

MEMORANDUM

TO: Members and Member Organizations  
FROM: John Dayton  
DATE: January 11, 2007  
RE: Benchmark and Contingent Crosses in XLE for Nasdaq Securities

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The Exchange has filed an immediately effective proposed rule change with the Securities and Exchange Commission (“Commission”) to clarify that XLE Participants are allowed to submit IOC Cross Orders marked as Benchmark and as Qualified Contingent Trades in Nasdaq listed securities before the trade through provisions (Rule 611) of Regulation NMS are operative on the Exchange (the “Trading Phase Date”), which is currently scheduled for February 5, 2007. A XLE Participant sending an IOC Cross Order marked as Benchmark or as Qualified Contingent Trades before the Trading Phase Date must ensure that they comply with new Phlx Rule 185A(c) and (d), which is attached.

Questions regarding the proposed rule change may be directed to John Dayton at (215) 496-5162. Questions regarding XLE functionality may be directed to the XLE Help Desk at (215) 496-5311 or 1-877-678-PHLX.

Rule Text

Underling indicates additions; brackets indicate deletions

**Rule 185A.**

**[Intermarket Sweep Orders]Orders and Order Execution - Temporary**

(a) An away market obligation is an immediate or cancel limit order for an NMS stock generated by Phlx in connection with the execution of an order by Phlx and routed to one or more away market centers to execute against all better-priced protected quotations displayed by the other market centers up to their displayed size. In the event that an away market that trades a particular security is capable of receiving intermarket sweep orders, then the Exchange may choose to generate and utilize intermarket sweep orders as the away market obligations for that market. Before Rule 611 of Regulation NMS is operative on the Exchange (the “Trading Phase Date”), the words “immediate-or-cancel intermarket sweep orders” in Rule 185(b)(1)(C)(i)-(ii) and (b)(2)(B) shall mean “away market obligations.”

(b) In addition, before the Trading Phase Date, a XLE Participant may submit an ISO or an IOC Cross Order marked by the XLE Participant entering the order as meeting the requirements of an intermarket sweep order to XLE only if it has simultaneously sent an intermarket sweep order (or comparable order) for the full displayed size of the top of book of every other ITS Participant

displaying a better-priced quotation. For Nasdaq Global Market Securities and Nasdaq Capital Market Securities, a XLE Participant may submit an ISO or an IOC Cross Order marked by the XLE Participant entering the order as meeting the requirements of an intermarket sweep order to XLE only if it has simultaneously sent an intermarket sweep order (or comparable order) for the full displayed size of the top of book of every national securities exchange or national securities association displaying a better-priced quotation.

(c) Before the Trading Phase Date, a XLE Participant may mark an IOC Cross Order in Nasdaq Global Market Securities or Nasdaq Capital Market Securities as Benchmark if it is an order: (1) at a price that was not based, directly or indirectly, on the quoted price of the NMS Stock at the time of the execution; and (2) for which the material terms were not reasonably determinable at the time the commitment to execute the order was made.

(d) Before the Trading Phase Date, a XLE Participant may mark an IOC Cross Order in Nasdaq Global Market Securities or Nasdaq Capital Market Securities as Qualified Contingent Trade. A Qualified Contingent Trade is a transaction consisting of two or more component orders, executed as agent or principal, where:

(1) at least one component order is in an NMS Stock;  
(2) all components are effected with a product or price contingency that either has been agreed to by the respective counterparties or arranged for by a broker-dealer as principal or agent;  
(3) the execution of one component is contingent upon the execution of all other components at or near the same time;

(4) the specific relationship between the component orders (e.g., the spread between the prices of the component orders) is determined at the time the contingent order is placed;

(5) the component orders bear a derivative relationship to one another, represent different classes of shares of the same issuer, or involve the securities of participants in mergers or with intentions to merge that have been announced or since cancelled (Transactions involving securities of participants in mergers or with intentions to merge that have been announced would meet this aspect of the requested exemption. Transactions involving cancelled mergers, however, would constitute Qualified Contingent Trades only to the extent they involve the unwinding of a pre-existing position in the merger participants' shares. Statistical arbitrage transactions, absent some other derivative or merger arbitrage relationship between component orders, would not satisfy this element of the definition of a Qualified Contingent Trade.);

(6) the IOC Cross Order marked as Qualified Contingent Trade is fully hedged (without regard to any prior existing position) as a result of the other components of the contingent trade (A XLE Participant may demonstrate that an IOC Cross Order marked as Qualified Contingent Trade is fully hedged under the circumstances based on the use of reasonable risk-valuation methodologies.); and

(7) the IOC Cross Order marked as Qualified Contingent Trade involves at least 10,000 shares or has a market value of at least \$200,000.