Division of Market Regulation:
Staff Legal Bulletin No. 12

"Frequently Asked Questions About Rule 11Ac1-5"

Action: Publication of Division of Market Regulation Staff Legal Bulletin

Date: March 12, 2001

Summary: This staff legal bulletin sets forth the views of the Division of Market Regulation in response to frequently asked questions concerning Rule 11Ac1-5 under the Securities Exchange Act of 1934.

Supplementary Information: The statements in this legal bulletin represent the views of the staff of the Division of Market Regulation. This legal bulletin is not a rule, regulation, or statement of the Securities and Exchange Commission ("Commission"). Further, the Commission has neither approved nor disapproved its content.

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I. Introduction

In November 2000, the Commission adopted Exchange Act Rule 11Ac1-5 ("Rule").[1] The Rule generally requires a "market center" (as defined in the Rule) that trades national market system securities to make available to the public monthly electronic reports that include uniform statistical measures of execution quality. The initial compliance date for the Rule recently was moved back by one month until May 1, 2001.[2] Accordingly, the first monthly reports (for May 2001) must be made available to the public by the end of June 2001.

The Rule also directed the self-regulatory organizations ("SROs") that trade national market system securities to act jointly and submit to the Commission a new national market system plan establishing procedures for market centers to follow in making their monthly reports available to the public. The SROs submitted such a plan ("Proposed Plan") on February 20, 2001, and it has been published by the Commission for public comment.[3] A copy of the Proposed Plan is attached as Appendix A.

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1 Securities Exchange Act Release No. 43590 (November 17, 2001), 65 FR 75414 ("Adopting Release").

2 Securities Exchange Act Release No. 44060 (March 9, 2001).

3 Securities Exchange Act Release No. 43992 (February 21, 2001), 66 FR 12571.

Since adoption of the Rule, the Division of Market Regulation ("Division") has received a number of inquiries concerning the implementation and operation of the Rule, some of which indicate that general interpretive guidance would be helpful. The Division is issuing this staff legal bulletin to address a variety of frequently asked questions.

The following questions and answers do not necessarily contain a discussion of all the material considerations necessary to reach the conclusions stated. Consequently, these questions and answers are intended to provide general guidance, but the facts and circumstances relating to particular market centers may differ, and the staff notes that even slight variations may require different responses. The Commission is not bound by these statements and may interpret the Rule as it deems necessary or appropriate in the public interest or for the protection of investors.

In addition, these questions and answers are premised on several important assumptions. First, the discussions assume close familiarity with the text of the Rule and the Adopting Release, and we urge you to read carefully the Rule and Adopting Release. The responses are a complement to, and not a substitute for, these sources. Second, the terms used in this staff legal bulletin have the meanings set forth in the definitions of paragraph (a) of the Rule. Third, several responses refer to specific provisions of the Proposed Plan in its current form. These responses are subject to change if the Commission does not approve the Proposed Plan or does not approve the Proposed Plan in its current form.

The Division may update these questions and answers periodically by issuing an updated staff legal bulletin. In each updated staff legal bulletin, the questions and answers with new material since the last update will be marked as "*new*."

The interpretive questions addressed in this bulletin are as follows:

Question 16: Adjusted or Voided Order Executions
Question 17: Calendar Month Reporting
Question 18: Phase-In of Reporting

II. Questions and Answers

Question 1: Format of Monthly Reports and Procedures for Making Reports Publicly Available

Q: What format and procedures should market centers follow in preparing their monthly reports and making them available to the public?

A: The format of monthly reports and procedures for making them available to the public are spelled out in the Proposed Plan, attached as Appendix A. In general, it requires market centers to make their monthly reports available in the form of electronic data files (standard, pipe-limited ASCII files). The Proposed Plan also sets forth in detail the required contents of the electronic data file, including the identity and order of the 26 fields of information that the file must contain.

