Proposed Rule Change by Philadelphia Stock Exchange

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

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Description

Provide a brief description of the proposed rule change (limit 250 characters).

Contact Information

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name: Richard  
Last Name: Rudolph

Title: Vice President and Counsel

E-mail: Richard.Rudolph@phlx.com

Telephone: (215) 496-5074  
Fax: (215) 496-6729

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date: 12/09/2005

By: Richard S. Rudolph  
Vice President and Counsel

Note: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.
<table>
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<tr>
<th><strong>Form 19b-4 Information</strong></th>
<th>The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.</th>
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<tr>
<td><strong>Exhibit 1 - Notice of Proposed Rule Change</strong></td>
<td>The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)</td>
</tr>
<tr>
<td><strong>Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications</strong></td>
<td>Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.</td>
</tr>
<tr>
<td><strong>Exhibit 3 - Form, Report, or Questionnaire</strong></td>
<td>Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.</td>
</tr>
<tr>
<td><strong>Exhibit 4 - Marked Copies</strong></td>
<td>The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.</td>
</tr>
<tr>
<td><strong>Exhibit 5 - Proposed Rule Text</strong></td>
<td>The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.</td>
</tr>
<tr>
<td><strong>Partial Amendment</strong></td>
<td>If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.</td>
</tr>
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</table>
1. **Text of the Proposed Rule Change**

The Philadelphia Stock Exchange, Inc. (“Phlx” or “Exchange”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) \(^1\) and Rule 19b-4 thereunder, \(^2\) proposes to amend Exchange Rule 1080(c)(iv) to provide for automatic executions when the Exchange’s disseminated market is crossed by one minimum trading increment (*i.e.*, $1.05 bid, $1.00 offer or $3.10 bid, $3.00 offer), and the Exchange’s disseminated price is the National Best Bid/Offer (“NBBO”). \(^3\) The Exchange further proposes to amend Rule 1085, Order Protection, to provide a new exception to liability for the satisfaction of trade-throughs under the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (the “Linkage Plan”) when a trade-through was the result of an automatic execution when the Exchange’s disseminated market is the NBBO and is crossed by not more than one minimum trading increment, or crosses the disseminated market of another options exchange by not more than one minimum trading increment.

Additionally, as a housekeeping matter, the proposed rule change would delete Rule 1080(c)(iv)(G), a reference to an obsolete pilot program relating to the disengagement of AUTO-X.

A notice of the proposed rule change for publication in the Federal Register is attached hereto as Exhibit 1. A copy of the amended text of the proposed rule change

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\(^3\) In order for an inbound sell order to be automatically executed, the Exchange must be disseminating the National Best Bid at the time of receipt of the sell order. In order for an inbound buy order to be automatically executed, the Exchange must be disseminating the National Best Offer at the time of receipt of the buy order.
indicating any additions to or deletions from the immediately preceding filing is attached hereto as Exhibit 4. The text of the proposed rule change is set forth below.

Brackets indicate deletions; underlining indicates new text

**Philadelphia Stock Exchange Automated Options Market (AUTOM) and Automatic Execution System (AUTO-X)**

**Rule 1080.** (a) - (b) No change.

(c)*****

(i) - (iii) No change

(iv) Except as otherwise provided in this Rule, in the following circumstances, an order otherwise eligible for automatic execution will instead be manually handled by the specialist:

(A) the Exchange’s disseminated market is crossed by more than one minimum trading increment (as defined in Exchange Rule 1034) (i.e., 2.10 bid, 2 offer), or crosses the disseminated market of another options exchange by more than one minimum trading increment;

(B) - (D) No change.

(E) if the Exchange’s bid or offer is not the NBBO; and

(F) when the price of a limit order is not in the appropriate minimum trading increment pursuant to Rule 1034; [, and

(G) respecting non-Streaming Quote Options, when the number of contracts automatically executed within a 15 second period in an option (subject to a Pilot program through April 30, 2005) exceeds the specified disengagement size, a 30 second period ensues during which subsequent orders are handled manually. If the Exchange's disseminated size exceeds the specified disengagement size and an eligible order is delivered for a number of contracts that is greater than the specified disengagement size, such an order will be automatically executed up to the disseminated size, followed by an AUTO-X disengagement period of 30 seconds. If the specialist revises the quotation in such an option prior to the expiration of such 30-second period, eligible orders in such an option shall again be executed automatically.]

