

## Decentralized Linkage: NASDAQ OMX PHLX

Updated 8/31/09

### 1. Q: What is Decentralized Linkage?

**Decentralized Linkage** (also referred to as Distributive Linkage or the Options Order Protection and Locked/Crossed Market Plan), is the replacement for the Plan for the Purpose of Creating and Operating an Options Intermarket Linkage (Linkage Plan). Under the Linkage Plan, which is being phased out, participants used the Options Clearing Corporation (OCC) Linkage Hub for inter-exchange routing. Under the Decentralized Linkage plan, participants will route orders by way of private connectivity and membership. PHLX will use the NASDAQ Options Services (NOS) broker-dealer to access away exchanges.

Decentralized Linkage addresses issues including locked and crossed markets, trade-throughs and the introduction of Intermarket Sweep Orders (ISOs).

### 2. Q: How will NASDAQ OMX PHLX access other options exchanges?

**NASDAQ OMX PHLX<sup>SM</sup> (PHLX<sup>®</sup>)** will use NASDAQ Options Services, a broker-dealer, to access the different options exchanges. PHLX has direct connectivity to each exchange. PHLX will maintain customer anonymity when accessing other options exchanges. Orders sent to away exchanges will not contain any information pertaining to the identity of the customer.

### 3. Q: What is an Intermarket Sweep Order?

In conjunction with Decentralized Linkage, options markets will introduce the Intermarket Sweep Order (ISO). An ISO allows the receiving options exchange to trade through the current National Best Bid and Offer (NBBO).

By sending an exchange an order marked ISO, the sender is affirming that it has attempted to access all better-priced Protected Quotations displayed by other exchanges for the entire size displayed.

A Protected Bid/Offer is the best Bid/Offer for each options exchange as represented through the Options Price Reporting Authority (OPRA).

### 4. Q: Will PHLX send ISOs when routing to other options exchanges?

Yes. PHLX always seeks the best prices by routing customer orders to the exchange with the best price. When it receives a routable customer order that is priced through the NBBO it will route to the top price level at each exchange. To avoid order rejects from away exchanges, routed orders will always be marked with the ISO flag.

### 5. Q: How will PHLX process incoming ISOs?

If an order is flagged with the ISO designation, it indicates that the entering firm has attempted to access all Protected Quotes and PHLX may execute the order in its own book regardless of other quotations in the marketplace.

**6. Q: Will an ISO post on PHLX if the Time-In-Force is not Immediate-Or-Cancel (IOC)?**

No. All ISO orders received by PHLX will be treated as IOC regardless of Time-In-Force instruction.

**7. Q: How do I mark an order as ISO?**

The ISO flag field for PHLX order entry protocols:

Protocol	Field	ISO Value
FIX to Trade Options	Tag 18 Execlnst	f

**8. Q: How does Decentralized Linkage address trade-throughs?**

Under Decentralized Linkage, participants cannot trade through protected Bids or Offers unless certain trade-through exemptions apply. The PHLX trading system is designed to avoid trading through Protected Quotations unless PHLX receives an ISO order.

**Exceptions** to the trade-through prohibition are granted under the following circumstances:

- **Crossed Market** – There is no trade-through protection when there is a Crossed Market. A Crossed Market exists when the National Best Bid is greater than the National Best Offer (PHLX Rule 1084(b)(iii)).
- **Intermarket Sweep Order (ISO)** – The transaction that constitutes the trade-through is the execution of an order identified as an ISO (PHLX Rule 1084(b)(iv)).
- **Exchange-Routed ISOs** – Transactions occurring when the exchange trades at a price level while simultaneously routing ISOs to execute against all other better-priced Protected Quotations (PHLX Rule 1084(b)(v)).
- **Flickering Quotes** – The transaction occurred when the exchange displaying the Protected Quotation had displayed, within one second prior to the execution, a price that was equal or inferior to the price of the trade-through execution (PHLX Rule 1084(b)(vi)).
- **Non-Firm Quotes** – If an exchange’s quotes are identified as Non-Firm, those quotes may be traded through (PHLX Rule 1084(b)(viii)).
- **Complex Trades** - The transaction that created the trade-Through was a component of a Complex Trade as defined in PHLX Rule 1083(d) (see PHLX Rule 1084(b)(viii)).
- **Opening Process** - The transaction creating the trade-through occurred during an opening rotation.
- **Self Help** - The Protected Quotation being traded through is on an exchange experiencing technical difficulties. Specifically, if the exchange repeatedly fails to respond to incoming orders within one second, Self Help can be declared against that exchange at which point that exchange’s Protected Quotations are ignored. When Self Help is declared against an exchange, the party declaring Self Help must ensure that the problem is not with their own systems. Additionally, the exchange experiencing problems must be notified that Self Help has been declared against

it. Reasonable policies and procedures must be maintained regarding the Self Help process (PHLX Rule 1084(b)(i)). When declaring Self Help against PHLX, an email should be sent to: [systems.support@nasdaqomx.com](mailto:systems.support@nasdaqomx.com), followed by a phone call to +1 215 496 1571.