Attached as Appendix B is a table indicating how a market center's statistics could appear for a single security "A" in a report on trading for the month of May 2001. Appearing horizontally across the page (designated as F1, F2, F3 . . . F26) are the 26 required fields of information. A description of each of the fields may be found in paragraphs (a)(1) through (a)(26) of Section VI of the Proposed Plan.

Appearing vertically down the page are 20 records – one reflecting each of the possible subcategories of order type (of which there are 5)[4] and order size (of which there are 4)[5] required for a single security. Sample statistics are provided in the table for the first record (representing market orders for 100-499 shares) to give a general idea of what a market center's statistics may look like. A full report would contain separate records for each individual national market system security upon which a market center must report. Although there potentially could be as many as 20 separate records for each individual security, Section VI(b) of the Proposed Plan provides that no record need be displayed if a market center received no covered orders that fall within the particular subcategory of security/order type/order size.

The electronic data files containing market center reports must be made available for downloading (through FTP) without charge from an Internet site ("Download Site"). Under

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4 The codes for order types are set forth in Section VI(a)(5) of the Proposed Plan as follows: market orders – "11"; marketable limit orders – "12"; inside-the-quote limit orders – "13"; at-the-quote limit orders – "14"; near-the-quote limit orders – "15".

5 The codes for order sizes are set forth in Section VI(a)(6) of the Proposed Plan as follows: 100-499 shares – "21"; 500-1999 shares – "22"; 2000-4999 shares – "23"; 5000 or more shares – "24".

Section VIII of the Proposed Plan, every market center will be responsible for making arrangements with an SRO to act as the market center's "Designated Participant." Designated Participants are responsible for assigning a unique market center identification code (which must be set forth in Field 2 of a market center's electronic data file)[6] to each market center for which it acts as Designated Participant.

In addition, every market center must notify its Designated Participant of the hyperlink to the market center's Download Site. In turn, each Designated Participant will maintain an Internet site ("Link Site") that includes a comprehensive list of hyperlinks to the respective Download Sites for all of its market centers. In this way, anyone who wishes to download all market center reports for each month can be assured that, if they visit the Link Sites of all Designated Participants, they will find hyperlinks to files containing all market center reports.

Question 2: Vendor or SRO Assistance in Making Reports Available

Q: Does the Rule require every market center to make its monthly reports available to the public in a separate file on its own Internet site, or is it permissible for a market center to arrange with other entities (such as a vendor or a market center's SRO) for assistance in making the market center's reports available?

A: A market center need not make is reports available on its own Internet site. Market centers have the option to make arrangements with other entities to perform the functions necessary to make their reports available to the public. Nor must each market center's report be downloadable in a separate data file. Thus, for example, an SRO may make the monthly reports for all of its members available in a single file. Section VIII of the Proposed Plan establishes procedures that will allow the public to determine the name of the file containing every market center's reports and the location where the file can be downloaded.

Question 3: Definition of Market Center – Multiple Trading Venues

Q: Firm X acts both as an exchange specialist and as an OTC market maker. How should Firm X report under the Rule?

A: Firm X operates as two separate market centers and must report separately (with a separate market center identification code) on trading in each venue.

The definitions in paragraph (a) of the Rule set out the different types of market centers that must report under the Rule. The term "market center" is defined in paragraph (a)(14) as "any exchange market maker, OTC market maker, alternative trading system, national securities exchange, or national securities association." An "exchange market maker" is defined in paragraph (a)(9) of the Rule as "any member of a national securities exchange that is registered as a specialist or market maker pursuant to the rules of such exchange." An "OTC market maker" is defined in paragraph (a)(18) of the Rule as "any dealer that holds itself out

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6 See Section VI(a)(2) of the Plan.

as being willing to buy from and sell to its customers, or others, in the United States, a national market system security for its own account on a regular or continuous basis otherwise than on a national securities exchange in amounts of less than block size."

Accordingly, Firm X, because it acts both as an exchange specialist and as an OTC market maker, would be considered two separate market centers under the Rule and must report separately on its trading in each venue. The same result would hold if a firm acted as a specialist on two different exchanges. The Rule is intended, among other things, to provide investors and the public with order execution information that will assist them in making order routing decisions. Different exchanges have different trading rules and systems that can affect order execution quality, as do firms when they act as OTC market makers. It therefore is important that monthly reports under the Rule reflect these differences.

