SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62519; File No. SR-Phlx-2010-79)

July 16, 2010

Self-Regulatory Organizations; NASDAQ OMX PHLX, Inc.; Notice of Filing of Proposed Rule Change Relating to the Establishment of NASDAQ OMX PSX as a Platform for Trading NMS Stocks

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 June 8, 2010, NASDAQ OMX PHLX, Inc. (the "Exchange" or "PHLX") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 the Substance of the Proposed Rule Change

PHLX is filing a proposed rule change to establish NASDAQ OMX PSX, a new electronic platform for trading NMS stocks. The text of the proposed rule change is available at http://nasdaqomxphlx.cchwallstreet.com, on the Commission's Web site at www.sec.gov, at the Exchange's principal office, and at the Commission's Public Reference Room. PHLX will implement the proposed rule change as soon as practicable following approval by the Commission.

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

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

[2]   17 CFR 240.19b-4.

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.   <u>Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change</u>

      1.   <u>Purpose</u>

      a.   <u>Introduction and Background</u>

PHLX proposes to introduce NASDAQ OMX PSX ("PSX" or the "System"), a new fully

integrated order display and execution system for all NMS stocks (as defined in SEC Rule

600(b)(47) under Regulation NMS).[3] Like the NASDAQ Market Center and the NASDAQ

OMX BX Equities System, PSX will be an open-access, fully electronic system that

accommodates diverse business models and trading preferences, using technology to aggregate

and display liquidity and make it available for execution. PSX will not list stocks, but rather will

trade only stocks listed on other exchanges.

PSX will allow PSX Participants to enter unlimited orders at multiple price levels.

Orders of all PSX Participants will be integrated and displayed via data feeds to Participants and

other data subscribers. PSX Participants will be able to access the aggregated trading interest of

all other PSX Participants in accordance with non-discretionary order execution algorithms. In

contrast with most markets, which use a price-time algorithm, however, PSX will use a price-

display-pro rata size algorithm. Incoming orders will be allocated first to resting orders with the

best price. As among orders with the same price, incoming orders will be allocated first to

resting Displayed Orders and then to resting Non-Displayed Orders. As among Displayed

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[3]   17 C.F.R. 242.600(b)(47).

Orders at the same price or Non-Displayed Orders at the same price, incoming orders will be allocated among resting orders pro rata based on the size of the resting orders.[4]

Existing PHLX rules that apply to members and member organizations with respect to their activities on PSX are listed in Rule 3202. In addition, two existing PHLX rules, Rule 160 and Rule 188, are being deleted and their content moved into the new 3300 series.[5]

b.   System Access

PSX will be open to all member organizations of PHLX that comply with the rules governing PSX.[6] There will not be separate classes of membership. Specifically, unlike the NASDAQ Market Center, PSX will not have a separate class of market makers. Accordingly, PHLX expects that all PSX Participants will participate on consistent terms by entering orders into PSX for the purpose of posting available liquidity and accessing that liquidity.

As provided in proposed Rule 3223, however, PSX will make its facilities available to any electronic communications network ("ECN") or alternative trading system ("ATS") that (i) wishes to use PSX as a means to display the best prices and sizes of orders entered into the ECN or ATS by subscribers of the ECN or ATS, if the ECN or ATS so chooses or is required by SEC Rule 301(b)(3) to display a subscriber's order, and (ii) allow any PHLX member organization the electronic ability to effect a transaction with such priced orders that is equivalent to the ability to

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[4]   The allocation methodology for odd-lot orders is discussed in greater detail below.