**9. Q: How does Decentralized Linkage address Locked and Crossed Markets?**

Locking or crossing Protected Quotations must be avoided under Decentralized Linkage.

**Exceptions** to this component of the plan are granted under the following circumstances:

- **System Malfunction (Self Help)** - The locking or crossing quotation was displayed at a time when the exchange was experiencing a failure, material delay or malfunction of its systems or equipment.
- **Crossed Market** - The locking or crossing quotation was displayed at a time when there was a Crossed Market.
- **Intermarket Sweep Order (ISO)** - The Member simultaneously routed an ISO to execute against the full displayed size of any locked or crossed Protected Bid or Protected Offer.

**10. Q: What are the data and record retention requirements for firms sending ISOs to PHLX?**

PHLX's Market Surveillance Group will monitor member activity to ensure that they do not engage in a pattern or practice of trading through Protected Quotations by entering orders marked ISO on PHLX without properly sweeping other markets with Protected Quotations. If PHLX Market Surveillance believes that a member may be improperly trading through away markets, PHLX Market Surveillance will request that the member provide evidence that the ISOs are being sent properly and that the member has effective policies and procedures in place to avoid trade-throughs. PHLX Market Surveillance will follow the standard set forth by the SEC in the [Responses to Frequently Asked Questions Concerning Rules 610 and Rule 611 of Regulation NMS](#)<sup>1</sup>.

**11. Q: Can non-customer orders be marked as ISO?**

Yes. Non-customer orders may be marked as ISO. When a firm submits a non-customer ISO to PHLX, the firm must simultaneously send ISOs to each exchange with a better-priced Protected Quotation.

**12. Q: How will PHLX process a non-ISO order that will lock or cross a Protected Quotation?**

PHLX only routes customer orders. If a firm sends a non-routable, non-ISO order that will lock or cross a Protected Quotation, PHLX will post the order on the book at a price that locks the NBBO and will disseminate the order to OPRA at a price that is one trading increment away from the NBBO so as not to lock the NBBO. PHLX will never trade through the NBBO if the order is not marked as ISO.

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<sup>1</sup> For example, a member could randomly select three trading days per month for review (known only to its compliance personnel) and maintain all relevant "snapshots" of the Firm-Specific Quotation Data from those days that are necessary to demonstrate the reasonableness of its policies and procedures. The following link shows responses to FAQs regarding Rules 610 and 611 of Regulation NMS. <http://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm>

**13. Q: What are the time requirements with regards to ISO orders and trades?**

In order to send an ISO, the sending party must simultaneously send ISOs to all exchanges with better Protected Quotations.

**14. Q: How does much time can elapse between sending an ISO and crossing?**

Crosses must be executed contemporaneously with the routing of ISOs.

**15. Q: How does a firm know when PHLX is open and its quotes are considered “protected”?**

When PHLX disseminates a firm quote on OPRA, the market is open and the quotes are protected. Additionally, the PHLX data feeds disseminate a message indicating when a particular option is open for trading, at which time quotations are firm and protected. Once PHLX is open with Protected Quotations, firms may send ISOs under appropriate circumstances.

**16. Q: Will the broker-dealer PHLX uses to access other exchanges be monitored for compliance?**

Yes. PHLX will use the NASDAQ Options Services (NOS) broker-dealer to access other exchanges. The sole use of NOS by PHLX system will be to route orders in options listed and open for trading on PHLX to away markets pursuant to Exchange rules on behalf of a PHLX member. PHLX member information is not sent to the away exchanges when the order is routed. NOS's Designated Examining Authority and the exchanges that NOS accesses will monitor the broker-dealer to ensure proper activity.

**17. Q: Where can I find more information?**

- Contact [PHLX System Support](#) at +1 215 496 1571
- Contact [Transaction Services U.S. Market Sales](#) at +1 800 846 0477