Question 4: Integrated Broker-Dealer Firms – Orders Received as Market Center and Orders Received Solely as Agent for Routing

Q: Firm X is an integrated broker-dealer that acts as an OTC market maker in 500 national market system securities and also accepts orders in other national market system securities solely as agent for routing to other market centers for execution. In addition, Firm X sometimes receives orders in its 500 market maker stocks that, either because of specific customer instructions or the nature of the particular customer (for example, an advisory client), Firm X is required to route as agent to another market center for execution. How should Firm X report its activities under the Rule?

A: The Rule applies to broker-dealers insofar as they act as a "market center" with respect to orders received from other persons. Consequently, for orders in securities for which Firm X does not act as an OTC market maker, Firm X would not be acting as a market center in those securities and therefore need not report on orders in those securities that it receives as agent and routes elsewhere for execution.

Conversely, the orders that Firm X receives from any person in the 500 securities in which it acts as an OTC market maker (and therefore is a market center) generally must be included in Firm X's monthly reports, even if Firm X ultimately routes some of the orders to other market centers for execution. These orders would be reflected in the "shares executed at any other venue" statistic required by paragraph (b)(1)(i)(E) of the Rule and otherwise would be reported in exactly the same way as if the order were executed at Firm X.

If, however, Firm X receives orders in stocks for which it acts as an OTC market maker that Firm X is required to route as agent to another market center for execution (either because of specific customer instructions or the nature of the particular customer -- it is, for example, an advisory client), then Firm X would not act as a market center for these types of orders and need not include them in its monthly reports.

Question 5: Definition of Covered Order – Special Handling Exclusions

Q: The Rule's definition of "covered order" specifically excludes a number of types of orders for which the customer requests special handling and therefore are not covered by the Rule. Are there other types of orders that fall within the special handling exclusion, such as fill-or-kill and average price orders?

A: The definition of covered order in paragraph (a)(8) of the Rule does not specifically identify every type of order that may fall within the "special handling" exclusion. In general, any market or limit order for which the customer requests a type of handling that may preclude the order from being executed promptly at the current market price at the time of order receipt (subject only to a limit price) would qualify for the special handling exclusion and not be covered by the Rule. Accordingly, fill-or-kill orders are excluded because they must be executed only at their full size ("executed only at their full size" is one of the specific examples in the Rule of a special handling order). In addition, average price orders (understood as orders that are not intended to be executed promptly at the current market price at the time of order receipt but at an average price over a period of time) also would qualify as special handling orders and be excluded from the Rule.

Question 6: Exemption for Manually-Received Orders

Q: Is a market center required to report on orders that it receives "manually" -- otherwise than through automated systems?

A: Not now. The Commission has issued an exemption pursuant to paragraph (c) of the Rule that temporarily exempts orders received by a market center otherwise than through automated systems.[7]

Although market centers receive the overwhelming majority of their orders through automated systems, they also receive orders manually, particularly those for large sizes. Many of these orders may qualify for one of the "special handling" exclusions from the definition of "covered order" under paragraph (a)(8) of the Rule. Nevertheless, unless the necessary information is captured in automated systems, it would be quite difficult to include these orders in the required statistics or to efficiently demonstrate that a particular exclusion applies. The exemption of manually-received orders from the Rule is intended to facilitate timely compliance with the Rule until market centers have automated systems in place to capture all orders.[8]

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7 See Letter from Annette L. Nazareth, Director, Division, SEC, to Stuart J. Kaswell, Senior Vice President and General Counsel, Securities Industry Association, dated March 12, 2001 ("SIA Exemption Letter").

8 For example, NASD Regulation currently is working on implementing Phase Three of the Order Audit Trail System ("OATS"), which would cover orders that are received manually by a firm's trading department. Exchange markets also are developing automated systems to capture manual orders.

