Proposed Rule Change by Philadelphia Stock Exchange

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

Initial Amendment Withdrawal

Section 19(b)(2) ✔ Section 19(b)(3)(A) Section 19(b)(3)(B)

Pilot

Extension of Time Period for Commission Action

Date Expires

Description

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

Proposed rule change relating to quoting obligations for Directed Streaming Quote Traders and Directed Remote Streaming Quote Traders.

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 02/03/2006

By Richard S. Rudolph Vice President and Counsel

(Name) (Title)

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.
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.
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") and Rule 19b-4 thereunder, proposes to amend Exchange Rule 1014(b)(ii)(D) and Rule 1017(b)(ii) that would: (1) delete the requirement that Streaming Quote Traders ("SQTs") and Remote Streaming Quote Traders ("RSQTs") submit continuous electronic quotations in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders; (2) establish a new quoting obligation for SQTs and RSQTs that receive Directed Orders; and, as a result of these changes, (3) establish that, if the specialist is not quoting at the opening, the system will nonetheless open a series when any two Phlx XL participants are quoting in such series within two minutes of the opening of the underlying security on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular), or when one Phlx XL participant is quoting in such series thereafter. The text of the proposed rule change is set forth below.

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3 An SQT is an ROT who has received permission from the Exchange to generate and submit option quotations electronically through AUTOM in eligible options to which such SQT is assigned. An SQT may only submit such quotations while such SQT is physically present on the floor of the Exchange. *See* Exchange Rule 1014(b)(ii)(A).

4 An RSQT is an ROT that is a member or member organization with no physical trading floor presence who has received permission from the Exchange to generate and submit option quotations electronically through AUTOM in eligible options to which such RSQT has been assigned. An RSQT may only submit such quotations electronically from off the floor of the Exchange. *See* Exchange Rule 1014(b)(ii)(B).

5 The term “Directed Order” means any customer order to buy or sell which has been directed to a particular specialist, RSQT, or SQT by an Order Flow Provider, as defined below. To qualify as a Directed Order, an order must be delivered to the Exchange via AUTOM. *See* Exchange Rule 1080(l)(i)(A). The term “Order Flow Provider” ("OFP") means any member or member organization that submits, as agent, customer orders to the Exchange. *See* Exchange Rule 1080(l)(i)(B).
A notice of the proposed rule change for publication in the Federal Register is attached hereto as Exhibit 1.

Brackets indicate deletions; underlining indicates new text.

**Obligations and Restrictions Applicable to Specialists and Registered Options Traders**

**Rule 1014.** (a) No change.

(b) ROT. (i) No change.

(ii) (A) – (C) No change.

(D) Market Making Obligations Applicable in Streaming Quote Options.

(1) In addition to the other requirements for ROTs set forth in this Rule 1014, an SQT and an RSQT shall be responsible to quote continuous, two-sided markets in not less than 60% of the series in each Streaming Quote Option (as defined in Rule 1080(k)) in which such SQT or RSQT is assigned, provided that, on any given day, a Directed SQT (“DSQT”) or a Directed RSQT (“DRSQT”) (as defined in Rule 1080(l)(i)(C)) shall be responsible to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange in at least 60% of the options in which such DSQT or DRSQT is assigned. Whenever a DSQT or DRSQT enters a quotation in an option in which such DSQT or DRSQT is assigned, such DSQT or DRSQT must maintain continuous quotations for all series of the option listed on the Exchange until the close of that trading day.

[<a Directed SQT or RSQT (as defined in Rule 1080(l)(i)(C)) shall be responsible to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders (as defined in Rule 1080(l)(i)(A))].

(2) The specialist shall be responsible to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which such specialist is assigned.

(3) [(1) During a six month period commencing on the date of the initial deployment of Phlx XL (the "initial six-month period"), any SQT or RSQT assigned in a Streaming Quote Option (and the specialist assigned in such Streaming Quote Option) may
submit electronic quotations with a size of fewer than 10 contracts for a period of sixty days after such option begins trading as a Streaming Quote Option. Beginning on the sixty-first day after such option begins trading as a Streaming Quote Option, SQTs, RSQTs and the specialist assigned in such Streaming Quote Option shall submit electronic quotations with a size of not less than 10 contracts.