[5]   Proposed Rules 3301(a), 3305(a)(1), 3309

[6]   Through a separate filing, PHLX will amend Rule 604 to require all member organizations trading on PSX to register representatives and principals in accordance with rules similar to those governing registration of associated persons of members of the NASDAQ Stock Market. PHLX will, at a later date, amend its rules governing registration of associated persons of member organizations that trade options but not cash equities through PHLX, to reflect consistent registration standards being developed by various self-regulatory organizations in consultation with the Commission.

effect a transaction with other orders displayed by PSX. Any such ECN or ATS would be

required to comply with the terms and conditions of PSX Rule 3223.[7]

Participants will gain access to PSX via direct or indirect electronic linkages utilizing the

Financial Information Exchange, or FIX, protocol, as well as proprietary RASH and OUCH

protocols. Each protocol is already used and widely accepted by market participants in the

NASDAQ Market Center and the NASDAQ OMX BX Equities System, and may be used by

Participants for order entry, modification and cancellation, and message transmittal for all

securities traded through PSX. Participants will have the ability to establish connectivity to PSX

directly or through third-party connectivity providers, including a range of extranets and service

bureaus. All of the communications protocols will be publicly available to allow Participants

and services bureaus to develop their own front-end software.

As provided in proposed Rule 3211, Participants must execute all applicable agreements

with PHLX (including the NASDAQ OMX U.S. Services Agreement[8]); maintain membership

in, or access arrangements with a participant of, a clearing agency registered with the

Commission that maintains facilities through which PSX compared trades may be settled;

comply with all applicable rules and operating procedures of PHLX and the Commission in the

use of the System; maintain the physical security of the equipment located on the Participant's

premises to prevent the improper use or access to PHLX systems, including unauthorized entry

of information into PSX; accept and settle each PSX trade that PSX identifies as having been

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[7]   Specifically, the ATS or ECN must be a PHLX member organization, enter into and comply with applicable agreements, agree that PHLX may disseminate the ECN's or ATS's best priced orders, demonstrate that it is compliance with applicable regulatory requirements, and accept automated executions against orders that it enters into the System.

[8]   http://www.nasdaqtrader.com/content/AdministrationSupport/AgreementsTrading/nasdaq_access_agreement.pdf.

effected by such Participant, or if settlement is to be made through another clearing member,

guarantee the acceptance and settlement of such identified PSX trade by the clearing member on

the regularly scheduled settlement date; and input accurate information into the System,

including, but not limited to, whether the member organization acted in a principal, agent, or

riskless principal capacity. Each PSX Participant will be under a continuing obligation to inform

PHLX of noncompliance with any of its registration requirements, and must make such reports

to PHLX as it may require.[9] In addition, each Participant must provide such information relating

to a specific PHLX rule, SEC rule, or term of a joint industry plan as PHLX regulatory staff may

request.[10] PHLX may impose on Participants such temporary restrictions on order entry as

PHLX may determine to be necessary to protect the integrity of PSX or other PHLX systems.[11]

In addition to proposed rules specific to the operation of PSX, member organizations must

comply with existing PHLX rules governing member conduct, to the extent that they are relevant

to trading on PSX. PHLX rules applicable to activities of member organizations on PSX are

listed in proposed rule 3202.

Failure by a PSX Participant to comply with any of the rules or registration requirements

applicable to PSX shall subject such Participant to censure, fine, suspension or revocation of its

registration as a PSX Participant, or any other fitting penalty under the rules of the Exchange.[12]

In accordance with the procedures of PHLX's Disciplinary Rules (Rules 960.1 through 960.12),

PHLX may suspend, condition, limit, prohibit or terminate the authority of a Participant to enter

orders in one more securities for violations of applicable requirements or prohibitions, or may

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[9]   Proposed Rules 3211(b), 3216.

[10]   Proposed Rule 3225.

[11]   Proposed Rule 3211(c).