Integrated broker-dealer firms, however, should be aware that the exemption only covers orders that are routed directly by manual means to the firm's trading desk. Orders received manually from brokerage customers, which are then input into an automated system for routing and execution would not be eligible for the exemption and would continue to be subject to the Rule. The time of receipt for such orders would be the time that the orders are captured in the automated system.[9]

In addition, this exemption is intended to facilitate compliance with the Rule for orders that currently are not captured in automated systems. Any change in order routing practices from automated to manual means to avoid reporting of orders under the Rule would be the basis for withdrawal of the exemption from that market center, and would raise serious questions with respect to a broker-dealer's obligation to obtain the best execution of its customers' orders.

Question 7: Locked and Crossed Quotes

Q: In several different contexts, the Rule requires reference to the consolidated best bid and offer ("Consolidated BBO") disseminated pursuant to an effective national market system plan. How should market centers report on orders whose statistics would be affected by a Consolidated BBO that is locked or crossed?

A: If the Consolidated BBO is locked (the best bid to buy equals the best offer to sell), the quotes still should be used for all purposes under the Rule. If the Consolidated BBO is crossed (the best bid to buy is higher the best offer to sell), a market center should follow the procedures set forth below.

The Rule requires reference to a Consolidated BBO in four different contexts: (1) classifying limit orders based on the Consolidated BBO at the time of order receipt into one of four categories defined in the Rule (marketable, inside-the-quote, at-the-quote, near-the-quote); (2) calculating the average effective spread for market and marketable limit orders based on the Consolidated BBO at the time of order receipt; (3) classifying executions of market and marketable limit orders as "with price improvement," "at the quote," or "outside the quote" based on the Consolidated BBO at the time of order receipt; and (4) calculating the average realized spread for all five types of orders defined in the Rule (market orders and the four types of limit orders) based on the Consolidated BBO five minutes after the time of order execution (as opposed to the time of order receipt).

When the Consolidated BBO is crossed for a significant period of time, it raises serious questions whether the quotes continue to provide a reliable benchmark for the statistical measures included in the Rule. The Commission therefore has exempted all orders from the Rule that would require reference to a Consolidated BBO that has been crossed for 30

9 See Question 13 below.

seconds or more.[10] In light of this exemption, market centers should follow the following procedure whenever a reference to the Consolidated BBO is necessary, whether at the time of order receipt or the time of order execution:

First, use the Consolidated BBO if the quotes are not crossed, or are locked.

Second, if the Consolidated BBO is crossed, reject the crossed quotes and use the next-in-time uncrossed Consolidated BBO if there has been less than 30 seconds between the last-in-time uncrossed Consolidated BBO and the next-in-time uncrossed Consolidated BBO.

Third, if there has been 30 seconds or more between the last-in-time uncrossed Consolidated BBO and the next-in-time uncrossed Consolidated BBO, the affected order is exempted from the Rule and must be excluded entirely from a market center's report (even if the crossed Consolidated BBO only affects a partial execution of the order).

The following examples illustrate how the foregoing procedure should apply:

Example 7-1: At 11:08:10,[11] a market center receives a limit order to buy 100 shares of Security A with a limit price of $20.75. The Consolidated BBO for Security A at the time of order receipt is $20.75 bid and $20.75 offer.

The locked quotes should be used. The order therefore would be classified as a "marketable limit order" under paragraph (a)(15) of the Rule because the limit price is equal to the consolidated best offer at the time of order receipt.[12] The midpoint of the Consolidated BBO for purposes of calculating an effective spread for the execution is $20.75. If the buy order is executed at a price of $20.75, the execution would classified as "at the quote" under paragraph (a)(10) of the Rule. If the buy order is executed at any price lower than $20.75, the execution would be classified as "with price improvement" under paragraph (a)(12) of the Rule. The calculation of a realized spread for the execution would be based on the midpoint of the Consolidated BBO five minutes after the time of order execution, so that the locked quotes at the time of order receipt would be irrelevant.

