

# Independent Broker Action Committee

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August 10, 2006

## **VIA EMAIL AND FEDERAL EXPRESS**

Nancy M. Morris, Esq.  
Secretary  
United States Securities and Exchange Commission  
Station Place  
100 F Street, NE  
Washington, DC 20549-9303

Re: File No. NYSE 2006-36; The Discretionary Order Type

Dear Ms. Morris:

As an organization representing over 100 independent New York Stock Exchange (“NYSE”) brokers, the Independent Broker Action Committee, Inc. (“IBAC”) has written previous comment letters to express our concern that the present market balance be scrupulously maintained in the Hybrid Market context. We write now to support the proposed Discretionary Order Type as an important tool in creating that balance in the Hybrid Market and to offer two suggestions to assure that it is effective in so doing.

The present market balance is created and maintained by an independent auction market with the specialist acting as agent to protect the public at point of sale. The full auto-execution market disrupts this relationship by compelling the specialist to trade for his account as principal rather than representing public flow (through DOT, for example). The problem is exacerbated by permitting the specialist to trade algorithmically with incoming order flow on a systematic basis. Given the specialist's ability to view the entire book and the speed of algorithmic trading, this would have created a time and place advantage for the specialists in the Hybrid Market; favoring the specialist as principal over the public as represented by the trading crowd.

The Discretionary Order Type (“d-Quote”) goes a long way towards recreating market balance in the hybrid environment because the d-Quote interacts with orders in the pipeline before orders are visible to the specialists’ algorithms. Consequently, the floor broker in the crowd can use his feel and sense of the market to create price improvement and can react to the environment around him by placing a d-Quote without being picked off by an algorithmic trade.

However, under the present d-Quote formulation there remains a situation where the specialist (now as principal) is given greater advantage than previously permitted. In the pre-Hybrid Market, a broker in the crowd can object to the specialist trading on parity to open or increase a position, and thereby block the trade. Rule 108. Inconsistently, the d-Quote as

submitted, although a displayed interest, trades on parity with specialists' algorithmic orders, even if the specialist is thereby opening or increasing a position. There is no provision in the proposed d-Quote rule to allow the broker to object to a specialist's algorithm trading on parity to open or increase a position. To as closely replicate the present auction market as possible, the d-Quote should include a feature enabling the broker to block a specialist from parity with the d-Quote in opening or increasing a position.

Proposed Amendment No. 1 further weakens the d-Quote by stripping it of its discretionary instructions in a sweep initiated by other orders. NYSE 2006-36, Amend. No. 1, Rule 70.25(d)(ix).

Undoubtedly, the d-Quote is a, if not the, central component in maintaining market balance in the hybrid environment. As such, we urge the Commission to require that d-Quotes and specialist algorithms be phased in together.

Amendment No. 1 to NYSE 2006-36 establishes the contrary procedure by providing that the d-Quote be part of Phase III of Implementation; while the specialist algorithms and APIs are contemplated for Phase II. (See File No. 2004-05 Amendment No. 8, p.14). Exacerbating the problem of delay in the implementation of the d-Quote is the inadequacy of technology presently being tested. Our members report ongoing difficulties with time and reliability of the d-Quote mechanisms now being tested.

To implement the specialist algorithms first in the absence of d-Quotes will risk a mass exodus of volume from the NYSE, as price improvement becomes virtually impossible without the d-Quote. To try to recapture volume once lost would be extraordinarily difficult. Therefore, to preserve price improvement – and volume – algorithms should not be implemented unless in tandem with d-Quotes.

Respectfully submitted,

INDEPENDENT BROKER ACTION COMMITTEE, INC.

By: \_\_\_\_\_  
Warren P. Meyers, President

cc: Mr. Robert L.D. Colby, Acting Director  
Ms. Heather Seidel, Senior Special Counsel  
Division of Market Regulation  
United States Securities and Exchange Commission