

MEMORANDUM

TO: Members, Member Organizations, Participants, Participant Organizations

FROM: Richard S. Rudolph, Vice President and Counsel
Legal Department

DATE: August 21, 2007

RE: Proposed Rule Change
Pilot Extension/Expansion
Options Quoted and Traded in Penny Increments

The Exchange has filed a **proposed** rule change to amend Exchange Rule 1034 that reflect the extension of a pilot program (the “pilot”) that permits certain options series to be quoted and traded in increments of \$0.01, through January 31, 2009; and (ii) an increase in the number of options included in the pilot as set forth in a rollout schedule specified by the Securities and Exchange Commission.

Summary: In June, 2006, the six U.S. options exchange began a six-month pilot program in which 13 options are quoted and traded in minimum increments of one cent.

Current Pilot

The pilot began on January 26, 2007, was extended once, and is now scheduled to expire September 27, 2007. All series in options included in the pilot (“pilot options,” listed below) with a price of less than \$3.00 are quoted and traded in minimum increments of \$0.01, and pilot options with a price of \$3.00 or higher are currently quoted and traded in minimum increments of \$0.05, except that options overlying the Nasdaq-100 Index Tracking Stock (“QQQQ”)¹ are quoted and traded in minimum increments of \$0.01 for all series regardless of the price. The options included in the **current** pilot are:

<u>Symbol</u>	<u>Underlying Security</u>
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IWM	Ishares Russell 2000
QQQQ	QQQQ
SMH	SemiConductor Holders
GE	General Electric
AMD	Advanced Micro Devices
MSFT	Microsoft
INTC	Intel
CAT	Caterpillar
WFMI	Whole Foods
TXN	Texas Instruments
A	Agilent Tech Inc.
FLEX	Flextronics International
SUNW	Sun Micro

Expanded Pilot

The current pilot will be expanded to include additional options in two phases beginning on September 28, 2007.

Phase I

Phase I will begin September 28, 2007, and will continue through March 27, 2008. Phase I will include the original 13 pilot options, together with 22 additional options. The 22 new options (listed below), combined with the original 13, will represent approximately 35% of national trading volume.

All options included in the pilot in Phase I will trade in \$0.01 increments in series trading below \$3.00, and in \$0.05 increments in series trading at \$3.00 and above. Options on QQQQ will continue to trade in increments of \$0.01 for all series. Options to be added to the pilot in Phase I:

<u>Symbol</u>	<u>Underlying Security</u>
SPY	SPDR Trust Series 1
AAPL	Apple Inc.
MO	Altria Group Inc.
DNDN	Dendreon Corporation
AMGN	Amgen, Inc.
YHOO	Yahoo!, Inc.
QCOM	Qualcomm, Inc.
GM	General Motors Corporation
XLE	S&P Energy Select Sector SPDR
DIA	DIAMONDS Trust Series I
OIH	Oil Services HOLDERS
NYX	NYSE Euronext
CSCO	Cisco Systems, Inc.

XLF	S&P Financial Select Sector SPDR
T	AT&T Corporation
C	Citigroup, Inc.
AMZN	Amazon.com, Inc.
MOT	Motorola, Inc.
RIMM	Research in Motion, Ltd.
FCX	Freeport-McMoRan Cooper & Gold, Inc.
COP	ConocoPhillips
BMJ	Bristol-Meyers Squibb Company

Phase II

Phase II will begin March 28, 2008, and will extend for one year, through March 27, 2009. Options will be added to the pilot in Phase II such that the Top 50 options by national volume will be included. Thus, any options in the Top 50 that are not included in Phase I will be added to the pilot in Phase II. Again, all penny options in Phase II will trade in \$0.01 increments in series trading below \$3.00, and in \$0.05 increments in series trading at \$3.00 and above. Options on QQQQ will continue to trade in increments of \$0.01 for all series.

Reporting

The Exchange (and all U.S. options exchanges) will be required to submit four (4) additional reports on the pilot, which will be due on the last day of the calendar month following a specified period, as follows:

- Report #1 will cover the period from May 1, 2007 - September 27, 2007.
- Report #2 will cover the period from September 28, 2007 - January 31, 2008.
- Report #3 will cover the period from February 1, 2008 - July 31, 2008.
- Report #4 will cover the period from August 1, 2008 - January 31, 2009.

The text of the proposed rule change is set forth below. Questions may be directed to Richard S. Rudolph, Vice President and Counsel, at (215) 496-5074.

Proposed Rule Text

Brackets indicate deletions; underlining indicates new text.

Minimum Increments

Rule 1034. (a) *****

(i) (A) No change.

(B) For a pilot period scheduled to expire [September 27, 2007] January 31, 2009 (the "pilot"), certain options shall be quoted and traded on the Exchange in minimum increments of \$0.01 for all series in such options with a price of less than \$3.00, and in

minimum increments of \$0.05 for all series in such options with a price of \$3.00 or higher, except that options overlying the Nasdaq-100 Index Tracking Stock (“QQQQ”) shall be quoted and traded in minimum increments of \$0.01 for all series regardless of the price. A list of such options shall be communicated to membership via Exchange circular.

(C) No change.

(ii) – (iii) No change.