(2) During a six month period commencing on the first day following the expiration of the initial six-month period, any SQT or RSQT assigned in a Streaming Quote Option (and the specialist assigned in such Streaming Quote Option) may submit electronic quotations with a size of fewer than 10 contracts for a period of thirty days after such option begins trading as a Streaming Quote Option. Beginning on the thirty-first day after such option begins trading as a Streaming Quote Option, SQTs, RSQTs and the specialist assigned in such Streaming Quote Option shall submit electronic quotations with a size of not less than 10 contracts.

(3) Thereafter, any SQT or RSQT assigned in a Streaming Quote Option that is newly deployed on Phlx XL (and the specialist assigned in such Streaming Quote Option) shall submit electronic quotations with a size of not less than 10 contracts beginning on the date on which such Streaming Quote Option begins trading on Phlx XL.]

(E) No change.

(c) – (h) No change.

Commentary: No change.

**Openings In Options**

Rule 1017. (a) No change.

(b) The system will calculate an Anticipated Opening Price (“AOP”) and Anticipated Opening Size (“AOS”) when a quote or trade has been disseminated by the primary market for the underlying security, and under the conditions set forth below. The specialist assigned in the particular option must enter opening quotes not later than one minute following the dissemination of a quote or trade by the primary market for the underlying security. An AOP may only be calculated if: (i) the Exchange has received market orders, or the book is crossed (highest bid is higher than the lowest offer) or locked (highest bid equals the lowest offer); and (ii) either (A) the specialist’s quote has been submitted; (B) the quotes of at least two Phlx XL participants [that are required to submit continuous, two-sided quotes in 99% of the series in all option issues in which such Phlx XL participant is assigned (“99% participants”),] have been submitted within
two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular); or (C) if neither the specialist’s quote nor the quotes of two [99%] Phlx XL participants have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange circular), one [99%] Phlx XL participant has submitted their quote. A Phlx XL participant that submits a quote pursuant to this Rule 1017(b) in any series when the specialist’s quote has not been submitted shall be required to submit continuous, two-sided quotes in such series until such time as the specialist submits his/her quote, after which the Phlx XL participant that submitted such quote shall be obligated to submit quotations pursuant to Rule 1014(b)(ii)(D).

In situations where an AOP may be calculated and there is an order/quote imbalance, the system will immediately send an imbalance notice indicating the imbalance side (buy or sell) and the AOP and AOS (an “Imbalance Notice”) to Phlx XL participants provided that the primary market for the underlying security has disseminated the opening quote or trade. Phlx XL participants that have not submitted opening quotes will then submit their opening quotes, and Phlx XL participants that have submitted opening quotes may submit revised opening quotes; thereafter the system will disseminate an updated Imbalance Notice every five seconds (or such shorter period as determined by the Options Committee and disseminated to membership via Exchange Circular) until the series is open. If no imbalance exists, no Imbalance Notice will be sent, and the system will establish an opening price as described in paragraph (c) below.

(c) – (d) No change.

(e) The system will not open a series if one of the following conditions is met:

   (i) there is no quote from the specialist or [a 99%] Phlx XL participants, as described in Rule 1017(b)(ii)(B) and (C) above;

   (ii) – (iii) No change.

(f) – (j) No change.

Commentary: 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 February 3, 2006.
Questions and comments on the proposed rule change may be directed to Richard S. Rudolph, Vice President and Counsel, 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 encourage Directed Orders by establishing a new quoting obligation for Directed SQTs (“DSQTs”) and Directed RSQTs (“DRSQTs”)⁶ that would require them to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange in at least 60% of the options in which such DSQT or DRSQT is assigned. The proposed rule change is similar to the quoting obligation for participants that receive Directed Orders on other exchanges.⁷

   **Deletion of 99% Quoting Requirement for Directed SQTs/RSQTs**

   Currently, Rule 1014(b)(ii)(D) requires DSQTs and DRSQTs to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders. For competitive reasons, the proposed rule change would delete the 99% quoting requirement applicable to DSQTs and DRSQTs. Instead, DSQTs and DRSQTs, would be obligated to submit quotations under proposed Exchange

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⁶ The term “Directed Specialist, RSQT, or SQT” means a specialist, RSQT, or SQT that receives a Directed Order. See Exchange Rule 1080(l)(i)(C).