[12]   Proposed Rule 3228(a).

terminate access to the System if a Participant fails to meet standards of eligibility or to pay for services rendered.[13]

PHLX disclaims liability for any losses, damages or other claims arising from the use of PSX; however, it may compensate users for losses directly resulting from PSX's actual failure to correctly process an order, message, or other data, in an amount not to exceed the larger of $500,000 per month or the amount of recovery obtained by PHLX under any applicable insurance policy.[14]

When it commences operation, PSX will allow sponsored access in accordance with rules identical to those currently in effect at the NASDAQ Stock Market ("NASDAQ"), which are reflected in proposed Rule 3211(d). When NASDAQ implements recently approved rules governing sponsored access,[15] PSX will adopt and implement identical rules to govern sponsored access. Under the current rules, a Sponsored Participant may obtain authorized access to PSX only if such access is authorized in advance by one or more member organizations as follows:

- Sponsored Participants must enter into and maintain customer agreements with one or more Sponsoring Member Organizations, establishing proper relationship(s) and account(s) through which the Sponsored Participant may trade on PSX. Such customer agreement(s) must incorporate the following Sponsorship Provisions:

- The Sponsoring Member Organization must acknowledge and agree that:

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[13]   Proposed Rules 3221, 3222.

[14]   Proposed Rule 3226. Accordingly, existing PHLX Rule 652(a) is not applicable to activity on PSX.

[15]   Securities Exchange Act Release No. 61345 (January 13, 2010), 75 FR 32631 (January 20, 2010) (SR-NASDAQ-2008-104). If NASDAQ's rules are superseded by rules adopted by the Commission, then both NASDAQ and PSX will operate in accordance with such rules.

- All orders entered by a Sponsored Participant and any person acting on behalf of or in the name of such Sponsored Participant and any executions occurring as a result of such orders are binding in all respects on the Sponsoring Member Organization; and

- The Sponsoring Member Organization is responsible for any and all actions taken by a Sponsored Participant and any person acting on behalf of or in the name of such Sponsored Participant.

- A Sponsoring Member Organization must comply with the PHLX Certificate of Incorporation, Bylaws, Rules and procedures with regard to PSX, and a Sponsored Participant must comply with the PHLX Certificate of Incorporation, Bylaws, Rules and procedures with regard to PSX, as if the Sponsored Participant were a PHLX Member Organization.

- A Sponsored Participant must maintain, keep current and provide to the Sponsoring Member Organization a list of individuals authorized to obtain access to PSX on behalf of the Sponsored Participant.

- A Sponsored Participant must familiarize its authorized individuals with all of the Sponsored Participant's obligations and assure that they receive appropriate training prior to any use or access to PSX.

- A Sponsored Participant may not permit anyone other than authorized individuals to use or obtain access to PSX.

- A Sponsored Participant must take reasonable security precautions to prevent unauthorized use or access to PSX, including unauthorized entry of information into PSX, or the information and data made available therein. A Sponsored Participant must

understand and agree that it is responsible for any and all orders, trades and other

messages and instructions entered, transmitted or received under identifiers, passwords

and security codes of authorized individuals, and for the trading and other consequences

thereof.

- A Sponsored Participant must acknowledge its responsibility to establish adequate

  procedures and controls that permit it to effectively monitor its employees', agents', and

  customers' use and access to PSX for compliance with the terms of the Sponsorship

  Provisions.

- A Sponsored Participant must pay when due all amounts, if any, payable to the

  Sponsoring Member Organization, PSX, or any other third parties that arise from the

  Sponsored Participant's access to and use of PSX. Such amounts include, but are not

  limited to applicable exchange and regulatory fees.

- The Sponsoring Member Organization must provide PHLX with a Notice of Consent

  acknowledging its responsibility for the orders, executions and actions of its Sponsored

  Participants.

