

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-60627; File No. SR-Phlx-2009-78)

September 4, 2009

Self-Regulatory Organizations; NASDAQ OMX PHLX, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to an Extension of the FLEX Minimum Size Pilot Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup>, and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on September 3, 2009, NASDAQ OMX PHLX, Inc. (“Phlx” or “Exchange”) filed with 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 Exchange. The Exchange filed the proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder.<sup>4</sup> 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 Exchange proposes to amend Phlx rules to amend its Rule 1079 (FLEX Index, Equity and Currency Options), to amend its Rule 1079 (FLEX Index, Equity and Currency Options), [sic] to extend through September 4, 2010, the Exchange’s pilot program that reduced from 250 contracts to 150 contracts the minimum value size for an opening transaction (other than FLEX

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

Quotes responsive to a FLEX Request for Quotes)<sup>5</sup> in any FLEX Equity Option<sup>6</sup> series in which there is no open interest at the time a FLEX Request for Quotes (“RFQ”) is submitted (the “Pilot Program”).<sup>7</sup>

The text of the proposed rule change is available on the Exchange’s Website at <http://www.nasdaqtrader.com/micro.aspx?id=PHLXRulefilings>, at the principal office of the Exchange, and at the Commission’s Public Reference Room.

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 Exchange 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 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 the proposed rule change is to extend the Pilot Program through September 4, 2010.

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<sup>5</sup> FLEX Quotes responsive to a FLEX Request for Quote (“RFQ”) have different parameters that were not changed by the pilot program proposal. See Phlx Rule 1079(a)(8)(C).

<sup>6</sup> FLEX Equity Options are flexible exchange-traded options contracts that overlie equity securities. FLEX Equity Options provide investors with the ability to customize basic option features including size, expiration date, exercise style, and certain exercise prices. FLEX Equity Options (as also FLEX index options) may have expiration dates within five years. See Phlx Rule 1079.

<sup>7</sup> See Securities Exchange Act Release No. 57824 (May 15, 2008), 73 FR 29805 (May 22, 2008) (SR-Phlx-2008-35)(notice of filing and immediate effectiveness establishing the Pilot Program).

On or about May 15, 2008, the Exchange filed SR-Phlx-2008-35 with the Commission to establish the Pilot Program. The Pilot Program reduced the minimum value size for an opening transaction (other than FLEX Quotes responsive to a FLEX RFQ) in any FLEX Equity Option series in which there is no open interest at the time an RFQ is submitted.<sup>8</sup> The proposed extension of the Pilot Program for opening FLEX option transactions should provide members that use FLEX Equity Options greater flexibility in structuring the terms of such options to better comport with the particular needs of the members and their customers.

Prior to the Pilot Program, Phlx Rule 1079(a)(8)(A) set the minimum opening transaction value size in the case of a FLEX Equity Option in a newly established series as the lesser of (i) 250 contracts or (ii) the number of contracts overlying \$ 1 million in the underlying securities. Under the Pilot Program, the Exchange reduced the “250 contracts” component to “150 contracts”; the \$ 1 million underlying value component continued to apply unchanged.<sup>9</sup>

The Exchange now proposes to extend the Pilot Program.

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<sup>8</sup> See Securities Exchange Act Release No. 57824 (May 15, 2008), 73 FR 29805 (May 22, 2008)(SR-Phlx-2008-35)(notice of filing and immediate effectiveness establishing the Pilot Program). The filing also modified the minimum value size for an opening transaction in a currently-opened FLEX Equity series (other than FLEX Quotes responsive to a RFQ) to the lesser of 100 contracts or the number of contracts overlying \$1 million in the underlying securities. Other options exchanges have established FLEX pilot programs that are similar to the Exchange’s. See, e.g., Securities Exchange Act Release No. 57429 (March 4, 2008), 73 FR 13058 (March 11, 2008) (SR-CBOE-2006-36)(approval order).

<sup>9</sup> Under the Pilot Program, an opening transaction in a FLEX Equity series in a stock priced at approximately \$ 66.67 or more would reach the \$ 1 million limit before it would reach the contract size limit, i.e., 150 contracts times the multiplier (100) times the stock price (\$ 66.67) equals just over \$ 1 million in underlying value. For a FLEX Equity series in a stock priced at less than \$ 66.67, the 150 contract size limit would apply.

Given that FLEX Equity Option transactions can occur in increments of 100 or more contracts in subsequent opening transactions,<sup>10</sup> the Exchange believes it is reasonable to permit the initial series opening transaction size to be 150 contracts (or \$ 1 million in underlying value, whichever is less). The Exchange notes that the opening size requirement for FLEX Equity Options was originally put in place to limit participation in FLEX Equity Options to sophisticated, high net worth investors rather than retail investors.<sup>11</sup> The Exchange believes that the reduction of the minimum value size for opening a series, per the Pilot Program, provides FLEX-participating members and their customers with greater flexibility in structuring the terms of FLEX Equity Options to better suit the FLEX traders' particular needs. The Exchange believes that market participants benefit from being able to trade these customized options in an exchange environment in several ways, including, but not limited to, enhanced efficiency in initiating and closing out positions; increased market transparency; and heightened contra-party creditworthiness due to the role of The Options Clearing Corporation as issuer and guarantor of FLEX Equity Options.