⁷ The Exchange notes that the International Securities Exchange, Inc. (“ISE”) currently has rules in effect concerning “Preferred Orders” that are virtually identical to the Exchange’s rules concerning Directed Orders (See ISE Rule 713, Supplementary Material .03). The quoting obligation applicable to ISE Competitive Market Makers, including those that receive “Preferred Orders” is contained in ISE Rule 804(e)(2). See also, Securities Exchange Act Release No. 51818 (June 10, 2005), 70 FR 35146 (June 16, 2005) (SR-ISE-2005-18). The instant proposed rule change, which tracks ISE Rule 804, is intended to enable the Exchange to compete for Directed Orders by establishing a quoting obligation for Directed SQTs and RSQTs that is virtually identical to the quoting obligation applicable to ISE Competitive Market Makers that receive “Preferred Orders.”
Rule 1014(b)(ii)(D)(1), described below. This obligation would be similar to that of other exchanges with Directed or Preferenced Order flow programs. The Exchange is now concerned that the current 99% quoting obligation is impeding Directed Order flow to the Exchange.

**New Quoting Obligation for DSQTs and DRSQTs**

The proposed rule change would provide that, on any given day, a DSQT or a DRSQT would be responsible to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange of at least 60% of the options in which such DSQT or DRSQT is assigned. The Exchange believes that this new quoting obligation for DSQTs and DRSQTs should encourage member organizations to send Directed Orders to DSQTs and DRSQTs on the Exchange.

In order to ensure continuity of quoting, the proposed rule change would provide that, whenever a DSQT or DRSQT enters a quotation in an option in which such DSQT or DRSQT is assigned, such DSQT or DRSQT must maintain continuous quotations for all series of the option listed on the Exchange until the close of that trading day. The Exchange believes that this should promote liquidity on the Exchange.

**Amendments to Rule 1017, Openings in Options**

Currently, Rule 1017(b) provides that a series may open when: (i) the Exchange has received market orders, or the book is crossed (highest bid is higher than the lowest offer) or locked (highest bid equals the lowest offer); and (ii) either (A) the specialist’s quote has been submitted; (B) the quotes of at least two Phlx XL participants that have the 99% quoting obligation (“99% participants”) have been submitted within two minutes.

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of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular); or (C) if neither the specialist’s quote nor the quotes of two 99% participants have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular), one 99% participant has submitted their quote.

The proposal would establish that if the specialist is not quoting at the opening, the system will open a series when any two Phlx XL participants are quoting within two minutes of the opening on the primary market for the underlying security, or when any single Phlx XL participant has submitted his/her quote thereafter, thus eliminating the requirement that such Phlx XL participants must be 99% participants in order for the series to open.

In order to ensure the continuity of quotations in series that are opened when the specialist has not submitted his or her quotation, the proposed rule change would provide that a Phlx XL participant that submits a quote pursuant to the proposed rule in any series when the specialist’s quote has not been submitted would be required to submit continuous, two-sided quotes in such series until such time as the specialist submits his/her quote, after which the Phlx XL participant that submitted such quote would be obligated to submit quotations as described above under proposed Rule 1014(b)(ii)(D).

b. **Statutory Basis**
The Exchange believes that its proposal is consistent with Section 6(b) of the Act\textsuperscript{9} in general, and furthers the objectives of Section 6(b)(5) of the Act\textsuperscript{10} in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, by enabling the Exchange to compete for order flow in Directed Orders by establishing a new quoting obligation applicable to DSQTs and DRSQTs.

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

   The Phlx 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.

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)(A) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)**

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\textsuperscript{9} 15 U.S.C. 78f(b).

\textsuperscript{10} 15 U.S.C. 78f(b)(5).
The Exchange requests accelerated effectiveness pursuant to Section 19(b)(2) of the Act\(^\text{11}\) in order to compete with other exchanges that have similar rules in effect, as cited below.