Example 7-2: At 2:47:20 p.m., a market center receives a market order to sell 500 shares of Security A. The Consolidated BBO for Security A at the time of order receipt is $55.40 bid and $55.30 offer. The time of the last uncrossed Consolidated BBO was 2:47:05 p.m. The next uncrossed Consolidated BBO is disseminated at 2:47:30 p.m. and is $55.35 bid and $55.35 offer. The market center should reject the crossed quotes at the time of order receipt and instead use the uncrossed quotes at 2:47:30 (even though they were locked) as the

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10 See SIA Exemption Letter, note 7 above.

11 The time of order receipt and time of order execution must be recorded "to the second" under paragraphs (a)(20) and (a)(21) of the Rule.

12 Note that the limit order could not be classified as an at-the-quote limit order because the definition of "at-the-quote limit order" in paragraph (a)(13) of the Rule only applies to -marketable limit orders."

Consolidated BBO at the time of order receipt. The midpoint of the Consolidated BBO for purposes of calculating the effective spread for the order execution is $55.35. If the market order to sell is executed at a price higher than, equal to, or lower than $55.35, the execution will be classified, respectively, as "with price improvement, "at the quote," or "outside the

Example 7-3: Same facts as Example 7-2 except that the next-in-time uncrossed Consolidated BBO after the time of order receipt is disseminated at 2:47:40 p.m. Because the period between the last-in-time uncrossed Consolidated BBO (2:47:05) and the next-in-time uncrossed Consolidated BBO (2:47:40) is 30 seconds or more, the market order to sell 500 shares of Security A is exempted from the Rule and must be excluded from the market center's monthly report.

Question 8: Trading Halts

Q: How should orders for a security be handled when they are received during regular trading hours, but trading in the security is halted at the market center either at the time of order receipt or shortly thereafter? Does the answer differ depending on whether the trading halt is a general regulatory halt or occurs solely at the particular market center that received the order?

A: The manner of reporting on orders under the Rule will be the same for all "announced" trading halts. To qualify as an "announced" trading halt, the halt must be either a general regulatory halt or a trading halt that is announced by a market center in accordance with all applicable regulatory rules. Orders that are received prior to and during the time of an announced trading halt should be handled in accordance with the following procedures.

First, all orders received during the period that trading is halted must be entirely excluded from a market center's monthly report. [13]

Second, if an order was received less than five minutes prior to the trading halt and remains outstanding (in whole or in part) at the time of the trading halt, the entire order is exempted from the Rule[14] and should be excluded from the market center's monthly report.

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13 To be a "covered order" under paragraph (a)(8) of the Rule, an order must be received during "regular trading hours" (defined in paragraph (a)(19) of the Rule) and during a time when a Consolidated BBO is being disseminated pursuant to an effective national market system plan. Consequently, any orders received during a regulatory trading halt (when no Consolidated BBO will be disseminated) are excluded from the definition of covered order. In addition, to assure uniform treatment of orders affected by trading halts, the Commission has exempted orders received during non-regulatory trading halts that are announced in accordance with all applicable regulatory rules. See SIA Exemption Letter, note 7 above.

14 See SIA Exemption Letter, note 7 above.

Third, for orders that are executed less than five minutes prior to the trading halt, the calculation of average realized spread should use the last Consolidated BBO disseminated prior to the time of the trading halt (analogous to the treatment of orders executed less than five minutes prior to the close of regular trading hours that is set forth in paragraph (a)(3) of the Rule).

Fourth, if an order was received five minutes or more prior to the trading halt and remains outstanding (in whole or in part) at the time of the trading halt, the order continues to be covered by the Rule; provided, however, that for executions that occur after the end of the trading halt, a market center may deduct the time period during which trading was halted from the calculations using the time of execution of the order.