The Exchange’s systems are designed and programmed to identify the conditions that cause inbound orders to be ineligible for automatic execution. Once it is established that inbound orders are ineligible for automatic execution, Exchange staff has the ability to determine which of the above conditions occurred.
Order Protection

Rule 1085. (a) No change.

(b) Exceptions to Trade-Through Liability. The provisions of paragraph (a) pertaining to the satisfaction of Trade-Throughs shall not apply under the following circumstances:

(1) – (7)

(8) in the case of a Trade-Through other than a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange from the Aggrieved Party promptly following the Trade-Through and, in any event, (i) except in the final five minutes of trading, within three minutes from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA, and (ii) in the final five minutes of trading, within one minute from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA; [or]

(9) in the case of a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange promptly following the Trade-Through. In applying this provision, the Aggrieved Party must send the Exchange a Satisfaction Order within three minutes from the time the report of the transaction that constituted the Trade-Through was disseminated over OPRA. To avoid liability for the Trade-Through, the Member receiving such Satisfaction Order must cancel the Satisfaction Order and inform the Aggrieved Party of the identity of the Participant Exchange that initiated the Trade-Through within three minutes of the receipt of such Satisfaction Order (within one minute in the final five minutes of trading). The Aggrieved Party then must send the Participant Exchange that initiated the Trade-Through a Satisfaction Order within three minutes of receipt of the cancellation of the initial Satisfaction Order (within one minute in the final five minutes of trading).[.] or

(10) the Trade-Through was the result of an automatic execution when the Exchange’s disseminated market is the NBBO and is crossed by not more than one minimum trading increment (as defined in Exchange Rule 1034), or crosses the disseminated market of another options exchange by not more than one minimum trading increment.

(c) – (d) No change.

2. Procedures of the Self-Regulatory Organization
The Exchange’s Executive Committee, pursuant to delegated authority, approved the proposal for filing with the Securities and Exchange Commission (“SEC” or “Commission”) on June 30, 2005.

Questions and comments on the proposed rule change may be directed to Richard S. Rudolph, Vice President and Counsel, at (215) 496-5074, or Edith Hallahan, Senior Vice President and Deputy General Counsel, at (215) 496-5179.

3. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

a. Purpose

The purpose of the proposed rule change is to increase the automated handling and execution of option orders on the Exchange by establishing that orders are eligible for automatic execution during crossed markets when such markets are crossed by one minimum trading increment.4 The purpose of this Amendment No. 1 is to establish an exception from trade-through and satisfaction liability when such a transaction occurs.

Currently, Exchange Rule 1080(c)(iv)(A) states that an order otherwise eligible for automatic execution will instead be manually handled by the specialist when the Exchange’s disseminated market is crossed or crosses the disseminated market of another options exchange.5 The proposed rule change would limit the specialist’s manual handling of orders during crossed markets to situations where the market is crossed by more than one minimum trading increment (i.e., 2.10 bid, 2 offer). The proposed rule

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4 Exchange Rule 1034, Minimum Increments, currently provides that all options on stocks, index options, and Exchange Traded Options quoting in decimals at $3.00 or higher shall have a minimum increment of $.10, and all options on stocks and index options quoting in decimals under $3.00 shall have a minimum increment of $.05.

would provide that an order otherwise eligible for automatic execution would instead be handled manually by the specialist when the Exchange’s disseminated market is crossed by more than one minimum trading increment, or crosses the disseminated market of another options exchange by more than one minimum trading increment.

Thus, the effect of the proposal is that orders would be eligible for automatic execution when the Exchange’s disseminated market is crossed or crosses another exchange’s market by just one minimum trading increment (and where the Exchange’s disseminated market is the NBBO). 6

The Exchange believes that establishing a limitation of one minimum trading increment as the amount by which a market may be crossed in order to provide automatic executions during crossed markets should provide Exchange specialists and Registered Options Traders (“ROTs”) with sufficient ability to manage their market risk during times of crossed markets. The Exchange believes that a market that is crossed by an amount greater than one minimum trading increment is an indication that one or more options market(s) or market makers may be experiencing quotation system issues that do not reflect current market conditions, and thus orders on the Exchange would be handled manually by the specialist in such circumstances.

On the other hand, the Exchange believes that markets that are crossed by only one single minimum trading increment in today’s increasingly electronic marketplace reflect the number and speed of electronic quotations and the number of market makers

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6 Orders otherwise eligible for automatic execution will instead be handled manually by the specialist when the Exchange’s disseminated market is not the NBBO. See Exchange Rule 1080(c)(iv)(E). Therefore, for an order to be eligible for automatic execution during a crossed market, the Exchange’s disseminated market must be the NBBO.
submitting such quotations, and therefore do not necessarily indicate system errors that
may result in unusual risk to market makers.