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

   The proposed rule change is based, in part, on ISE Rules 713, Supplementary Material .03, and 804(e)(2).\(^\text{12}\)

9. **Exhibits**

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

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Exhibit 1

SECURITIES AND EXCHANGE COMMISSION
(Release No.                  ; File No. SR-Phlx-2006-11)

Self-Regulatory Organizations; Notice of Filing and Accelerated Approval of Proposed
Rule Change by the Philadelphia Stock Exchange, Inc. Relating to Quoting Obligations
for Directed Streaming Quote Traders and Directed Remote Streaming Quote Traders

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 ______________________ 2006,
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) of the Act\(^3\) and Rule 19b-4 thereunder,\(^4\)
proposes to amend Exchange Rule 1014(b)(ii)(D) and Rule 1017(b)(ii) that would: (1)
delete the requirement that Streaming Quote Traders (“SQTs”)\(^5\) and Remote Streaming

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\(^5\) An SQT is an ROT who has received permission from the Exchange to generate and submit option
quotations electronically through AUTOM in eligible options to which such SQT is assigned. An SQT may
only submit such quotations while such SQT is physically present on the floor of the Exchange. See
Exchange Rule 1014(b)(ii)(A).
Quote Traders ("RSQTs")\(^6\) submit continuous electronic quotations in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders;\(^7\) (2) establish a new quoting obligation for SQTs and RSQTs that receive Directed Orders; and, as a result of these changes, (3) establish that, if the specialist is not quoting at the opening, the system will nonetheless open a series when any two Phlx XL participants are quoting in such series within two minutes of the opening of the underlying security on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular), or when one Phlx XL participant is quoting in such series thereafter. The text of the proposed rule change is set forth below.

Brackets indicate deletions; underlining indicates new text.

**Obligations and Restrictions Applicable to Specialists and Registered Options Traders**

**Rule 1014.** (a) No change.

(b) ROT. (i) No change.

(ii) (A) – (C) No change.

(D) Market Making Obligations Applicable in Streaming Quote Options.

(1) In addition to the other requirements for ROTs set forth in this Rule 1014, an SQT and an RSQT shall be responsible to quote continuous, two-sided markets in not less than 60% of the

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\(^6\) An RSQT is an ROT that is a member or member organization with no physical trading floor presence who has received permission from the Exchange to generate and submit option quotations electronically through AUTOM in eligible options to which such RSQT has been assigned. An RSQT may only submit such quotations electronically from off the floor of the Exchange. See Exchange Rule 1014(b)(ii)(B).

\(^7\) The term “Directed Order” means any customer order to buy or sell which has been directed to a particular specialist, RSQT, or SQT by an Order Flow Provider, as defined below. To qualify as a Directed Order, an order must be delivered to the Exchange via AUTOM. See Exchange Rule 1080(l)(i)(A). The term “Order Flow Provider” (“OFP”) means any member or member organization that submits, as agent, customer orders to the Exchange. See Exchange Rule 1080(l)(i)(B).
series in each Streaming Quote Option (as defined in Rule 1080(k)) in which such SQT or RSQT is assigned, provided that, on any given day, a Directed SQT (“DSQT”) or a Directed RSQT (“DRSQT”) (as defined in Rule 1080(l)(i)(C)) shall be responsible to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange in at least 60% of the options in which such DSQT or DRSQT is assigned. Whenever a DSQT or DRSQT enters a quotation in an option in which such DSQT or DRSQT is assigned, such DSQT or DRSQT must maintain continuous quotations for all series of the option listed on the Exchange until the close of that trading day.

[a Directed SQT or RSQT (as defined in Rule 1080(l)(i)(C)) shall be responsible to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders (as defined in Rule 1080(l)(i)(A))].

(2) The specialist shall be responsible to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which such specialist is assigned.

(3) [(1) During a six month period commencing on the date of the initial deployment of Phlx XL (the "initial six-month period"), any SQT or RSQT assigned in a Streaming Quote Option (and the specialist assigned in such Streaming Quote Option) may submit electronic quotations with a size of fewer than 10 contracts for a period of sixty days after such option begins trading as a Streaming Quote Option. Beginning on the sixty-first day after such option begins trading as a Streaming Quote Option, ] SQTs, RSQTs and the specialist assigned in such Streaming Quote Option shall submit electronic quotations with a size of not less than 10 contracts.