The following examples illustrate how these foregoing procedures should apply:

Example 8-1: At 10:45:30 a.m., Market Center X halts trading in all securities because of a serious systems breakdown. It announces the trading halt in accordance with all applicable regulatory rules. At 11:25:30 a.m., Market Center X resumes trading in all securities. All orders received for execution by Market Center X from 10:45:30 until 11:25:30 are exempted from the Rule and must be excluded from Market Center X's monthly report.

Example 8-2: Same facts as Example 8-1, except that Market Center X receives a marketable limit order at 10:44:45 that is unexecuted at the time trading is halted 45 seconds later. The order is exempted from the Rule and must be excluded from Market Center X's monthly report.

Example 8-3: Same facts as Example 8-1, except that Market Center X receives a marketable limit order for 500 shares at 10:42:15 that receives a partial execution of 200 shares at 10:42:20, with the balance of 300 shares still unexecuted and outstanding at the time of the trading halt. The entire order is exempted from the Rule and must be excluded (including the 200-share execution) from Market Center X's monthly report.

Example 8-4: Same facts as Example 8-1, except that Market Center X receives a near-the-quote limit order at 10:38:15 a.m. that is unexecuted and outstanding at the time of the trading halt. At 11:28:05 a.m., after the end of the trading halt, the order is executed. Because the order was received more than five minutes before the trading halt, the order remains covered by the Rule, except that Market Center X may deduct the 40-minute period of the trading halt from the time of execution. The time of execution for non-marketable limit orders must only be reported in one of the five time buckets set forth in paragraphs (b)(1)(i)(F) through (J) of the Rule. Accordingly, the execution of the order would fall within the time bucket for order executions between 5 and 30 minutes after the time of order receipt (11:28:05 minus 10:38:15 minus 40 minutes).

Question 9: Activity within the Intermarket Trading System (“ITS”)

Q: Must a market center report on commitments to trade that are received from other market centers pursuant to ITS Plan provisions?

A: Yes. Market centers are required to report under the Rule on commitments to trade received pursuant to the ITS Plan procedures. If a market center’s handling of ITS commitments to trade differs materially from its handling of orders received through other mechanisms, it would be permissible to report on ITS activity as a separate market center (i.e., by obtaining a separate market center identification code pursuant to Section VIII of the Proposed Plan for the market center’s ITS activity).

Question 10: Activity within SOES and SelectNet

Q: How should orders sent to Nasdaq’s Small Order Execution System (“SOES”) and through its SelectNet system be reported under the Rule?

A: SOES is itself a market center for which Nasdaq will issue monthly reports under the Rule.

SelectNet, in contrast, is merely an order routing system and is not a separate market center. Market centers therefore must report under the Rule on orders received through SelectNet that are routed specifically to them for execution. Analogous to the treatment of ITS activity set forth in Question 9 above, if a market center’s handling of SelectNet orders differs materially from its handling of orders received through other mechanisms, it would be permissible to report on SelectNet orders as a separate market center (i.e., by obtaining a separate market center identification code pursuant to Section VIII of the Proposed Plan for the market center’s SelectNet activity).

Finally, SelectNet “broadcast” orders (which are not directed to any specific market center) would not be considered as received for execution by any market center and therefore should not be reported under the Rule.

Question 11: Partial Executions and/or Partial Cancellations

Q: How should a market center report on partial executions and partial cancellations of orders under the Rule?

A: The Rule’s statistics are designed to handle multiple partial executions and/or cancellations of an order. Immediately upon receipt by a market center, an order is permanently classified as falling within one of the 20 possible records relating to a subcategory of security/order type/order size. Thereafter, all executions and/or cancellations of the order will be included in the fields of information for that single record. Except for the field of information for total number of covered orders, all of the other fields of information required by the Rule are reported in terms of number of shares or share-weighted amounts. Consequently, each partial execution or cancellation can be reflected separately in the statistics.

Example 11-1: A market center receives a market order to buy 3000 shares of Security A at 3:30:00 p.m. The Consolidated BBO for Security A at the time of order receipt is $25.30 bid and $25.60 offer. The market center executes the order in three partial executions: 400 shares at $25.50 at 3:30:08, 1000 shares at $25.55 at 3:30:15, and 1600 shares at $25.60 at 3:31:02.

