

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-54466; File No. SR-NYSEArca-2006-48)

September 18, 2006

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Proposed Rule Change to Amend NYSE Arca Equities, Inc.'s Clearly Erroneous Executions Rule to Include an Appeal Fee for the Archipelago Exchange

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 11, 2006, NYSE Arca, Inc. ("NYSE Arca" 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 by NYSE Arca. 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 Arca proposes to amend NYSE Arca Equities Rule 7.10 governing clearly erroneous executions ("CEE") on the Archipelago Exchange, the equities trading facility of NYSE Arca Equities, Inc. ("NYSE Arca Equities"). Specifically, the Exchange proposes to assess a fee associated with the appellate mechanism of NYSE Arca Equities Rule 7.10.

The text of the proposed rule change is available on NYSE Arca's Web site (<http://www.nysearca.com>), at NYSE Arca's principal office, and at 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 Arca included statements concerning the

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

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

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. NYSE Arca 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

The Exchange amended NYSE Arca Equities Rule 7.10 (Clearly Erroneous Executions) to include subsections (c)(2)-(4), which amendment became effective May 16, 2005. NYSE Arca Equities Rules 7.10(c)(2)-(4) provide for an appeals panel that includes the Exchange's Chief Regulatory Officer ("CRO"), or a designee of the CRO, and two representatives from Equity Trading Permit ("ETP") Holders (together with the CRO, the "CEE Panel") to review the determination of clearly erroneous executions that are made by an NYSE Arca Equities officer under NYSE Arca Equities Rule 7.10(c)(1).

As part of its continuing efforts to enhance the appeal process, the Exchange proposes to add NYSE Arca Equities Rule 7.10(c)(5).<sup>3</sup> Under the proposed rule, if the CEE Panel votes to uphold the decision made pursuant to NYSE Arca Equities Rule 7.10(c)(1), the Exchange would assess a \$500.00 fee against the ETP Holder(s) who initiated the request for appeal. The Exchange's experience with the appeal process strongly indicates that some ETP Holders are improperly taking advantage of the appeal opportunity provided under the rule. The Exchange believes that assessing a \$500.00 fee against the ETP Holder(s) who appeals a decision made

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<sup>3</sup> Telephone Call between David Hsu, Special Counsel, Division of Market Regulation, Commission, and Melanie Grace, Associate General Counsel, NYSE Group, Inc., on September 8, 2006.

under NYSE Arca Equities Rule 7.10(c)(1) that is subsequently upheld by the CEE Panel would discourage frivolous and abusive practices of the appeal process.

Since NYSE Arca Equities Rules 7.10(c)(2)-(4) were adopted, the Exchange has found that some ETP Holders have taken advantage of the process by categorically appealing all decisions in which they are involved, including decisions that involve a de minimis value. According to the Exchange, in effect, these ETP Holders file appeals simply to “get a second bite at the apple.” More specifically, in the months of August and September 2005, three ETP Holders were responsible for filing approximately 52% of all appeals filed at the Exchange. In addition, on July 26, 2005, an ETP Holder appealed an Exchange ruling to bust a 34-share transaction.

Furthermore, under NYSE Arca Equities Rule 7.10(c)(1), an ETP Holder may request that an NYSE Arca Equities officer review any transaction the ETP Holder regards as erroneous. Accordingly, an officer renders an official determination whether the transaction is erroneous and, if so, whether it should be canceled or modified. The initial determination made by the NYSE Arca Equities officer is done at no charge to the ETP Holder, and the Exchange believes that any further examination of the execution should incur a modest fee, in the event the original decision is upheld, to reduce the number of frivolous and abusive appeals.<sup>4</sup>

The Exchange notes that the appeal process draws upon the resources of not only the Exchange but also of the ETP Holders who volunteer as appeal panelists pursuant to NYSE Arca Equities Rule 7.10(c)(2)(A). Specifically, an appeal requires the efforts of two NYSE Arca Equities employees to accept and process the appeal (i.e., contact members in the pool of appeal panelists to determine their availability to serve on the CEE Panel, write up the circumstances of

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<sup>4</sup> Id.

the trade(s) leading up to the appeal, moderate the actual appeal that is conducted by conference call, contact the parties to the appeal after the CEE Panel reaches a decision and document the process and decision). From start to finish, the appeal process may take up to 1½ hours to complete.

Moreover, the CEE Panel is largely dependent on ETP Holder participation. Each panel member is a volunteer and dedicates his or her own time to the CEE Panel, which often meets during the busiest periods in a trading day. The Exchange believes that constant abuse of this process would likely foster volunteer frustration and may lead panelists to withdraw entirely from participating in the process.

The Exchange believes that appeals such as those described above represent an unintended use of the appeal process and demonstrate that abuses can proliferate when ETP Holders incur no downside risk to filing repeated appeals, whether valid or otherwise, and, in effect, are given a free second bite at the apple. Therefore, the Exchange believes that it necessary to limit the abuse of the process and reduce the number of frivolous and de minimis appeals by assigning a modest fee for all appeals that are upheld.<sup>5</sup>

When the Exchange amended NYSE Arca Equities 7.10(c)(2) to provide for an appeals process, the Exchange did not intend for the CEE Panel to serve as a redundant decision making mechanism, and it did not anticipate that the CEE Panel would be called upon to meet as frequently as it does today. Additionally, while the Exchange does not have statistical data surrounding other self-regulatory organizations' appeal processes, the Exchange understands that usage of their appellate mechanism is done sparingly and is not exploited by their members.

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<sup>5</sup> Id.

The Exchange did not anticipate these effects when it proposed NYSE Arca Equities Rule 7.10(c)(2)-(4). As a result, the Exchange deems it necessary to propose a fee of \$500 against each ETP Holder who appeals a decision made under NYSE Arca Equities Rule 7.10(c)(1) and such decision is confirmed by the CEE Panel.

2. Statutory Basis

The proposed rule change is consistent with Section 6(b)<sup>6</sup> of the Act, in general, and furthers the objectives of Section 6(b)(5)<sup>7</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principals of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanisms of a free and open market and a national market system.

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 purpose 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

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<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the Exchange consents, the Commission will:

- (A) by order approve the 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](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEArca-2006-48 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-NYSEArca-2006-48. 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 the Exchange. 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-NYSEArca-2006-48 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

Nancy M. Morris  
Secretary

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<sup>8</sup> 17 CFR 200.30-3(a)(12).