change in price from trade to trade; [5] (2) market depth, which is the maximum price change over a 3000-share sequence of trades; [6] (3) quotation spread, which is the difference between the bid price and the ask price; [7] and (4) specialist capital utilization.[8]

Stocks will be separated into three broad categories: (1) Stocks in the top 200 stocks in the S&P 500 Stock Index and other stocks that are as active; (2) the remaining component stocks of the S&P 500 Index and stocks among the 500 most active stocks on the Exchange; and (3) all other stocks. The following stocks will be excluded from the near neighbor analysis: Foreign stocks, preferred stocks, warrants, when issued stocks, IPOs (for the first 60 days), closed-end funds, stocks selling for $5 and under, stocks with less than 2,000 shares average daily trading volume, stocks with two classes of shares, merger/acquisition stocks if there was a significant impact on the price or volume, and stocks that have been delisted for more than half of the examination period.[9]

Each month, each specialist units' eligible stocks are classified as belonging to one of the three broad categories noted above. A determination is then made for each individual stock (the ''target stock'') as to which other stocks are statistically similar to it (its ''near neighbors''), based on certain market characteristics. The characteristics that are used in this determination are price, non-block volume, daily high low range, and the dollar value of the stock's ''float'' (*i.e.,* shares that are available for trading that are not closely held).[10] A statistical

formula is applied to each stock's four market characteristics to determine its statistical ''distance'' from the target stock. Stocks with distances of 1.000 or less are considered to be ''near neighbors'' of the target stock. Stocks with distances greater than 1.000 are considered to be too different to be considered ''near neighbors'' of the target stock.[11]

For all stocks with three or more near neighbors, a single weighted [12] average performance percentage combining the results for all the near neighbors is calculated for each market quality measure. Then, using statistical techniques involving standard deviations, each target stock's actual performance in the market quality measures listed above is compared to the combined performance of its near neighbors.

When a comparison with its near neighbors is made, the target stock is then placed into one of three groups: a stock whose performance is statistically poorer than the mean performance of the near neighbor stocks is classified in the ''Below Mean'' group; a stock whose performance is statistically similar to the mean performance is classified in the ''Mean'' group; and a stock whose performance is statistically better than the mean is classified in the ''Above Mean'' group. Stocks that have fewer than three near neighbors are automatically classified in the ''Mean'' group. An additional analysis is performed on the stocks in the ''Mean'' group to highlight those stocks that have relatively high performance even though that performance is statistically similar to the calculated average of their near neighbors. A ''Mean'' group stock will be considered to have relatively high performance if its performance percentage is in the top quartile of all stocks in its stock category (*i.e.,* top 200, next 300, or other).

Each specialist unit will receive three reports each month containing the results of the near neighbor analyses for the most recent three-month period. These will include: (1) A Stock Detail Report for each stock that provides market data and performance information about the stock and each of

the other stocks that were identified as its ''near neighbors,'' (2) a Stock Summary Report that lists each stock and provides data on the performance of the target stock and the average performance of its near neighbors, as well as whether the target stock's performance is ''Below Mean,'' ''Mean,'' or ''Above Mean,'' for each performance measure, and (3) a Specialist Unit Summary Report that shows, for each performance measure and within each stock category, the number of stocks that are in each group classification, and the percentage of the unit's total stocks that are in each group classification. The Unit Summary Report also shows the percentage of the unit's ''Mean'' group stocks that had high performance percentages.

The Allocation Committee will receive only the summary data appearing on the Specialist Unit Summary Report, which will be updated each month (covering the three most recent months) upon the distribution of the reports to the specialist units. The Allocation Committee will not receive near neighbor performance data for individual stocks. The Allocation Committee also will receive a list of each unit's stocks that had fewer than three near neighbors and were automatically classified in the ''Mean'' group. Included with each stock will be its percentage of the unit's total dollar value of shares traded.

The Exchange also is modifying the specialist capital utilization performance measure to ensure commonality between it and the near neighbor program as follows: (1) Exclusion of stocks with two classes of shares (*e.g.,* Class A & Class B), ''merger/acquisition'' stocks if there was a significant impact on the price or volume, and stocks that have been delisted for more than half of the examination period; and (2) reduction of the performance review period for measuring capital utilization from a rolling 12 months to a rolling three months.[13]

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder

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[5] Continuity is measured by the percentage of trades with a change of 1/8th point or less from the previous trade.

[6] Depth is measured by the percentage of depth sequences with a high/low range of 1/8 point or less.

[7] Spread is measured by the percentage of reported quotations with a spread of 1/4 point or less.

[8] A capital utilization percentage is derived for each specialist unit by dividing the average daily dollar value of the unit's stabilizing purchases and sales by the average daily total dollar value of shares traded in the unit's stocks. Capital utilization is measured two ways: (1) using stabilizing dealer volume; and (2) using stabilizing plus reliquifying dealer volume.

[9] *See* letter from Daniel Pucker Odell, NYSE, to Katherine Simmons, SEC, dated June 30, 1995 (excluding stocks that have been delisted for more than half the examination.

[10] A stock will be considered ''similar'' to a target stock if: (1) the median average daily price is within 30% of a target stock under $20, or within $6 of a target stock between $20 and $60, or within 10% of a target stock above $60; (2) the median daily non-block volume (*i.e.,* trades under 25,000 shares) is within 30% of the target stock; (3) the median daily high-low range equals the median high-low range of the target stock +/−7.5% of:

i. 30% of the price for a target stock under $20,

ii. $6 for a target stock between $20 and $60,

iii. 10% of the price for a target stock above $60 and (4) the market value of the float is within 30% of the target stock.

[11] If there are more than 20 stocks with distances of 1.000 or less, only the 20 stocks that are closest to the target stock are used in the analysis.

[12] The weight of a near neighbor stock decreases as its distance from the target stock increases. If a stock's distance from the target stock is less than 0.500, then its weight is 1.000. If a stock's distance from the target stock is greater than 0.500, then its weight is less than 1.000.

[13] The Commission also has approved an NYSE proposal to reduce the weight given in the allocation decision making process to the Specialist Performance Evaluation Questionnaire from 1/3 to 1/4 in recognition of the Exchange's adoption for allocation decision purposes of the near neighbor and capital utilization objective measures. *See* Securities Exchange Act Release No. 35932 (June 30, 1995).