The market center would report on the 3000 share market order as follows. First, the order would be classified at the time of order receipt as falling within the record for Security A/market orders/2000 to 4999 shares. Thereafter, all information relating to the order will be included in one of the fields for that single record. Thus, 400 shares would fall within the field for shares executed from 0-9 seconds; 1000 shares would fall within the field for shares executed from 10-29 seconds; and the remaining 1600 shares would fall within the field for shares executed from 30-59 seconds.

Next, in calculating effective spreads, each partial execution would be treated separately and weighted according to the size of the partial execution. Thus, the effective spread for the first execution would be 10 cents: 25.50 minus 25.45 (the midpoint of the Consolidated BBO at the time of order receipt) multiplied by 2; the effective spread for the second execution would be 20 cents: 25.55 minus 25.45 multiplied by 2; and the effective spread for the final execution would be 30 cents: 25.60 minus 25.45 multiplied by 2. The 10 cent effective spread would be weighted by 400 shares, the 20 cent effective spread would be weighted by 1000 shares, and the 30 cent effective spread would be weighted by 1600 shares.

The remaining fields of information required for an order would be calculated in an analogous manner (e.g., a separate realized spread would be calculated for each partial execution).

Example 11-2: Same facts as Example 11-1, except that the final 1600 shares were cancelled by the customer prior to execution. All calculations discussed above under Example 11-1 would remain the same for the first two partial executions, but the final 1600 shares would now simply be included in the field of information for shares cancelled prior to execution.

Question 12: Orders Left Unexecuted and Uncancelled at End of Regular Trading Hours

Q: How should a market center report on orders received during regular trading hours, but that remain unexecuted and uncancelled at the end of regular trading hours on the day of order receipt?

A: Orders left unexecuted and uncancelled, in whole or in part, at the end of regular trading hours on the day of order receipt should be reflected in the market center's monthly report as having been received. No further information, however, should be reported concerning the unexecuted part of such orders, regardless of whether they are executed or cancelled in the hours, days, or weeks after the end of regular trading hours on the day of order receipt. In other words, a market center's statistical report should reflect the disposition of orders solely during regular trading hours on the day of order receipt, and each day begins with a clean slate of orders.

Example 12-1: A market center receives a 500 share at-the-quote limit order in Security A at 10:45:00 on April 30. At 10:45:08, 300 shares of the order are executed at the limit price. The remaining balance of 200 shares is left unexecuted and unexecuted at the end of regular trading hours on April 30. At 9:45:00 on the next day, May 1, the remaining 200 shares are executed.

The market center would reflect the order in its April report as follows. A single at-the-quote limit order for 500 shares would be reflected as having been received. The 300 share partial execution would be included in the field of information for shares executed at the market center and shares executed from 0-9 seconds after the time of order receipt. In addition, a realized spread would be calculated for the partial execution (the Rule does not require an effective spread and price improvement/disimprovement statistics for non-marketable limit orders). Nothing would be reported concerning the 200-share execution that occurred the following day, either in the market center's April report or in the market center's May report.

Question 13: Establishing Time of Order Receipt

Q: How should a market center establish the time it receives an order when the order passes through various automated systems before it actually reaches the point at which it is executed? What about an integrated broker-dealer firm that initially receives orders from its brokerage customers?

A: A market center must assign a time of order receipt to its orders at the time they first are captured in an automated order handling system operated by, or on behalf of, the market center. For an integrated broker-dealer that receives orders from its brokerage customers, the time of order receipt is the time that it first captures these orders in the firm's automated order handling system.[15]

The time of order receipt is an essential element in calculating nearly every one of the Rule's statistics, such as assigning quotes as benchmarks for effective spread and price improvement statistics, as well as calculating speed of execution statistics. In the Adopting Release, the Commission emphasized that "it is critically important for market centers to assign a time of receipt (including seconds) to orders in a prompt, consistent, and non-manipulatory manner" and that "failure to meet the standard would be a serious violation of the Rule.[16] Examples of such compliance concerns would include a market center queuing orders without immediately assigning a time stamp or a market center implementing preliminary selection

15 In this respect, integrated broker-dealers will assign a time of order receipt under the Rule in the same way that such a time is assigned under the NASD's OATS rules. See Securities Exchange Act Release No. 43344 (Sept. 26, 2000), 65 FR 59038 (NASD proposed rule change relating to amendments to Order Audit Trail System Rules).

