



**Securities Industry Association**

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April 26, 2002

Jonathan Katz  
Secretary  
U.S. Securities and Exchange Commission  
450 Fifth Street, N.W.  
Washington, DC 20549-0609

Re: File No. SR-NYSE-99-51; Order Tracking

Dear Mr. Katz:

The Ad-hoc OATS/OTS Committee of the Securities Industry Association (“SIA”)<sup>1</sup> is pleased to offer its comments in response to the proposed amendments to NYSE Rules 123 and 132 creating new requirements for order tracking.<sup>2</sup> The Committee consists of operations, systems, legal and compliance professionals from over twenty broker-dealers and was originally formed to respond to the NASDR’s Order Audit Trail System (“OATS”) proposal. The Ad-hoc Committee has worked diligently over the last several years with staff from the SEC and NASDR to provide industry input on certain reporting requirements of the OATS proposal which raise operational, systemic, competitive and best execution concerns.

The NYSE is proposing the adoption of new rules, which would require members and member organizations to record and retain order information. Specifically, the NYSE is proposing to add new reporting requirements to its existing Rule 123 requiring electronic capture of execution reports at the point of sale. The NYSE is also proposing in Rule 132 to require the electronic capture of orders at the point of receipt. The NYSE

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<sup>1</sup> The Securities Industry Association brings together the shared interests of nearly 700 securities firms to accomplish common goals. SIA member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift, and pension plans, and generates \$358 billion of revenue. Securities firms employ approximately 760,000 individuals in the United States. (More information about SIA is available on its home page: <http://www.sia.com>.)

<sup>2</sup> Exchange Act Release No. 45326; 67 FR 4479 (1/30/02).

states that the purpose of the amendments is to provide a complete systemic record of orders handles by members and member organizations.

SIA believes that the NYSE proposal raises many of the same concerns that we previously identified in the OATS context, particularly with respect to the handling of manual orders. Moreover, the rule filing does not address the cost to each firm or the industry as a whole of systemically linking information that resides in multiple locations in both electronic and non-electronic formats. Given these costs and the fact that the information sought is already maintained pursuant to SEC recordkeeping rules, SIA believes it is questionable whether the SEC could make the required statutory conclusion that this SRO rule promotes efficiency, competition, and capital formation.<sup>3</sup> For these reasons, we urge the Commission and the NYSE to reconsider the proposal.

SIA notes the following concerns in connection with the proposed rule changes:

Application to Manual Orders – The most pressing concern is how the NYSE rule will accommodate manual orders and how the recording of the required information will be accomplished. Creating an execution report from the comprehensive information already entered at the source of the execution, i.e, the trading desk, presents few logistical issues. However, creating a systemic record of an order from the multiple locations through which that order may pass, many of which may not be automated, is fraught with costs and problems.

Footnote 8 of Exchange Act Release No. 45326 states that for purposes of proposed Rule 132(b), the time of receipt of an electronic order is the time the order is received by an electronic order-routing or execution system while the receipt time for manual orders is defined as the time the order is first received by the member organization from the customer.<sup>4</sup> In the bigger firms, retail orders received at the branch are promptly entered into an order-routing or execution system, which can link up with information in execution and other systems to create a complete systemic record of the order. However, at many smaller firms, and especially in block trading areas of larger firms, the process of recording order information is still primarily by order ticket. In such cases, order information is not electronically captured and thus, cannot be linked to other data for the purpose of creating a complete systemic record of the order.

Compliance with the rule would not simply be a question of investing in new technology. For many kinds of orders – particularly blocks, thinly traded issues and those with special instructions - manual handling is still the most efficient method of order handling. Institutions typically communicate buying and selling interest to an institutional salesperson or sales trader who prepares physical order tickets. The sales

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<sup>3</sup> Section 3(f) of the Securities Exchange Act of 1934.

<sup>4</sup> We wish to convey at the outset the absolute need for the NYSE to define “receipt time” consistent with the NASD’s definition. A lack of consistency in defining common terms will only serve to confuse firm personnel responsible for complying with the rules and increase the costs of programming the changes required.

trader serves as the link between the customer and the point or points of execution (specialist, ECN, etc...) and uses his or her judgment and knowledge of the markets to determine how to obtain the best execution for the customer's order.

Even if there were no expense involved, there would be a huge cost to investors for requiring sales-traders to use such a system. As already noted, firm orders are quickly noted and time-stamped on an order ticket and these tickets are subject to recordkeeping under SEC rules). However, the task of collecting and electronically recording all required data elements would be significantly more time-consuming and would detain the sales-trader from his or her primary task – handling the customer's order. Timing and price are perhaps the most crucial factor that determine service on these types of orders and a few pennies on a 20,000 share order as a result of a missed market can add up. A legion of sales-traders performing clerical duties rather than monitoring markets for execution opportunities will make the markets riskier, less efficient and less accessible to investors.

Order Identifier – The NYSE rule changes would require the recording of an order identifier to be included with the order from the time it is received, through re-transmission to another department within the member, to another member, or to a non-member and finally through execution and reporting (or modification or cancellation).