[(2) During a six month period commencing on the first day following the expiration of the initial six-month period, any SQT or RSQT assigned in a Streaming Quote Option (and the specialist assigned in such Streaming Quote Option) may submit electronic quotations with a size of fewer than 10 contracts for a period of thirty days after such option begins trading as a Streaming Quote Option. Beginning on the thirty-first day after such option begins trading as a Streaming Quote Option, SQTs, RSQTs and the specialist assigned in such Streaming Quote Option shall submit electronic quotations with a size of not less than 10 contracts.]
(3) Thereafter, any SQT or RSQT assigned in a Streaming Quote Option that is newly deployed on Phlx XL (and the specialist assigned in such Streaming Quote Option) shall submit electronic quotations with a size of not less than 10 contracts beginning on the date on which such Streaming Quote Option begins trading on Phlx XL.]

(E) No change.

(c) – (h) No change.

Commentary: No change.

**Openings In Options**

**Rule 1017.** (a) No change.

(b) The system will calculate an Anticipated Opening Price (“AOP”) and Anticipated Opening Size (“AOS”) when a quote or trade has been disseminated by the primary market for the underlying security, and under the conditions set forth below. The specialist assigned in the particular option must enter opening quotes not later than one minute following the dissemination of a quote or trade by the primary market for the underlying security. An AOP may only be calculated if: (i) the Exchange has received market orders, or the book is crossed (highest bid is higher than the lowest offer) or locked (highest bid equals the lowest offer); and (ii) either (A) the specialist’s quote has been submitted; (B) the quotes of at least two Phlx XL participants [that are required to submit continuous, two-sided quotes in 99% of the series in all option issues in which such Phlx XL participant is assigned (“99% participants”),] have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular); or (C) if neither the specialist’s quote nor the quotes of two [99%] Phlx XL participants have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange circular), one [99%] Phlx XL participant has submitted their quote. A Phlx XL participant that submits a quote pursuant to this Rule 1017(b) in any series when the specialist’s quote has not been submitted shall be required to submit continuous, two-sided quotes in such series until such time as the specialist submits his/her quote, after which the Phlx XL participant that submitted such quote shall be obligated to submit quotations pursuant to Rule 1014(b)(ii)(D).

In situations where an AOP may be calculated and there is an order/quote imbalance, the system will immediately send an imbalance notice indicating the imbalance side (buy or sell) and the AOP and AOS (an “Imbalance Notice”) to Phlx XL participants provided that the primary market for the underlying security has disseminated the opening quote or trade. Phlx XL participants that have not submitted opening quotes will then submit their opening quotes, and Phlx XL participants that have submitted opening quotes may submit
revised opening quotes; thereafter the system will disseminate an updated Imbalance Notice every five seconds (or such shorter period as determined by the Options Committee and disseminated to membership via Exchange Circular) until the series is open. If no imbalance exists, no Imbalance Notice will be sent, and the system will establish an opening price as described in paragraph (c) below.

(c) – (d) No change.

(e) The system will not open a series if one of the following conditions is met:

   (i) there is no quote from the specialist or [a 99%] Phlx XL participants, as described in Rule 1017(b)(ii)(B) and (C) above;

   (ii) – (iii) No change.

(f) – (j) No change.

Commentary: 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 encourage Directed Orders by establishing a new quoting obligation for Directed SQTs (“DSQTs”) and Directed RSQTs (“DRSQTs”)

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8 The term “Directed Specialist, RSQT, or SQT” means a specialist, RSQT, or SQT that receives a Directed Order. See Exchange Rule 1080(l)(i)(C).
not less than 99% of the series listed on the Exchange in at least 60% of the options in which such DSQT or DRSQT is assigned. The proposed rule change is similar to the quoting obligation for participants that receive Directed Orders on other exchanges.\(^9\)

**Deletion of 99% Quoting Requirement for Directed SQTs/DRSQTs**

Currently, Rule 1014(b)(ii)(D) requires DSQTs and DRSQTs to quote continuous, two-sided markets in not less than 99% of the series in each Streaming Quote Option in which they receive Directed Orders. For competitive reasons, the proposed rule change would delete the 99% quoting requirement applicable to DSQTs and DRSQTs. Instead, DSQTs and DRSQTs, would be obligated to submit quotations under proposed Exchange Rule 1014(b)(ii)(D)(1), described below. This obligation would be similar to that of other exchanges with Directed or Preferenced Order flow programs.\(^10\) The Exchange is now concerned that the current 99% quoting obligation is impeding Directed Order flow to the Exchange.