16 Adopting Release, note 1 above, section III.C.1.

criteria (e.g., to determine whether an order should be retained or routed to another market center for execution) prior to the time that the orders are marked as received and assigned a time of order receipt.

Question 14: Orders Received in Same Second as a Quote Change

Q: The Rule requires market centers to record the time of order receipt "to the second." How should a market center assign a Consolidated BBO to an order that is received during the same second as one or more quote changes?

A: A market center may use any neutral algorithm to assign a Consolidated BBO to orders that are received during the same second as one or more quote changes. An algorithm is neutral if it chooses the quote in a consistent manner without reference to its impact on the market center's statistics. For example, it would not be appropriate for a market center to adopt an algorithm that assigns the intra-second Consolidated BBO with the highest offer to market orders to buy and the Consolidated BBO with the lowest bid to market orders to sell.

Question 15: Time of Execution for "Stopped" or "Guaranteed" Orders

Q: Is it permissible for a market center to assign an execution time to orders when they are "stopped" or "guaranteed" an execution at no worse than a specific price and later assigned a specific execution price?

A: Yes. The statistical measures required by the Rule may be calculated using the guarantee time as the time of order execution, but only under the following conditions. First, the guarantee must be made pursuant to an SRO rule setting forth the standards for guaranteed or stopped executions. Second, the customer must be immediately informed of the guarantee and the guarantee price. Third, the guarantee must be final with no opportunity for rescission. Finally, the guarantee price must be no worse than the Consolidated BBO at the time of order receipt and for the full size of the order.

If guarantee time is used as the time of execution for an order, it must be used for all purposes under the Rule, including both the calculation of speed of execution statistics and the calculation of average realized spread, as defined in paragraph (a)(3) of the Rule.

Question 16: Adjusted Or Voided Order Executions

Q: How should a market center report an order execution whose terms are subsequently adjusted or an order execution that is voided entirely?

A: If the terms of an order execution are adjusted or the execution is voided within a normal settlement cycle, the market center should report on the order in accordance with the terms of execution as they were finally received by the customer. Orders not adjusted or voided until after the normal settlement cycle should be reported as they were originally executed.

Example 16-1: A market center originally executes a market order to buy 200 shares of Security A at $15.80. The next day and prior to settlement, the market center receives an "exceptions report" indicating that the order should have been executed at a more favorable price to the customer. The market center adjusts the price to $15.70 and gives this price to the customer. The market center should report on the order based on a $15.70 execution price. All other reporting would remain the same (e.g., time of order execution).

Question 17: Calendar Month Reporting

Q: Should a market center's monthly report encompass all trading days that fall within a calendar month, as opposed to settlement days that fall within the calendar month?

A: A market center's monthly report should encompass all trading days that fall within the calendar month. Thus, orders received and executed on April 30 must be reported in a market center's April report, even though trades were not settled until May.

Question 18: Phase-In of Reporting

Q: The Adopting Release sets forth a phase-in of compliance dates for the Rule in three stages, with the 1000 NYSE, 1000 Nasdaq, and 200 Amex most actively traded securities to be reported in the initial phase-in that is now set for May 1, 2001. Is it permissible for a market center to begin reporting on all securities covered by the Rule on the initial compliance date?

A: Yes. Nothing prohibits a market center from reporting on all national market system securities covered by the Rule on the May 1, 2001 initial compliance date.

Attachments Appendix A (Proposed Plan)
Appendix B (Table with Rule 11Ac1-5 Sample Statistics)