

TO: ALL MEMBERS AND MEMBER ORGANIZATIONS

SUBJECT: TWO NEW "CROSSING SESSIONS" IN THE OFF-HOURS TRADING FACILITY (RULES 900 & 907)

The Securities and Exchange Commission has approved¹ the establishment of two new crossing sessions in the Exchange's Off-Hours Trading Facility ("OHTF") for a pilot, beginning on **June 15, 2004** and expiring on December 1, 2004. The Exchange has adopted new Rule 907 (attached as Exhibit A) to establish:

- "Crossing Session III," for the execution of guaranteed price coupled orders by member organizations to fill the balance of customer orders at a price that was guaranteed to a customer prior to the close of the Exchange's 9:30 a.m. to 4:00 p.m. trading session.
- "Crossing Session IV," whereby an unfilled balance of an order may be filled at a price such that the entire order is filled at no worse price than the Volume Weighted Average Price ("VWAP") for the subject security.

An amendment to Rule 900 provides a definition of "guaranteed price couple orders." (also attached as Exhibit A).

Background

Currently, the OHTF consists of "Crossing Session I," which permits the execution at the Exchange's closing price of single-stock, single-side closing price orders and crosses of single-stock, closing price buy and sell orders.

The OHTF also consists of "Crossing Session II," which permits the execution of crosses of multiple-stock ("basket") aggregate-price buy and sell orders. The basket must meet the definition of a "program," a group of 15 or more stocks having a total market value of \$1 million or more. Trade reporting for Crossing Session II is accomplished by reporting to the Consolidated Tape the total number of shares and the total market value of the aggregate-

¹ See Securities Exchange Act Release No. 48857 (Dec. 1, 2003), 68 FR 68440 (Dec. 8, 2003).

price trades. No indication of the individual component stocks involved in the aggregate-price transactions is reported in Crossing Session II to the Consolidated Tape.

Additionally, CS II transactions must be reported to the Exchange via the Daily Program Trade Reporting (DPTR) application, and the member organization must also submit a CS II Detail Report, both by T+2. In this connection, please see Information Memo 03-9 (March 17, 2003) and Information Memo 04-31 for details, which from time to time may be supplemented by subsequent Information Memos.

"Upstairs Stops"/ Crossing Session III

In serving their institutional customers, member firms may offer them a guarantee that a large size order will receive no worse than a particular price. Such practice is usually referred to as an "upstairs stop," meaning that the firm guarantees its customer's order will be executed at no worse price than the agreed-upon, guaranteed price, with the member firm trading for its own account, if necessary, to effectuate the guarantee.

Typically, a member firm will seek to execute as much of the order as possible during the trading day at or below the "stop" price (in the case of a buy order) or at or above the "stop" price (in the case of a sell order). Any portion of the order not filled during the trading day will be completed after hours, with the firm either buying from, or selling to, its customer at a price which ensures that the entire order is executed at a price no worse than the "stop" price. Upon receipt of the order, the member organization would be required to document its "stop" price agreement with the customer.

The Commission has approved new post-4:00 p.m. "Crossing Session III" to accommodate member firms that are trading to complete an "upstairs stop" and thereby obviate any perceived need to execute these transactions in London or elsewhere.

VWAPs/Crossing Session IV

The Exchange has adopted a new Rule 907 to add "Crossing Session IV," a facility whereby member firms may fill the unfilled balance of a customer's order at a price such that the overall order is executed at a price that is no worse than the volume weighted average price ("VWAP") for the subject security on that trading day. Upon receipt of the order, the member firm would be required to document its VWAP agreement with the customer and the basis upon which the VWAP price would be determined.

New Rule 907 prescribes the operation of Crossing Sessions III and IV. Crossing Sessions III and IV would operate as follows:

- (i) the original order as to which an "upstairs stop" or "VWAP" has been granted must be for at least 10,000 shares;
- (ii) the customer must have received a "stop" (guaranteed price) or VWAP for the entire order;

(iii) upon receipt of the order, the member firm must record all details of the order, including the price it has guaranteed its customer or that the entire order will be filled at no worse than the VWAP;

(iv) the unfilled balance of the order that would be executed in Crossing Session III or Crossing Session IV must be at least 10,000 shares;

(v) the customer's order must be executed in Crossing Session III or Crossing Session IV at a price that ensures that the entire order is executed at a price that is no worse than the guaranteed price or the VWAP;

(vi) orders may be entered in Crossing Session III or Crossing Session IV between 4:00 p.m. and 6:30 p.m., and must be identified as either a Crossing Session III or Crossing Session IV order;

(vii) member firms will receive an immediate report of execution upon entering an order into Crossing Session III or Crossing Session IV;

(viii) orders may be entered into Crossing Session III for execution at prices outside the trading range in the subject security during the 9:30 a.m. to 4:00 p.m. trading session;

(ix) orders may not be entered into Crossing Session III or Crossing Session IV in a security that is subject to a trading halt at the close of the regular 9:30 a.m. to 4:00 p.m. trading session; and

(x) beginning at 6:30 p.m., the Exchange will print trades reported through Crossing Session III as guaranteed price coupled orders or in Crossing Session IV as VWAP executions.

Operation of Crossing Sessions III and IV

Entry of Crossing Session III and IV orders will take place in a web-based password protected system. The systems template will allow a user to enter multiple orders for both crossing sessions before submitting the details to the Exchange. Orders can be entered beginning at 4:00 p.m. and must be completed by 6:30 p.m. A link to this system will be emailed to all users who request it. For Security purposes, passwords will be distributed only by telephone.

The following details must be entered by participants for a cross to be valid:

- Side (Buy, Sell, Sell Short, as determined by the member firm's position),
- Order Size (at least 10,000 shares),
- price,
- program/non-program designation; and

- which crossing session the trade applies to.

After the cross details are submitted, traders will receive a status back from the Exchange on whether the trade is approved or rejected.

If the Crossing Session IV order is part of a program, as defined earlier, it must also be reported to the Exchange via the DPTR application in accordance with Information Memo 03-9 (March 17, 2003) and Information Memo 04-31. Additionally, there is no overlap between a program entered and executed in Crossing Session II and a VWAP order which is part of a program entered and executed in Crossing Session IV. A member organization can use either Crossing Session II or Crossing Session IV for entry and execution of a given program, or in the case of Crossing Session IV, part of a given program, but can NOT use both for the same program, given that all other requirements for entry of orders in either Crossing Session II or Crossing Session IV are met.

Extension of Hours of Operation of Crossing Session II

Effective **June 15, 2004**, Crossing Session II will be extended to 6:15 p.m., meaning that orders can be entered beginning at 4:00 p.m. and ending at 6:15 p.m. See also Info. Memo 04-31 on the Extension of Crossing Session II.

Questions concerning the subject matter of this Memo should be addressed to:

Operation of Crossing Sessions III and IV: Bob Airo (Competitive Position Group) at (212) 656-5663

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Attachments