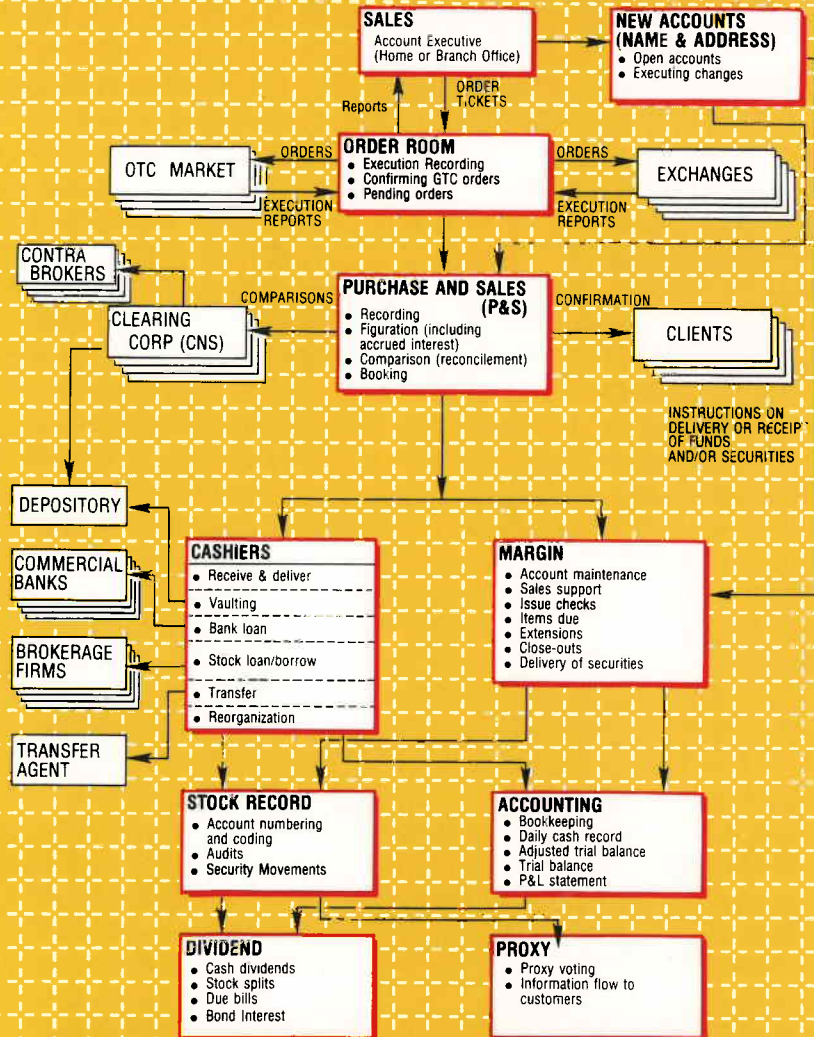


Second Edition

AFTER THE TRADE IS MADE

Processing Securities Transactions



DAVID M. WEISS

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executes because of priority, C executes because of precedence, and B executes before D because of time advantage.

Parity. When two brokers can both fill the order and both enter their intentions at the same time, there isn't any logical way of awarding the trade. This is parity. In this case, either the brokers agree to an equitable distribution, or they flip a coin and the winner takes the trade.

Example: The quote is 22-1/2, and the bids are:

Broker M: 100 shares, 10:14

Broker N: 100 shares, 10:15

Broker O: 100 shares, 10:15

If Broker Z enters the crowd with a sell market order for 100 shares, Broker M executes. If Broker Z enters the crowd with a sell market order for 200 shares, M executes 100 shares. Since Brokers N and O can fill or best fill the order and neither has a time advantage, they have parity. So Brokers N and O either agree to one of these two taking the 100 shares or toss a coin, and the winner of the toss executes 100 shares.

When an execution takes place, *the floor is cleared*, all remaining bids or offers at that price must be resubmitted. This procedure keeps quotes updated while reaffirming all orders.

The Specialist's Book

Specialists enter public orders, that are away from the market, in their books by price and in the order they are received.

Example: See Figure 4-2. If this specialist's book represents the highest bid and lowest offer of the crowd, the quote is 22 1/4-5/8. The highest bid is 22 1/4, the lowest offer, 22 5/8. If these orders are the only shares comprising the quote, the size is 5 by 9. The largest order for a buy at 22 1/4 is for 500 shares (200 by Broker D and 300 by Broker E). The largest order for sale at 22 5/8 is 900 shares (300 by Broker F and 600 by Broker G).

Specialists execute orders from their books by price on a first-in/first-out (FIFO) basis. The first order in is the first order out.

Example: If Broker Z enters the crowd with a 200-share buy order at the market, the specialist executes 200 of Broker F's 300-share order at 22 5/8.

because of precedence, and B stage.

both fill the order and both... there isn't any logical way... In this case, either the... or they flip a coin and

ids are:

all market order for 100 shares, the crowd with a sell market order... since Brokers N and O can fill or... advantage, they have parity. So... these two taking the 100 shares... s executes 100 shares.

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are away from the market, in... r they are received.

ist's book represents the highest... quote is 22 1/4-5/8. The highest... these orders are the only shares... 9. The largest order for a buy at... and 300 by Broker E). The largest... 0 by Broker F and 600 by Broker

m their books by price on a... first order in is the first order

with a 200-share buy order at the... broker F's 300-share order at 22 5/8.

FIGURE 4-2. A page in the specialist's book.

| BUY | | SELL |
|----------------------------|-----|----------------------------|
| BKR R - 100 | 22 | |
| | | |
| BKR L - 300 BKR A - 500 | 1/8 | |
| | | |
| BKR D - 200 BKR E - 300 | 1/4 | |
| | | |
| | 3/8 | |
| | | |
| | 1/2 | |
| | | |
| | 5/8 | BKR F - 300 BKR G - 600 |
| | | |
| | 3/4 | BKR B - 100 BKR M - 200 |
| | | |
| | 7/8 | BKR S - 400 |
| | | |

The NYSE specialist's book is maintained on a CRT and referred to as *display book*. This electronic book sorts all orders coming to the specialist in time and price sequence; it also keeps track of executed orders, so that inquiries from member firms may be quickly researched.

Display book is part of a larger system, known as DOT (*designated order turnaround*). DOT orders are executed by the specialist either against other DOT orders (orders entered by member firms into the DOT system), or against brokers in the "crowd" or against the specialist's own position.

THE AMERICAN STOCK EXCHANGE (AMEX)

The Amex membership is basically like the NYSE's. On the floor are commission house brokers, two-dollar brokers, specialists, and traders. Their functions are very similar to those of their counterparts on the NYSE.

One notable difference from the NYSE is the way the member firms communicate with their employees. Conversations regarding security, shares, price, and the like are carried on through a system of hand signals. The individuals actually discuss quote, size, and other terms without speaking or writing a word.

The Amex trading floor also operates differently than the NYSE. Its procedure for awarding trades is known as *priority prorata*. Under this system, one broker may have priority, as on the NYSE. After priority, however, shares are allocated in round lots among the other participating brokers. Precedence and parity do not play a part in the Amex procedure.

Example: Three brokers enter bids for ABC at 26, as follows:

Broker A: 100 shares, 10:14

Broker B: 200 shares, 10:15

Broker C: 300 shares, 10:15

Broker X enters the crowd with a 400-share sell market order. Broker A executes a trade for 100 shares (priority). Broker B then buys 100 shares, and Broker C takes 200 shares. In other words, the remaining 300 shares are distributed "prorata."