The Exchange also proposes to amend Rule 1085, Order Protection, to add a new
exception to Trade-Through\(^7\) satisfaction liability when the Trade-Through was the result
of an automatic execution when the Exchange’s disseminated market is the NBBO and is
crossed by not more than one minimum trading increment (as defined in Exchange Rule
1034), or crosses the disseminated market of another options exchange by not more than
one minimum trading increment. The Exchange believes that, while the proposed rule
change might result in trade-throughs, it would ultimately benefit customers. Customers,
who would receive automatic executions and instant reports of such transactions, would
be able to rely on firm quotations disseminated by Exchange specialists and Registered
Options Traders (“ROTs”). The Exchange further believes that the proposed rule change
would assist specialists in fulfilling their obligations under Exchange and Commission
rules concerning firm quotations.\(^8\)

Finally, as a housekeeping matter, the Exchange proposes to delete Rule
1080(c)(iv)(G), a reference to an expired pilot program relating to the disengagement of
AUTO-X for “non-Streaming Quote Options.”\(^9\) There are no longer any non-Streaming

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\(^7\) “Trade-Through” means a transaction in an options series at a price that is inferior to the NBBO, but shall
not include a transaction that occurs at a price that is one minimum quoting increment inferior to the NBBO
provided a Linkage Order is contemporaneously sent to each Participant Exchange disseminating the
NBBO for the full size of the Participant Exchange’s bid (offer) that represents the NBBO. See Exchange
Rule 1083(t). When a trade-through occurs, a party traded-through may send a “Satisfaction Order”
through the Linkage to notify a member of another exchange of the trade-through and to seek satisfaction
of the liability arising from the trade-through. See Exchange Rule 1083(k)(iii).

\(^8\) See, e.g., Exchange Rule 1082. See also, Rule 11Ac1-1 under the Act, 17 CFR 240.11Ac1-1.

\(^9\) A “non-Streaming Quote Option” was previously defined as an option that is not traded on the
Exchange are now traded on Phlx XL.
Quote Options traded on the Exchange; therefore Rule 1080(c)(iv)(G) is no longer applicable.

b. **Statutory Basis**

The Exchange believes that its proposal is consistent with Section 6(b) of the Act in general, and furthers the objectives of Section 6(b)(5) of the Act in particular, in that it is designed to perfect the mechanisms of a free and open market and the national market system, protect investors and the public interest and promote just and equitable principles of trade, by establishing conditions under which the Exchange will provide automatic executions during times of crossed markets, thus increasing the number of orders that are handled electronically on the Exchange.

4. **Self-Regulatory Organization’s Statement on Burden on Competition**

The Phlx does not believe that the proposed rule change will impose any inappropriate burden on competition.

5. **Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

No written comments were either solicited or received.

6. **Extension of Time Period for Commission Action**

The Exchange does not consent to an extension of the time period for Commission action.

7. **Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)**

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The Exchange requests accelerated effectiveness pursuant to Section 19(b)(2) of the Act in order to establish rules that would increase the number of orders and contracts handled and executed electronically on the Exchange.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

The proposed rule change is not based on the rules of another self-regulatory organization or of the Commission.

9. Exhibits

   1. Notice of proposed rule for publication in the Federal Register.

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SECURITIES AND EXCHANGE COMMISSION  
(Release No.                  ; File No. SR-Phlx-2005-45)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the  
Philadelphia Stock Exchange, Inc. Relating to the Automatic Execution of Option  
Transactions During Crossed Markets

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")\(^1\), and  
Rule 19b-4\(^2\) thereunder, notice is hereby given that on ______________________ 2005,  
the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities  
and Exchange Commission ("SEC" or "Commission") the proposed rule change as  
described in Items I, II, and III, below, which Items have been prepared by the Phlx. The  
Commission is publishing this notice to solicit comments on the proposed rule change  
from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the  
Proposed Rule Change

The Phlx, pursuant to Section 19(b)(1) and Rule 19b-4 thereunder,\(^3\) proposes to  
amend Exchange Rule 1080(c)(iv) to provide for automatic executions when the  
Exchange’s disseminated market is crossed by one minimum trading increment (i.e.,  
$1.05 bid, $1.00 offer or $3.10 bid, $3.00 offer), and the Exchange’s disseminated price  
is the National Best Bid/Offer ("NBBO").\(^4\) The Exchange further proposes to amend

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\(^3\) 17 CFR 240.19b-4.