**New Quoting Obligation for DSQTs and DRSQTs**

The proposed rule change would provide that, on any given day, a DSQT or a DRSQT would be responsible to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange of at least 60% of the options in which such DSQT or DRSQT is assigned. The Exchange believes that this new quoting obligation

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\(^9\) The Exchange notes that the International Securities Exchange, Inc. ("ISE") currently has rules in effect concerning “Preferenced Orders” that are virtually identical to the Exchange’s rules concerning Directed Orders (See ISE Rule 713, Supplementary Material .03). The quoting obligation applicable to ISE Competitive Market Makers, including those that receive “Preferenced Orders” is contained in ISE Rule 804(e)(2). See also, Securities Exchange Act Release No. 51818 (June 10, 2005), 70 FR 35146 (June 16, 2005) (SR-ISE-2005-18). The instant proposed rule change, which tracks ISE Rule 804, is intended to enable the Exchange to compete for Directed Orders by establishing a quoting obligation for Directed SQTs and RSQTs that is virtually identical to the quoting obligation applicable to ISE Competitive Market Makers that receive “Preferenced Orders.”

for DSQTs and DRSQTs should encourage member organizations to send Directed Orders to DSQTs and DRSQTs on the Exchange.

In order to ensure continuity of quoting, the proposed rule change would provide that, whenever a DSQT or DRSQT enters a quotation in an option in which such DSQT or DRSQT is assigned, such DSQT or DRSQT must maintain continuous quotations for all series of the option listed on the Exchange until the close of that trading day. The Exchange believes that this should promote liquidity on the Exchange.

**Amendments to Rule 1017, Openings in Options**

Currently, Rule 1017(b) provides that a series may open when: (i) the Exchange has received market orders, or the book is crossed (highest bid is higher than the lowest offer) or locked (highest bid equals the lowest offer); and (ii) either (A) the specialist’s quote has been submitted; (B) the quotes of at least two Phlx XL participants that have the 99% quoting obligation (“99% participants”) have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular); or (C) if neither the specialist’s quote nor the quotes of two 99% participants have been submitted within two minutes of the opening trade or quote on the primary market for the underlying security (or such shorter time as determined by the Options Committee and disseminated to membership via Exchange Circular), one 99% participant has submitted their quote.

The proposal would establish that if the specialist is not quoting at the opening, the system will open a series when any two Phlx XL participants are quoting within two minutes of the opening on the primary market for the underlying security, or when any
single Phlx XL participant has submitted his/her quote thereafter, thus eliminating the requirement that such Phlx XL participants must be 99% participants in order for the series to open.

In order to ensure the continuity of quotations in series that are opened when the specialist has not submitted his or her quotation, the proposed rule change would provide that a Phlx XL participant that submits a quote pursuant to the proposed rule in any series when the specialist’s quote has not been submitted would be required to submit continuous, two-sided quotes in such series until such time as the specialist submits his/her quote, after which the Phlx XL participant that submitted such quote would be obligated to submit quotations as described above under proposed Rule 1014(b)(ii)(D).

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act\textsuperscript{11} in general, and furthers the objectives of Section 6(b)(5) of the Act\textsuperscript{12} in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, by enabling the Exchange to compete for order flow in Directed Orders by establishing a new quoting obligation applicable to DSQTs and DRSQTs.

\textsuperscript{11} 15 U.S.C. 78f(b).

\textsuperscript{12} 15 U.S.C. 78f(b)(5).
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\(^\text{13}\) in order to compete with other exchanges that have similar rules in effect, as cited below.

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 [here](http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-Phlx-2006-11 on the subject line.

**Paper comments:**

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• 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-2006-11. 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-2006-11 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