

MEMORANDUM

February 1, 1980

TO: Commissioner Evans

FROM: Sheldon Rappaport, Deputy Director *SR*
Division of Market Regulation

SUBJECT: List of subjects for use in speech
before NYSE during first week of
March 1980

1. Modernization of NYSE trading and communication systems

- A. DOT--Provides direct communication to specialist posts from member firms' upstairs offices of orders of up to 499 shares. We are informed that from 20% to as many as 45% of trades are received and reported back to the member firms through the DOT system. Described by some, when it was first implemented in 1975 (?), as the NYSE's response to the Pacific Exchange's Scorex (formerly called "Comex") system, DOT has made it possible 4 and 5 years later for the NYSE to cope with greatly increased volume.
- B. NYSE program for adding mark-sense card transaction reporting terminals--This will reduce reporting time for transactions and quotation revisions (and will thereby reduce apparent trade-throughs), enhancing accuracy of sequencing of trades. The addition of a couple of mark-sense card readers in 1976 helped solve what appeared to be a tape racing problem in the options market by substantially reducing reporting time for NYSE stock transactions in IBM and one or two other securities. Even though that appeared primarily to benefit another marketplace, the CBOE, Mr. Batten's farsightedness helped avoid introduction of an additional regulatory framework to deal with the problem of tape racing. This was a useful lesson that self-regulatory initiative can serve as a prophylactic against what in the long run may be more complex and more costly governmental responses to problems unaddressed by self-regulatory organizations that do not hang together, to solve inter-market problems.
- C. Efforts to reduce ITS response time--Under the leadership of the NYSE efforts are being made to facilitate use of ITS: introduction of "universal template" which enables users to avoid replicating typed-in information in different fields of the

screen; addition of more ITS terminals throughout the floor; and experimentation in the use of mark sense cards.

- D. Upstairs market maker pilot--Described at pp. 70-73 of the NYSE's December 14, 1979 Progress Report to the SEC on National Market System and other Related Developments, and at pp. 9-11 of DME's January 9, 1980 Informational Memorandum on a Meeting with Representatives of NYSE, the pilot would appear to represent progress in that it would facilitate the ability of upstairs market makers to communicate from their upstairs trading room bids and offers in securities traded at different posts throughout the floor (e.g., oil stocks). However, the pilot would exclude use of the system by upstairs market makers to transmit agency orders, an anomaly in view of the NYSE's representations as to the presence of a continuous auction at its trading posts. Caution should be exercised in addressing this pilot since we have only a sketchy understanding of it.
- E. EAGLE, information retrieval system for broker-dealer compliance surveillance--This computerized system makes accessible at remote locations a central information file which, among other things, streamlines NYSE staff's inspections of member organizations and enables NYSE staff more efficiently to target firms for cause inspections where, for example, there have been an unusual number of customer complaints. Although the NASD also has been working on a similar system and although second and third generation systems can be expected to provide even greater efficiencies, EAGLE represents a welcome break-through in applying computer capability to what formerly had been highly labor intensive information collation.

II. Remaining Anticompetitive restraints

- A. Proposed Rule 19c-3. You needed no help on this.
- B. Rule 19c-2. You needed no help on this.

- C. Rule 113 (The portion of 113 which restricts specialists from transacting, without an intervening broker, with institutions) —It should be noted that elimination of this portion of Rule 113 would only tend to facilitate potential specialist competition on the NYSE floor. It would enable specialists to develop upstairs block capability and upstairs informational capability and enable upstairs firms who deal with institutions to compete as specialists on the NYSE floor.
- D. ITS--Cincinnati Interface--To date there has been no visible progress. The NYSE has refused to meet Cincinnati on the ITS interface. Our staff (George Simon and Dan Brooks) were so advised at a meeting with the ITS Operating Committee. The NYSE seems to want a hold-out principle from Cincinnati. You might observe that the NYSE does not appear willing to "hold out" its order flow to other markets. (As you know, the NYSE believes a hold-out is necessary where integrated firms have substantial public order flow but that when such firms bring their orders to the NYSE and other stock exchange trading posts, at least the specialist and his book are present and other persons may be.)
- E. ITS--NASD automated interface--The question here is whether the NYSE will continue to exclude member firms from an NASD interface. We understand that some progress is being achieved at an ongoing meeting in San Francisco. Rick Ketchum (272-2904), or George Simon (272-2880) will update you on this and also on a meeting which is to take place on February 12th. You may wish to observe in addressing ITS, as a system, that it, in effect, only permits competition from other market centers when the NYSE specialist decides not to match the competing quotation.

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Rick Ketchum (272-2904), Steve Parker (272-2890), George Simon (272-2880) and Doug Scarff are aware of your desire to discuss matters for inclusion in this speech. They will bring to your attention any additional developments. You should feel free to call on any of them. Rick will furnish you with relevant information and supporting documents and will contact you next week in that regard.

cc: Doug Scarff
George Simon
Rick Ketchum
Steve Parker