- The Sponsored Participant and its Sponsoring Member Organization must have entered

  into and maintained a User Agreement with PHLX. The Sponsoring Member

  Organization must designate the Sponsored Participant by name in its User Agreement as

  such.

c.   Trading of Securities Pursuant to Unlisted Trading Privileges

With the launch of PSX, PHLX will not resume its listings business. PSX will, however,

trade all NMS stocks on an unlisted trading privileges ("UTP") basis; accordingly, all securities

that it trades will be registered under Section 12(a) of the Act unless they are subject to an

exemption by the Commission that allows them to be listed on a national securities exchange in the absence of such registration. As provided by SEC Rule 12f-5,[16] PHLX may extend unlisted trading privileges to any security for which PHLX has in effect rules providing for transactions in such class or type of security.[17] Accordingly, to support UTP trading of all NMS stocks, existing PHLX Rule 803 is being amended in several respects. First, Rule 803(o) will clearly state that PHLX will not list any securities, and that provisions of Rules 800 through 868 that permit listings will not be effective until PHLX files a proposed rule change under Section 19(b)(2) of the Act to amend its rules to make any changes needed to comply with SEC Rule 10A-3[18] and to incorporate additional qualitative listing standards, and such proposed rule change is approved by the Commission. Second, PHLX is adopting new standards for securities linked to the performance of indexes and commodities (including currencies) and managed fund shares, to reflect the fact that PHLX may engage in UTP trading of these securities,[19] and is

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[16]   17 C.F.R. 240.12f-5.

[17]   Notably, with respect to new derivative securities products (as defined in SEC Rule 19b-4(e), 17 C.F.R. 240.19b-4(e)) trading on the Exchange, Rule 803(o) requires the distribution of an information circular that includes information on the (1) the special risks of trading the new derivative securities product ("NDSP"); (2) the Exchange's rules that will apply to the NDSP, including the suitability rule (proposed Rule 763); (3) information about the dissemination of value of the underlying assets or indexes; and (4) the risk of trading during the period from 9:00 a.m. to 9:30 a.m. and from 4:00 p.m. to 5:00 p.m. due to the lack of calculation or dissemination of the underlying index value, the Intraday Indicative Value, the Indicative Optimized Portfolio Value or other comparable estimate of the value of a share of the NDSP. Rule 803(o) also requires that members and member organizations adhere to applicable prospectus delivery requirements of the Securities Act of 1933, and requires that the Exchange enter into comprehensive surveillance sharing agreements with markets trading components of the index or portfolio on which the NDSP is based to the same extent as the listing market of the NDSP.

[18]   17 C.F.R. 240.10A-3.

[19]   Rule 803(m) and (n) (as proposed to be amended). As with other standards, however, PHLX will not list these securities until the filing and approval of a proposed rule change to authorize such listing.

modifying Rule 803(f) (Other Securities) to adopt continued listing standards that would be applicable to securities listed under that provision if PHLX resumed its listing business and that contain provisions that are complementary to the new standards for securities linked to commodities. Third, PHLX is deleting current Rules 803(m) and (n), which contain standards for index-linked exchangeable notes and index-linked securities; these security types are covered more comprehensively by the adoption of a standard for securities linked to the performance of indexes and commodities (including currencies). Fourth, PHLX is deleting certain restrictions in Rule 803(o) on the activities of market makers, since PSX's market structure will not allow for a class of market makers.

PHLX is also adopting Rule 3230 to establish additional rules to govern UTP trading of Commodity-Related Securities on PSX. The term "Commodity-Related Security" includes any security that is issued by a trust, partnership, commodity pool or similar entity that invests, directly or through another entity, in any combination of commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives, or the value of which is determined by the value of commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives. The term "commodity" has the meaning given to it under the Commodity Exchange Act. The rule provides that members and member organizations must provide all purchasers of a newly issued Commodity-Related Security a prospectus for such Commodity-Related Security.[20] The rule further provides that unless otherwise noted, a Commodity-Related Security is eligible for trading during all PSX market sessions (i.e. from 9:00 a.m. through 5:00 p.m.) if member

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[20] Provisions from the corresponding NASDAQ rule, Rule 4630, that govern the conduct of market makers in Commodity-Related Securities have been omitted because PSX will not have market makers.

organizations comply with Rule 3231 when accepting Commodity-Related Security orders for execution in the pre-market session (9:00 a.m. through 9:30 a.m.) or post-market session (4:00 p.m. through 5:00 p.m.).