In support of extending the Pilot Program, the Exchange has submitted to the Commission a FLEX Pilot Program Report ("Report") detailing the Exchange's experience with the Pilot Program. Specifically, the Report contains data and written analysis regarding: (i) the open interest and trading volume in FLEX Equity Options for which series were opened with a

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<sup>10</sup> Specifically, for FLEX Equity Options the minimum value size for a transaction in any currently-opened FLEX series is the lesser of 100 contracts or the number of contracts overlying \$ 1 million in the underlying securities; or the lesser of 25 contracts or the remaining size in the case of a closing transaction. Additionally, the minimum value size for a FLEX Quote entered in response to a RFQ in FLEX Equity Options is the lesser of 25 contracts or the remaining size in a closing transaction. See Phlx Rules 1079(a)(8)(B)(ii) and 1079(a)(8)(C)(ii).

<sup>11</sup> The existing customer base for FLEX Options includes institutional investors, retail investors, and high net worth individuals.

minimum opening size of 150 to 249 contracts and less than \$ 1 million in underlying value; and (ii) analysis on the types of investors that initiated opening FLEX Equity Options transactions (i.e., institutional, high net worth, or retail, if any). The Report was submitted under separate cover and seeks confidential treatment under the Freedom of Information Act.

The Exchange believes there is sufficient investor interest and demand in the Pilot Program to warrant its extension. The Exchange believes that, during the time that the Pilot Program has been in operation, it has afforded investors with additional means of managing their risk exposures and carrying out their investment objectives. The Exchange represents that it has the necessary system capacity to continue to support the option series listed under the Pilot Program.

Should the Exchange desire to propose an extension, expansion, or permanent implementation of the Pilot Program, the Exchange would submit, along with a filing proposing any necessary amendments to the Pilot Program, a pilot program Report for the extended period during which the Pilot Program is in effect<sup>12</sup> The Report, along with any filing to extend or permanently implement the Pilot Program, would be submitted to the Commission at least forty-five days prior to the expiration date of the Pilot Program.

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<sup>12</sup> The report would provide: (i) data and analysis on the open interest and trading volume in FLEX Equity Options for which series were opened with a minimum opening size of 150 to 249 contracts and less than \$ 1 million in underlying value; and (ii) analysis on the types of investors that initiated opening FLEX Equity Options transactions (i.e., institutional, high net worth, or retail, if any).

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>13</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>14</sup> 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 extending the Exchange's Pilot Program in respect of FLEX options. The Exchange believes that extension of the Pilot Program will result in a continuing benefit to investors by allowing them additional means to manage their risk exposure and carry out their investment objectives, and will allow the Exchange to further study investor interest in the Pilot Program.

### 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

Because the proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative prior to 30 days from the date on which it was filed, or such shorter time as the Commission may designate, if consistent with the protection of investors and the public interest,

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<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>15</sup> and Rule 19b-4(f)(6) thereunder.<sup>16</sup>

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative for 30 days after the date of filing.<sup>17</sup> However, Rule 19b-4(f)(6)(iii) permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest.<sup>18</sup> The Exchange has requested that the Commission waive the 30-day operative delay so that the proposal may become operative immediately upon filing, thereby allowing the Exchange to seamlessly continue the Pilot Program in respect of FLEX options.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because such waiver will allow the Exchange to continue its Pilot Program without interruption in its current form. The Commission notes that the Exchange did not provide a pilot program report to the Commission at least ninety days prior to the expiration date of the Pilot Program as the Exchange had undertaken to do as part of its original proposal.<sup>19</sup> Waiving the operative delay to accommodate an extension of the Pilot Program will provide investors with a continued ability to utilize the lower minimum value size for an opening transaction in a FLEX Equity Option series on Phlx and also will provide the Exchange with additional time to collect data and prepare and submit to the Commission a pilot

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<sup>15</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>16</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the self-regulatory organization to submit to the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

<sup>17</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>18</sup> See id.

<sup>19</sup> See Securities Exchange Act Release No. 57824 (May 15, 2008), 73 FR 29805, 29806 (May 22, 2008) (SR-Phlx-2008-35).

program report in the event that it seeks to extend or permanently implement the Pilot Program.<sup>20</sup> For these reasons, the Commission designates the proposed rule change as operative upon filing.<sup>21</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.<sup>22</sup>

#### 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 (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-Phlx-2009-78 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

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<sup>20</sup> The Commission notes that the Exchange has undertaken in this filing to submit a pilot program report at least forty-five days prior to the expiration date of the Pilot Program.

<sup>21</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>22</sup> 15 U.S.C. 78s(b)(3)(C).



All submissions should refer to File Number SR-Phlx-2009-78. 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, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. 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-2009-78 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>23</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>23</sup> 17 CFR 200.30-3(a)(12).