SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49968; File No. SR-Phlx-2004-27)

July 2, 2004

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval to a Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to the Processing of Satisfaction Orders following a Trade-Through Pursuant to the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on April 23, 2004, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") submitted to the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II 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 is proposing to amend Exchange Rule 1085 to modify the method in which following a Trade-Through,[3] the Exchange processes Satisfaction Orders[4] pursuant to the Linkage Plan when there is a change in the status of the underlying customer order.

The text of the proposed rule change is available at the Exchange and at the Commission.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 A "Trade-Through" is a transaction in an options series at a price that is inferior to the National Best Bid or Offer. See Section 2(29) of the Linkage Plan and Exchange Rule 1083(t).

4 A "Satisfaction Order" is defined as an order sent through the Options Intermarket Linkage to notify a Participant of a Trade-Through and to seek satisfaction of the liability arising from that Trade-Through. See Section 2(16)(c) of the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage ("Linkage Plan") and Exchange Rule 1083(k)(iii).

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 had received on the proposed rule change. The text of these statements may be examined at the places specified in Item III below. The Exchange 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 this filing is to enhance the manner in which the Phlx processes Satisfaction Orders following a Trade-Through, which also is the subject of a recent amendment to the Linkage Plan.[5] If the displayed price that is traded through represents a customer order, the Phlx specialist representing that order can send a Satisfaction Order requiring the member on the exchange that caused the Trade-Through to satisfy the customer order.[6] The proposed rule change would modify the manner in which Satisfaction Orders are processed in three ways.

First, the size of the Satisfaction Order would be limited to the lesser of the size of the customer order traded through and the size of the transaction that caused the Trade-Through. Currently, Section 8(c)(ii)(B)(2) of the Linkage Plan and Exchange Rule 1085 permits a Satisfaction Order to be submitted for the full size of the customer order traded through,

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5 See Securities Exchange Act Release No. 49691 (May 12, 2004), 69 FR 28954 (May 19, 2004) (File No. 4-429) (Notice of filing Joint Amendment No. 11 to the Linkage Plan).

6 See Sections 7(a)(ii)(D) and 8(c)(ii) of the Linkage Plan.

regardless of the size of the transaction that caused the Trade-Through. Under the proposal, a Satisfaction Order would be limited to the lesser of the size of the Verifiable Number of Customer Contracts[7] in the disseminated bid or offer that was traded through, or the size of the transaction that caused the Trade-Through.

Second, the Exchange proposes to amend its rules concerning the cancellation of pending Satisfaction Orders if the underlying customer order is executed or canceled. Currently, Exchange Rule 1085 and the Linkage Plan[8] permit a Phlx specialist that sends a Satisfaction Order to reject a message from the receiving exchange that the customer order has been satisfied (hereinafter, a "fill" of that Satisfaction Order) if the underlying customer order has been executed on the Phlx or has been canceled while the Satisfaction Order is being processed. There is, however, no current requirement for the Phlx specialist to cancel the pending Satisfaction Order if the underlying customer order is executed or canceled. Therefore, the Phlx specialist may send a rejection of a fill of a Satisfaction Order that might have been avoided if the pending Satisfaction Order had been canceled when the underlying customer order was executed or canceled. The proposed rule change is intended to address this issue by requiring the exchange that sends a Satisfaction Order to cancel such Satisfaction Order when the underlying customer order has been executed or canceled.

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7 "Verifiable Number of Customer Contracts" is defined as the number of Customer contracts in the book of a Participant. See Section 2(30) of the Linkage Plan. A "Participant" is defined as an Eligible Exchange whose participation in the Linkage Plan has become effective pursuant to Section 4(c) of the Linkage Plan. See Section 2(24) of the Linkage Plan. Currently, the Participants in the Linkage Plan are the International Securities Exchange, Inc., the American Stock Exchange LLC, the Chicago Board Options Exchange, Inc., the Pacific Exchange, Inc., the Phlx, and the Boston Stock Exchange, Inc.

8 See Section 8(c)(ii)(C) of the Linkage Plan.

Third, as noted above, a specialist that sends a Satisfaction Order currently may reject a fill of such Satisfaction Order if the underlying customer order is executed or canceled while the Satisfaction Order is pending. The proposed rule change would limit the circumstances under which the sender of a Satisfaction Order could reject a fill of that order when the underlying customer order is executed or canceled while the Satisfaction Order is pending. Specifically, the sender of the Satisfaction Order would not be permitted to reject such a fill when the sender, itself, trades against the underlying customer order while the Satisfaction Order is pending. The Exchange believes that this provision should ensure that the sender of a Satisfaction Order would not be permitted to reject a fill of the Satisfaction Order when it executes against the underlying customer order for its own account.

2. Statutory Basis

The Exchange believes that the proposed rule is consistent with Section 6(b) of the Act,[9] in general, and furthers the objectives of Section 6(b)(5)[10] in particular in that it 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 providing enhancements to the current method of Satisfaction Order processing.

B. 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.

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

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[9] 15 U.S.C. 78f(b).

[10] 15 U.S.C. 78f(b)(5).

No written comments were solicited or received with respect to the proposed rule change.

III. 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 (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-Phlx-2004-27 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-2004-27. 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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such 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-2004-27 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.[11] In particular, the Commission finds that the proposed rule change is consistent with the requirements of Section 6(b)(5) of the Act[12] which requires, among other things, that the rules of an exchange be 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 to protect investors and the public interest. The Commission believes that the proposed rule change should facilitate the handling of Satisfaction Orders in an efficient and fair manner.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of the notice thereof in the Federal Register. As noted above, the proposed rule change incorporates changes into the Phlx Rules that correspond to changes made to the Linkage Plan through Joint Amendment No. 11, which was published for

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[11] In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[12] 15 U.S.C. 78f(b)(5).

public comment in the Federal Register on May 19, 2004.[13] The Commission received no comments in response to publication of Joint Amendment No. 11. The Commission believes that no new issues of regulatory concern are being raised by Phlx's proposed rule change. The Commission believes, therefore, that granting accelerated approval of the proposed rule change is appropriate and consistent with Sections 6 and 19(b) of the Act.[14]

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[15] that the proposed rule change (SR-Phlx-2004-27) is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[16]

Margaret H. McFarland
Deputy Secretary

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13 See supra note 5.

14 15 U.S.C. 78f and 78s(b).

15 15 U.S.C. 78s(b)(2).

16 17 CFR 200.30-3(a)(12).