

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55615; File No. SR-NYSE-2007-34)

April 11, 2007

Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Proposed Rule Change to Amend NYSE Rule 80A.40(b) to Update the Definition of “Program Trading,” to Substitute Simplified Audit Trail Requirements, and to Make Conforming Amendments to NYSE Rule 410B

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on March 22, 2007, the New York Stock Exchange LLC (“NYSE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared substantially by NYSE. 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

NYSE proposes to amend NYSE Rule 80A.40(b) to update the definition of “program trading” by eliminating the pre-determined minimum dollar value requirement for trading strategies that involve the related purchase or sale of a “basket” or group of 15 or more stocks, to substitute simplified audit trail requirements, and to make conforming amendments to Rule 410B. The text of the proposed rule change is available at NYSE, www.nyse.com, and the Commission’s Public Reference Room.

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

In its filing with the Commission, NYSE included statements concerning the purpose of

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

and basis for the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NYSE 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

In order to improve the reporting and monitoring of program trading by the Exchange, NYSE proposes to clarify what constitutes program trading and to streamline the process for entering and identifying program trades. To accomplish this, the Exchange is proposes (i) to amend NYSE Rule 80A.40 to eliminate the minimum dollar value from the definition of program trading, and (ii) to substitute simplified audit trail requirements in place of the more cumbersome reporting requirements that currently apply to program trading. The proposed amendments also include certain conforming amendments to NYSE Rule 410B. In connection with these changes, the Exchange also intends to issue guidance regarding the definition of a “coordinated strategy,” as that term is used in Rule 80A.40.

Background

The Exchange adopted Rule 80A in the wake of the 1987 market break to address various coordinated professional trading strategies, in particular, program trading that was using the cash market to take advantage of trading in the derivatives market. To ensure that the rule would encompass the various permutations that such trading strategies might take, the Exchange defined program trading as either index arbitrage or “any trading strategy involving the related purchase or sale of a ‘basket’ or group of 15 or more stocks having a total market value of \$1 million or more.” The monetary value was believed at the time to capture program trading strategies that would be significant in the context of the market. Despite a significant increase in

the size and value of trading in the market since 1987, however, this monetary component of the definition has not been updated since it was adopted.

Proposed Redefinition of Program Trading

Given the technical and automated nature of the trading environment that exists today, the Exchange believes that the current definition of “program trading” is no longer workable, since, among other things, it captures certain computer-driven or algorithmic trading strategies that are not intended to be program trades. At the same time, certain strategies that could fairly be classified as programs—that is, strategies involving 15 or more stocks that are intended to be coordinated, but which do not meet the monetary threshold—are not being captured.

In contrast to 1987, most firms today employ algorithmic trading to manage and carry out both plain-vanilla execution strategies that are not intended to be programs, including public-customer driven parameter-based trading (that is, trading in which the customer specifies certain desired execution conditions such as timing, pricing, quantity, or marketplace selection, and the algorithm evaluates market information and generates orders that best match the specified conditions without further human intervention), and more complex trading strategies that are intended to be programs. The Exchange therefore recognizes that not all computer-driven trading strategies constitute Program Trading. For example, if they otherwise lack the other definitional characteristics of program trading, algorithmic trading, volume-weighted average price (“VWAP”) trading, statistical arbitrage, and similar computer-driven trading strategies may not need to be classified or reported as a program simply because the strategy is executed through a computer model or “black box.”

This has led to regulatory confusion; indeed, member firms have informed the Exchange that in order to ensure full compliance with the rule, they feel compelled to report computer-

driven trading strategies that meet the technical definition of a program even though they are not, in fact, intended as program trading.

To address the issue of the overbroad definition of program trading and to improve the precision of program trade reporting, the Exchange proposes to amend the definition of program trading under NYSE Rule 80A.40 to eliminate the requirement that program trades must have a combined value of \$1 million or more. The Exchange believes that the minimum dollar value currently contained in Rule 80A.40 establishes an arbitrary and artificial bar for determining whether a coordinated strategy constitutes program trading. In the absence of the dollar threshold, the Exchange proposes assessing whether a trading program constitutes a coordinated strategy examining its attributes rather than relying on such an arbitrary limitation.