\(^4\) In order for an inbound sell order to be automatically executed, the Exchange must be disseminating the National Best Bid at the time of receipt of the sell order. In order for an inbound buy order to be automatically executed, the Exchange must be disseminating the National Best Offer at the time of receipt of the buy order.
Rule 1085, Order Protection, to provide a new exception to liability for the satisfaction of trade-throughs under the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (the “Linkage Plan”) when a trade-through was the result of an automatic execution when the Exchange’s disseminated market is the NBBO and is crossed by not more than one minimum trading increment, or crosses the disseminated market of another options exchange by not more than one minimum trading increment.

Additionally, as a housekeeping matter, the proposed rule change would delete Rule 1080(c)(iv)(G), a reference to an obsolete pilot program relating to the disengagement of AUTO-X.

The text of the proposed rule change is set forth below.

Brackets indicate deletions; underlining indicates new text

**Philadelphia Stock Exchange Automated Options Market (AUTOM) and Automatic Execution System (AUTO-X)**

**Rule 1080.** (a) - (b) No change.

(c)*****

(i) - (iii) No change

(iv) Except as otherwise provided in this Rule, in the following circumstances, an order otherwise eligible for automatic execution will instead be manually handled by the specialist:

(A) the Exchange’s disseminated market is crossed by more than one minimum trading increment (as defined in Exchange Rule 1034) (i.e., 2.10 bid, 2 offer), or crosses the disseminated market of another options exchange by more than one minimum trading increment:

(B) - (D) No change.

(E) if the Exchange’s bid or offer is not the NBBO; and
(F) when the price of a limit order is not in the appropriate minimum trading increment pursuant to Rule 1034; and

(G) respecting non-Streaming Quote Options, when the number of contracts automatically executed within a 15 second period in an option (subject to a Pilot program through April 30, 2005) exceeds the specified disengagement size, a 30 second period ensues during which subsequent orders are handled manually. If the Exchange’s disseminated size exceeds the specified disengagement size and an eligible order is delivered for a number of contracts that is greater than the specified disengagement size, such an order will be automatically executed up to the disseminated size, followed by an AUTO-X disengagement period of 30 seconds. If the specialist revises the quotation in such an option prior to the expiration of such 30-second period, eligible orders in such an option shall again be executed automatically.]

The Exchange’s systems are designed and programmed to identify the conditions that cause inbound orders to be ineligible for automatic execution. Once it is established that inbound orders are ineligible for automatic execution, Exchange staff has the ability to determine which of the above conditions occurred.

Order Protection

Rule 1085. (a) No change.

(b) Exceptions to Trade-Through Liability. The provisions of paragraph (a) pertaining to the satisfaction of Trade-Throughs shall not apply under the following circumstances:

(1) – (7)

(8) in the case of a Trade-Through other than a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange from the Aggrieved Party promptly following the Trade-Through and, in any event, (i) except in the final five minutes of trading, within three minutes from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA, and (ii) in the final five minutes of trading, within one minute from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA; [or]

(9) in the case of a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange promptly following the Trade-Through. In applying this provision, the Aggrieved Party must send the Exchange a Satisfaction Order within three minutes from the time the report of the transaction that constituted the Trade-Through was disseminated over OPRA. To avoid liability for the Trade-Through, the Member receiving such Satisfaction Order must cancel the Satisfaction Order and inform the Aggrieved Party of the identity of the Participant Exchange that initiated the Trade-Through within three minutes of the
receipt of such Satisfaction Order (within one minute in the final five minutes of trading). The Aggrieved Party then must send the Participant Exchange that initiated the Trade-Through a Satisfaction Order within three minutes of receipt of the cancellation of the initial Satisfaction Order (within one minute in the final five minutes of trading).

(10) the Trade-Through was the result of an automatic execution when the Exchange’s disseminated market is the NBBO and is crossed by not more than one minimum trading increment (as defined in Exchange Rule 1034), or crosses the disseminated market of another options exchange by not more than one minimum trading increment.

(c) – (d) No change.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Phlx included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Phlx has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of the proposed rule change is to increase the automated handling and execution of option orders on the Exchange by establishing that orders are eligible for automatic execution during crossed markets when such markets are crossed by one minimum trading increment.\(^5\) The purpose of this Amendment No. 1 is to establish an exception from trade-through and satisfaction liability when such a transaction occurs.