Rule 3231 provides that no member organization may accept an order from a customer for execution in the pre-market session or post-market session without disclosing to such customer that extended hours trading involves material trading risks, including the possibility of lower liquidity, high volatility, changing prices, unlinked markets, an exaggerated effect from news announcements, wider spreads and any other relevant risk. The absence of an updated underlying index value or intraday indicative value is an additional trading risk in extended hours for Derivative Securities Products (as defined in Rule 3100). With these changes, as well as the adoption of the other rules contained in this filing, PHLX believes that it will have rules in place to allow the UTP trading of all NMS stocks.

d.   Entry and Processing of Orders

Only orders for NMS stocks may be entered and executed through PSX.[21] PSX is the only venue on the Exchange for the entry and execution of orders in NMS stocks.[22] Participants may submit multiple orders at multiple price levels, which PSX will manage and display, consistent with the parameters of each order.[23] PSX will time-stamp each order upon receipt, although as discussed below, the time stamp does not determine the order's ranking for execution purposes.[24] The System does not allow Participants to display orders on an

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[21]   Proposed Rule 3305(a)(1).

[22]   Id.

[23]   Proposed Rule 3306.

[24]   Id.

attributable basis.[25] However, orders may be entered either as Displayed Orders, in which case they will be displayed as individual orders, each with an identical anonymous identifier, in market data disseminated by PSX concerning resting orders, or may be entered as Non-Displayed Orders, in which case they will not be displayed but nevertheless remain available for potential execution against incoming orders.[26]

Displayed Orders will be displayed to Participants through a system book feed. In addition, the aggregate size of all orders at the best price to buy and sell resident in the System will be transmitted for display to the appropriate network processor unless the aggregate size is less than one round lot.[27] However, Non-Displayed Orders and reserve size will not be displayed.[28]

Marketable orders are directed to resting orders for execution. Non-marketable orders are made available for execution by incoming orders, and either displayed or not displayed, as directed by the entering party. Upon entry of a marketable order, PSX will identify the order(s) against which the incoming order will be executed, based on the algorithm described below. The System will automatically execute against such orders and send the relevant Participant(s) an execution report.

e.   Order Types and Time-in-Force Designations

An order may be of a size up to 999,999 shares[29] and must indicate whether it is a buy, long sale, or short sale.[30] The minimum increment for orders priced at $1.00 or above will be

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[25]   Proposed Rule 3301(a).

[26]   Proposed Rule 3301(e).

[27]   Proposed Rule 3306(c)(1) and (2).

[28]   Proposed Rule 3306(c)(3).

[29]   Proposed Rule 3301(g).

$0.01.[31] The minimum increment for orders priced below $1.00 will be $0.0001.[32] All orders are firm and automatically executable for their displayed and non-displayed size in the System.[33] The System will operate from 9:00 a.m. through 5:00 p.m. Eastern Time, and except as noted below, all orders types and times-in-force may be entered during that period.[34] PSX will not have any specialized opening or closing processes. Rather, the System will be open for order entry at 9:00 a.m., and will immediately start processing orders as they are entered.[35]

The following order types will be available in PSX:[36]

- "Limit Orders" are orders to buy or sell a stock at a specified price or better.

- "Pegged Orders" are orders that, after entry, have their price automatically adjusted by the System in response to changes in either the PSX inside bid or offer or the best bid or offer in the national market system, as appropriate. A Pegged Order can specify that its price will equal the inside quote on the same side of the market ("Primary Peg"), the opposite side of the market ("Market Peg"), or the midpoint of the national best bid and offer ("Midpoint Peg"). A Pegged Order may have a limit price beyond which the order shall not be executed. In addition, the Primary Peg and Market Peg Orders may also establish their pricing relative to the appropriate bids or offers by the selection of one or more offset amounts that will adjust the price of the order by the offset amount selected. A Midpoint Peg Order is priced based upon the national best bid and offer, excluding the

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[30]   Proposed Rule 3305.