To assist firms in determining whether a particular set of trades constitutes a “program,” the Exchange intends to issue guidance to member organizations regarding factors to consider in determining whether a trading strategy is “coordinated.” This guidance will focus on how the primary investment objective of the trading, as well as the linkage or dependency between and among simultaneous (or substantially simultaneous) trades in different securities, relate to the investment objective. As described more fully below, under the revised rule, the Exchange would consider any execution of 15 or more stocks that is entered as part of a single investment strategy (including liquidation, rebalancing, or realignment of a basket/portfolio) with the intention to execute all or most of the stocks to be a “coordinated strategy.”

“Coordinated strategies” would include any purchase or sale of 15 or more stocks that is (i) coordinated pursuant to a broader investment strategy such as economic, financial, or fundamental characteristics (such as a particular industry, sector, or industry) or market activity, and (ii) where the execution of the securities within the portfolio is linked, as opposed to being

merely coincidental single stock definitions. A coordinated strategy would include a portfolio or basket strategy of 15 or more stocks wherein each stock execution is dependent upon the execution of all or most of the securities within the portfolio or basket. And, as before, program trading would also include all index arbitrage trading. Accordingly, any strategy that attempts to capture identified mispricings between an S&P 500 component security and its related future as the filters for buying or selling such stock, regardless of the number of stocks involved, is a program.

As noted above, not all computer-driven trading strategies would be defined as program trading. For example, portfolio VWAP transactions that attempt to provide a customer with an average price for the purchase or sale of stocks would not necessarily be a program. For VWAP trading to constitute a program, the trading would have to involve a portfolio or basket of 15 or more stocks as part of a coordinated strategy.

In addition, pairs trading, in which stocks are put into pairs by fundamental or market-based similarities and traded versus each other, would not necessarily be program trading. For pairs trading to fall within the program trading definition, the engine or algorithm used for execution of the selected pairs would have to consist of a group of related stocks that would be defined as a program, e.g., an automotive “pairs” algorithm that typically trades more than 15 different automotive stocks.

Streamlining Reporting of Program Trades

The Exchange is also proposing to streamline the reporting process that member organizations must follow when reporting program trading. Since 1988, the Exchange has required that member firms report program trading activities by the close of business on the second business day following the trade date on a Daily Program Trading Report (“DPTR”).

Member firms currently file their DPTRs via an electronic filing platform operated by the Exchange.

Because the DPTR is created after the trades have been executed, rather than in connection with the entry of orders at issue, the DPTR is potentially less accurate than determining program trading information based on audit trail information, which captures trading information at the time of execution. Moreover, because all information reported on the DPTR is already available to the Exchange via audit trail information, the DPTR has become redundant. Accordingly, to streamline the reporting process, the Exchange is proposing to eliminate the DPTR requirement, and to rely instead on audit trail information to determine whether firms are engaging in program trading. To assist in identifying program trading, the Exchange is redefining two of the eight existing program trading related audit trail account types so that member firms can mark the specific program trading strategy at the time of order entry and execution, rather than waiting to report via the DPTR.

The Exchange does not believe that the proposed changes to Rules 80A and 410B would in any way compromise its existing surveillances, or impair the ability to conduct additional surveillances, as necessary. To the contrary, the Exchange believes that the proposed changes to the definition of program trading and the revised audit trail information will lead to more focused surveillances for assessing whether member organizations engage in program trading.

2. Statutory Basis

The basis under the Act for this proposed rule change is the requirement under Section 6(b)(5)³ that an Exchange have rules that are designed to promote just and equitable principles of

³ 15 U.S.C. 78f(b)(5).

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.

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 has neither solicited nor received written comments on the 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 self-regulatory organization 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 No. SR-NYSE-2007-34 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSE-2007-34. 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 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-2007-34 and should be submitted on or before [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁴

Florence E. Harmon
Deputy Secretary

⁴ 17 CFR 200.30-3(a)(12).