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\(^5\) Exchange Rule 1034, Minimum Increments, currently provides that all options on stocks, index options, and Exchange Traded Options quoting in decimals at $3.00 or higher shall have a minimum increment of $.10, and all options on stocks and index options quoting in decimals under $3.00 shall have a minimum increment of $.05.
Currently, Exchange Rule 1080(c)(iv)(A) states that an order otherwise eligible for automatic execution will instead be manually handled by the specialist when the Exchange’s disseminated market is crossed or crosses the disseminated market of another options exchange.\(^6\) The proposed rule change would limit the specialist’s manual handling of orders during crossed markets to situations where the market is crossed by more than one minimum trading increment (i.e., 2.10 bid, 2 offer). The proposed rule would provide that an order otherwise eligible for automatic execution would instead be handled manually by the specialist when the Exchange’s disseminated market is crossed by more than one minimum trading increment, or crosses the disseminated market of another options exchange by more than one minimum trading increment.

Thus, the effect of the proposal is that orders would be eligible for automatic execution when the Exchange’s disseminated market is crossed or crosses another exchange’s market by just one minimum trading increment (and where the Exchange’s disseminated market is the NBBO).\(^7\)

The Exchange believes that establishing a limitation of one minimum trading increment as the amount by which a market may be crossed in order to provide automatic executions during crossed markets should provide Exchange specialists and Registered Options Traders (“ROTs”) with sufficient ability to manage their market risk during times of crossed markets. The Exchange believes that a market that is crossed by an

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\(^7\) Orders otherwise eligible for automatic execution will instead be handled manually by the specialist when the Exchange’s disseminated market is not the NBBO. \textit{See} Exchange Rule 1080(c)(iv)(E). Therefore, for an order to be eligible for automatic execution during a crossed market, the Exchange’s disseminated market must be the NBBO.
amount greater than one minimum trading increment is an indication that one or more options market(s) or market makers may be experiencing quotation system issues that do not reflect current market conditions, and thus orders on the Exchange would be handled manually by the specialist in such circumstances.

On the other hand, the Exchange believes that markets that are crossed by only one single minimum trading increment in today’s increasingly electronic marketplace reflect the number and speed of electronic quotations and the number of market makers submitting such quotations, and therefore do not necessarily indicate system errors that may result in unusual risk to market makers.

The Exchange also proposes to amend Rule 1085, Order Protection, to add a new exception to Trade-Through\(^8\) satisfaction liability when the Trade-Through was the result of an automatic execution when the Exchange’s disseminated market is the NBBO and is crossed by not more than one minimum trading increment (as defined in Exchange Rule 1034), or crosses the disseminated market of another options exchange by not more than one minimum trading increment. The Exchange believes that, while the proposed rule change might result in trade-throughs, it would ultimately benefit customers. Customers, who would receive automatic executions and instant reports of such transactions, would be able to rely on firm quotations disseminated by Exchange specialists and Registered Options Traders (“ROTs”). The Exchange further believes that the proposed rule change

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\(^8\) “Trade-Through” means a transaction in an options series at a price that is inferior to the NBBO, but shall not include a transaction that occurs at a price that is one minimum quoting increment inferior to the NBBO provided a Linkage Order is contemporaneously sent to each Participant Exchange disseminating the NBBO for the full size of the Participant Exchange’s bid (offer) that represents the NBBO. See Exchange Rule 1083(t). When a trade-through occurs, a party traded-through may send a “Satisfaction Order” through the Linkage to notify a member of another exchange of the trade-through and to seek satisfaction of the liability arising from the trade-through. See Exchange Rule 1083(k)(iii).
would assist specialists in fulfilling their obligations under Exchange and Commission rules concerning firm quotations.  

Finally, as a housekeeping matter, the Exchange proposes to delete Rule 1080(c)(iv)(G), a reference to an expired pilot program relating to the disengagement of AUTO-X for “non-Streaming Quote Options.” 10 There are no longer any non-Streaming Quote Options traded on the Exchange; therefore Rule 1080(c)(iv)(G) is no longer applicable.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act 11 in general, and furthers the objectives of Section 6(b)(5) of the Act 12 in particular, in that it is designed to perfect the mechanisms of a free and open market and the national market system, protect investors and the public interest and promote just and equitable principles of trade, by establishing conditions under which the Exchange will provide automatic executions during times of crossed markets, thus increasing the number of orders that are handled electronically on the Exchange.