[31]   Proposed Rule 3213(a).

[32]   Id.

[33]   Proposed Rule 3213(b).

[34]   Proposed Rules 3217 and 3306(a)(3).

[35]   Proposed Rule 3302.

[36]   Proposed Rule 3301(e) and (f).

effect that the Midpoint Peg Order itself has on the inside bid or inside offer. Midpoint

Peg Orders will never be displayed. A Midpoint Peg Order may be executed in sub-

pennies if necessary to obtain a midpoint price. A Pegged Order may be entered only

between 9:30 a.m. and 4:00 p.m.[37]

- "Minimum Quantity Orders" are orders that require that a specified minimum quantity of

  shares be obtained, or the order is cancelled. Minimum Quantity Orders may only be

  entered with a time-in-force designation of System Hours Immediate or Cancel.

- "Intermarket Sweep Orders" or "ISOs" are limit orders that are executed by the System at

  multiple price levels, without consideration of protected quotations of other market

  centers within the meaning of Rule 600(b) of Regulation NMS under the Act.[38]

  Simultaneously with the routing of an ISO to the System, one or more additional limit

  orders, as necessary, must be routed by the entering party to execute against the full

  displayed size of any protected bid or protected offer (as defined in Rule 600(b) of

  Regulation NMS under the Act) in the case of a limit order to sell or buy with a price that

  is superior to the limit price of the limit order identified as an ISO. These additional

  routed orders must also be identified as ISOs.

- "Price to Comply Orders" are orders that if, at the time of entry, would lock or cross the

  quotation of an external market, the order will be priced to the current low offer (for bids)

  or to the current best bid (for offers) and displayed at a price one minimum price

  increment lower than the offer (for bids) or higher than the bid (for offers). The

  displayed and undisplayed prices of a Price to Comply order may be adjusted once or

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[37] Proposed Rule 3305(a)(1)(C).

[38] 17 C.F.R. 242.600(b).

multiple times depending upon the method of order entry and changes to the prevailing national best bid or offer.

- "Post-Only Orders" are orders that if, at the time of entry, would lock an order on the System, the order will be re-priced and displayed by the System to one minimum price increment (i.e., $0.01 or $0.0001) below the current low offer (for bids) or above the current best bid (for offers).

- "Non-Displayed Orders" are limit orders that are not displayed in the System, but nevertheless remain available for potential execution against all incoming orders until executed in full or cancelled. All orders that are not designated as Non-Displayed Orders will be displayed, but without attribution to the entering Participant.

- In addition to the any of the foregoing designations, an order may also be designated as a "Reserve Order." Reserve Orders have both a round-lot displayed size and an additional non-displayed share amount. Both the displayed and non-displayed portions of the Reserve Order are available for potential execution against incoming orders. If the round-lot displayed portion of a Reserve Order is reduced to less than a normal unit of trading, the System will replenish the display portion from reserve up to at least a single round-lot amount.

The following times-in-force will be available in PSX.[39] Except as noted above in connection with Minimum Quantity Orders, any time-in-force may be combined with any order type.

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[39]   Proposed Rule 3301(h).

- "System Hours Immediate or Cancel" or "SIOC" means that if, after entry into the System, an order (or a portion thereof) is not marketable, the order (or unexecuted portion thereof) will be canceled and returned to the entering Participant.

- "System Hours Day" or "SDAY" means that if, after entry into the System, an order is not fully executed, the order (or the unexecuted portion thereof) will remain available for potential display and/or execution from 9:00 a.m. until 5:00 p.m. Eastern Time on the day it was submitted unless cancelled by the entering party.

- "System Hours Expire Time" or "SHEX" means that if, after entry into the System, an order is not fully executed, the order (or the unexecuted portion thereof) will remain available for potential display and/or execution for the amount of time specified by the entering Participant (up until 5:00 p.m. on the day entered) unless canceled by the entering Participant.