It is one thing to be able to generate an order identifier for an execution as currently required by NYSE Rule 123 when the whole execution function occurs in one location and is already electronic. It is a wholly different task to be able to generate and transmit an order identifier when an order is manually received and manually re-transmitted up to the point of execution. As we noted in connection with the OATS proposal, two critical issues of implementation are left unaddressed by this proposal: (1) how will an originating firm generate an ID number for manually received orders that are routed to another member or market center for execution upon receipt? and (2) how will an originating firm reliably and efficiently transmit ID numbers for manually transmitted orders?

As we noted above, manually handled orders are typically written down and not entered into the receiving firm's system. Therefore, no systemic order identifier is systemically generated. Assigning a trader the responsibility of generating and appending an order identifier would compound the problems described above with respect to delay and inefficiency in the handling of orders. Furthermore, the risk of confusion, duplication and bad data will be exacerbated as the order identifier is orally relayed and recorded at multiple control points both inside and outside of the firm.

Moreover, given the difficulty of manually generating, relaying and repeating a multi-digit order identifier, order-routing decisions could increasingly be driven by the ability of an individual member or market center to offer an efficient means of recording and transmitting the information. Certainly, every firm and/or market center that could conceivably partner up on an order will need to have worked out a protocol for those

orders that pass between them. NYSE's statements regarding competitive impact to the contrary, it would appear that the exceptions to the rule proposed for orders transmitted to the NYSE floor via SuperDot and orders transmitted to another member on the Floor could give the exchange a leg up on competing market centers that are not already hard-wired to a member firm considering where to send order flow.<sup>5</sup>

Requirement to Record Online Comparison System ("OCS") Control Number – As required by the rule, broker-dealers would be required to record this number as part of the systemic record of the order. The number provides the firm with the means to check on any settlement problems that may occur between the firm and the exchange. This number does not incorporate customer-specific information and firms presently do not feed this number into the customer order or trade records that would most likely be used to produce the systemic record required by this rule. Firms would have to build such a feed and the cost would be significant.

This requirement is symptomatic of a broader concern relating to recordkeeping requirements. SIA appreciates the need for regulators to have audit trails to help facilitate our shared goals of investor protection, however, we believe it is essential to consider the interplay of these requirements with existing recordkeeping rules. Traditional SEC recordkeeping rules have focused on identifying the records that a firm must *maintain*. The SEC rules do not require records to be systemically linked. Instead, firms are free to organize the records in the manner they find most efficient provided that those records can be made available to regulators quickly and easily. Many new rules (like OATS and OTS), however, are mandating the grouping of selected individual records into a new systemic record for use by a specific regulator. These rules are not only duplicative of existing SEC rules, but each new customized systemic recordkeeping requirement requires a significant and costly retooling of recordkeeping resources.<sup>6</sup> We can appreciate each SRO's desire for access to specific records that interrelate in a systemic manner, but question whether the piecemeal introduction of customized recordkeeping requirements constitutes a wise approach.

We reiterate that we share the goal of modern recordkeeping and audit trails to serve investor protection goals. But firm resources for both compliance and technology are not unlimited, especially in the current economic environment. SIA believes it is much wiser for regulators and the industry to work together to maximize resources. We urge the SEC to evaluate the proliferation of individual customized recordkeeping requirements in the context of current practices and its own recordkeeping agenda. To develop a more consistent and comprehensive approach to recordkeeping, SIA believes

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<sup>5</sup> While the potential for misuse of the data is a concern, SIA believes that the statutory analysis of the burden on competition should focus on the degree to which ease of compliance with this rule will influence the choice of market centers. See Section 6(b)(8) of the Securities Exchange Act of 1934, which provides that the rules of an exchange shall "not impose any burden on competition not necessary or appropriate in furtherance of the purposes of this title."

<sup>6</sup> Indeed, heightened concerns about duplicative and inefficient rules associated with broker-dealer membership in multiple SROs has prompted a self-initiated GAO study into the existing regulatory structure and process by which such rules are developed.

the SEC, the SROs and the industry must work together on an overall framework that will better align the goals and resources of recordkeeping. We believe that this approach will improve coordination among regulators, will assist firms in discharging their critical compliance obligations, and will better achieve the ultimate goal of strengthening investor protection.

Requirement to include a Bunched Order Route Indicator – SIA believes that compliance with this provision may prove impossible. A firm typically does not know at the time an order is received whether the order will ultimately be part of a bunched order since the customer makes these determinations. This provision can only be complied with by retroactively locating and affixing an indicator to the various parts of an order, each of which may have been executed at a different marketplace or execution facility. The amount of time and personnel that would be required for this search effort would be so costly as to make the rule unworkable.

We thank you for the opportunity to present our views. If you have any questions or would like to discuss this further with the SIA Ad-hoc Committee, please contact Scott Kursman, Vice President and Associate General Counsel of the SIA, at 212-618-0508 ([skursman@sia.com](mailto:skursman@sia.com)).

Very truly yours,

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