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9 See, e.g., Exchange Rule 1082. See also, Rule 11Ac1-1 under the Act, 17 CFR 240.11Ac1-1.


B. **Self-Regulatory Organization's Statement on Burden on Competition**

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

C. **Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

No written comments were either solicited or received.

III. **Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

The Exchange requests accelerated effectiveness pursuant to Section 19(b)(2) of the Act\(^{13}\) in order to establish rules that would increase the number of orders and contracts handled and executed electronically on the Exchange.

IV. **Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

**Electronic comments:**

- Use the Commission’s Internet comment form \(\text{http://www.sec.gov/rules/sro.shtml}\); or

- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-Phlx-2005-45 on the subject line.

**Paper comments:**

• Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-Phlx-2005-45. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission’s Internet Web site (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission’s Public Reference Room. Copies of the filing also will be available for inspection and copying at the principal office of the Phlx.

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-Phlx-2005-45 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority. ¹⁴

Margaret H. McFarland
Deputy Secretary

Exhibit 4

Brackets indicate deletions; underlining indicates new text; bold indicates additional text submitted since the immediately preceding filing

Philadelphia Stock Exchange Automated Options Market (AUTOM) and Automatic Execution System (AUTO-X)

Rule 1080. (a) - (b) No change.

(c)****

(i) - (iii) No change.

(iv) Except as otherwise provided in this Rule, in the following circumstances, an order otherwise eligible for automatic execution will instead be manually handled by the specialist:

(A) the Exchange’s disseminated market is crossed by more than one minimum trading increment (as defined in Exchange Rule 1034) (i.e., 2.10 bid, 2 offer), or crosses the disseminated market of another options exchange by more than one minimum trading increment;

(B) - (D) No change.

(E) if the Exchange’s bid or offer is not the NBBO; and

(F) when the price of a limit order is not in the appropriate minimum trading increment pursuant to Rule 1034; [, and

(G) respecting non-Streaming Quote Options, when the number of contracts automatically executed within a 15 second period in an option (subject to a Pilot program through April 30, 2005) exceeds the specified disengagement size, a 30 second period ensues during which subsequent orders are handled manually. If the Exchange’s disseminated size exceeds the specified disengagement size and an eligible order is delivered for a number of contracts that is greater than the specified disengagement size, such an order will be automatically executed up to the disseminated size, followed by an AUTO-X disengagement period of 30 seconds. If the specialist revises the quotation in such an option prior to the expiration of such 30-second period, eligible orders in such an option shall again be executed automatically.]

The Exchange’s systems are designed and programmed to identify the conditions that cause inbound orders to be ineligible for automatic execution. Once it is established that inbound orders are ineligible for automatic execution, Exchange staff has the ability to determine which of the above conditions occurred.
Order Protection

Rule 1085. (a) No change.

(b) Exceptions to Trade-Through Liability. The provisions of paragraph (a) pertaining to the satisfaction of Trade-Throughs shall not apply under the following circumstances:

(1) – (7)

(8) in the case of a Trade-Through other than a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange from the Aggrieved Party promptly following the Trade-Through and, in any event, (i) except in the final five minutes of trading, within three minutes from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA, and (ii) in the final five minutes of trading, within one minute from the time the report of the transaction(s) that constituted the Trade-Through was disseminated over OPRA; [or]

(9) in the case of a Third Participating Market Center Trade-Through, a Satisfaction Order with respect to the Trade-Through was not received by the Exchange promptly following the Trade-Through. In applying this provision, the Aggrieved Party must send the Exchange a Satisfaction Order within three minutes from the time the report of the transaction that constituted the Trade-Through was disseminated over OPRA. To avoid liability for the Trade-Through, the Member receiving such Satisfaction Order must cancel the Satisfaction Order and inform the Aggrieved Party of the identity of the Participant Exchange that initiated the Trade-Through within three minutes of the receipt of such Satisfaction Order (within one minute in the final five minutes of trading). The Aggrieved Party then must send the Participant Exchange that initiated the Trade-Through a Satisfaction Order within three minutes of receipt of the cancellation of the initial Satisfaction Order (within one minute in the final five minutes of trading).[.]. or

(10) the Trade-Through was the result of an automatic execution when the Exchange's disseminated market is the NBBO and is crossed by not more than one minimum trading increment (as defined in Exchange Rule 1034), or crosses the disseminated market of another options exchange by not more than one minimum trading increment.

(c) – (d) No change.