonds for which this exemption may not be available, such as certain structured products, the Exchange has represented that transactions effected on NYSE Bonds meet the requirements of Rule 11a2-2(T) under the Exchange Act.<sup>49</sup> Similarly, the Commission notes that Section 11(b) of the Exchange Act<sup>50</sup> and Rule 11b-1 thereunder,<sup>51</sup> which pertain to specialists and market-makers, would not be implicated because there would be no specialists or market makers on NYSE Bonds.

Applicability of Rule 10a-1 under the Exchange Act

In its filing, NYSE states that: "The staff of the Division of Market Regulation of the Securities and Exchange Commission has stated that it would not recommend that the Commission take enforcement action if short sales in exchange-listed bonds and debentures are

(Nasdaq Closing Cross), Securities Exchange Act Release No. 49406 (March 11, 2004), 69 FR 12879 (March 18, 2004) (SR-NASD-2003-173).

<sup>47</sup> 15 U.S.C. 78k(a).

<sup>48</sup> 17 CFR 240.11a1-4(T).

<sup>49</sup> The Commission notes that, to the extent that any security trading on NYSE Bonds is an NMS security, see 17 CFR 242.600(b)(46), the Commission is not making any finding herein as to whether NYSE Bonds is compliant with the requirements of Regulation NMS under the Exchange Act.

<sup>50</sup> 15 U.S.C. 78k(b).

<sup>51</sup> 17 CFR 240.11b-1.

effected without complying with SEC Rule 10a-1.”<sup>52</sup> By this filing, the Exchange seeks continued effect of this position. The staff maintains this position. However, the Commission notes that the staff’s position does not apply to convertible bonds.<sup>53</sup> Accordingly, convertible bonds would continue to be excluded from applicability of this position.

#### V. Accelerated Approval

Pursuant to Section 19(b)(2) of the Exchange Act,<sup>54</sup> the Commission may not approve any proposed rule change prior to the 30<sup>th</sup> day after the date of publication of notice of the filing thereof, unless the Commission finds good cause for so doing and publishes its reasons for so finding. In Amendment No. 3, the Exchange, among other things:

- revised proposed NYSE Rule 86(b) to indicate that, if other NYSE rules relating to bonds conflict with the provisions of proposed NYSE Rule 86, Rule 86 would control;
- eliminated references to the “Floor” of the Exchange to make clear that NYSE Bonds is a fully electronic trading platform;
- noted that dealers trading municipal bonds must report such transactions to the Municipal Securities Rulemaking Board (“MSRB”) in accordance with MSRB Rule G-14;

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<sup>52</sup> See Bond Short Sale No-Action Position, supra note 19 (footnote omitted) (stating that, “From and after the date of this release until the Commission takes final action on the proposed amendment to Rule 10a-1(b), the staff of the Division will not recommend that the Commission take enforcement action under Rule 10a-1 if short sales in exchange-listed bonds and debentures are effected without complying with the Rule”).

<sup>53</sup> See id. (noting that convertible bonds are defined as “equity securities” in the Exchange Act and that “Exchange Act Section 3(a)(11), 15 U.S.C. 78c(a)(11), defines the term ‘equity security’ to include ‘any stock or similar security, or any security convertible, with or without consideration, into such a security....’ Short selling of convertible bonds...may have an impact on the price of related exchange-traded equity securities”).

<sup>54</sup> 15 U.S.C. 78s(b)(2).

- revised proposed NYSE Rule 86(b)(2)(E) to indicate that, unless otherwise designated, an order will be treated as a day order;
- revised proposed NYSE Rule 86(b)(2)(G) to indicate that, if no bids are submitted to a Bond Auction, the Indicative Match Price will be the lowest offer price;
- revised proposed NYSE Rule 86(e) to clarify that the price collars will only apply during ordinary trading and not during the queuing of bond orders or during bond auctions;
- revised proposed NYSE Rule 86(h) to clarify that orders designated only for the Opening Bond Trading Session that do not execute in the Opening Bond Auction or Opening Bond Trading Session will be eligible to participate in the Core Bond Auction and would be cancelled if not executed in the Core Bond Auction;
- modified proposed NYSE Rule 86(i) to clarify that orders may be entered into NYSE Bonds until 8:00 p.m. ET and to otherwise clarify the operation of the three proposed bond trading sessions;
- revised proposed NYSE Rule 86(l) to indicate that, beginning at 3:30 am ET, the IMP for the Opening Bond Auction and the Core Bond Auction, and any associated Imbalance, will be published by the Exchange. In addition, the changes to proposed NYSE Rule 86(l) further explain the functionalities of the Bond Auctions;
- clarified in proposed NYSE Rule 86(m) the possible outcomes after review of potentially erroneous transactions by the Reviewer and by the Clearly Erroneous Execution Panel. In addition, the Exchange added factors that may be considered in the determination of a Clearly Erroneous Execution;



- revised proposed NYSE Rule 86(n)(2)(G) to indicate that orders that are eligible for execution in the Bond Halt Auction may be cancelled at any time;
- revised portions of proposed NYSE Rule 86(o) related to a sponsored access to NYSE Bonds to conform substantially to related provisions of other national securities exchanges, including NYSE Arca;<sup>55</sup>
- represented that transactions effected on NYSE Bonds meet the requirements of Rule 11a2-2(T) under the Exchange Act and included an accompanying discussion;
- represented that NYSE Regulation can effectively regulate NYSE Bonds; and
- made other minor clarifying and technical changes to the proposal.

The Commission believes that these changes do not raise any significant or novel regulatory issues. Accordingly, the Commission hereby finds good cause for approving the proposed rule change, as modified by Amendment No. 3, prior to the 30<sup>th</sup> day after publishing notice of the amended proposal in the Federal Register.

#### VI. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 3, including whether Amendment No. 3 is consistent with the Exchange 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](mailto:rule-comments@sec.gov). Please include File Number SR-NYSE-2006-37 on the subject line.

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<sup>55</sup> See NYSE Arca Equities Rule 7.29.

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-2006-37. 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. Copies of the 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-2006-37 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

VII. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Exchange Act,<sup>56</sup> that the proposed rule change (SR-NYSE-2006-37), as amended, be, and it hereby is, approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>57</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>56</sup> 15 U.S.C. 78s(b)(2).

<sup>57</sup> 17 CFR 200.30-3(a)(12).