- "Good-til-market close" or "GTMC" means that if, after entry into the System, an order is not fully executed, the order (or unexecuted portion thereof) will remain available for potential display and/or execution until cancelled by the entering party, or until 4:00 p.m., after which it shall be returned to the entering party. GTMC orders entered after 4:00 p.m. will be treated as SIOC orders.

f. Execution of Transactions

Incoming orders that are not marketable against posted interest in the System book will be cancelled or posted to the book, depending on the time-in-force for the order.[40] Incoming marketable orders are executed against orders on the book, and the posted orders are

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[40]   Proposed Rule 3301(h).

decremented accordingly.[41] To determine the allocation of incoming marketable orders against orders on the book, the System uses a price/display/pro-rata allocation to size that is designed to encourage Participants to display large orders in transparent markets, thereby enhancing the quality of price discovery processes.[42] The algorithm executes trading interest in the System in the following order:

- Price—Better priced trading interest will be executed ahead of inferior-priced trading interest.

- Display—Displayed Orders at a particular price with a size of at least one round lot will be executed ahead of Non-Displayed Orders, the reserve portion of Reserve Orders, and odd-lot orders at the same price. Thus, an order receives priority to the extent of the Participant's willingness to display liquidity: undisplayed liquidity receives lower priority.

- Pro-Rata Allocation to Size Among Displayed Orders With a Size of One Round Lot or More—As among equally priced Displayed Orders with a size of at least one round lot, the System will allocate round lot portions of incoming executable orders to displayed trading interest within the System pro rata based on the size of the Displayed Orders. Portions of an order that would be executed in a size other than a round lot if they were allocated on a pro rata basis will be allocated for execution against available displayed trading interest on the basis of a random function that assigns probability of execution based on the size of displayed interest. For example, if Displayed Orders to buy at 10 reside on the PSX book with sizes of 6,000 (Participant A) and 4,000 (Participant B), and

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41   Proposed Rule 3307(a)(2).

42   Proposed Rule 3307(a)(1).

an incoming order to sell 1,100 at 10 comes into the System, the System will allocate 600

shares of the incoming order to Participant A and 400 shares of the incoming order to

Participant B. The remaining 100 shares of the incoming order will be allocated on the

basis of a random function that assigns a 60% probability of executing the 100 shares to

Participant A and a 40% probability to Participant B.

- Displayed Odd-Lot Orders—As among equally priced Displayed Orders with a size of

  less than one round lot, the System will allocate incoming orders based on the size of the

  Displayed Orders, but not in pro rata fashion. Thus, a resting order with a size of 90

  shares would get filled in full before an order with size of 50 shares. If there are two or

  more odd lot orders of equal size, the System will determine the order of execution on the

  basis of a random function that assigns each order an equal probability of execution.

- Pro-Rata Allocation to Size Among Non-Displayed Interest With a Size of One Round

  Lot or More—As among equally priced Non-Displayed Orders and the reserve portion of

  Reserve Orders (collectively, "non-displayed interest") with a size of at least one round

  lot, the System will allocate round lot portions of incoming executable orders to non-

  displayed interest within the System pro rata based on the size of non-displayed interest.

  Portions of an order that would be executed in a size other than a round lot if they were

  allocated on a pro rata basis will be allocated for execution against available non-

  displayed interest on the basis of a random function that assigns probability of execution

  based on the size of non-displayed interest.

- Non-Displayed Odd-Lot Orders—As among equally priced Non-Displayed Interest with

  a size of less than one round lot, the System will allocate incoming orders based on the

  size of the Non-Displayed Interest, but not in pro rata fashion. Thus, a larger odd-lot

order would be filled before a smaller odd-lot order. If there are two or more odd lot

orders of equal size, the System will determine the order of execution on the basis of a

random function that assigns each order an equal probability of execution.

An incoming order with a price that crosses the price of a posted order will execute at the

price of the posted order. Accordingly, any potential price improvement resulting from an

execution in the System will accrue to taker of liquidity.[43] For example, if a buy order resides

on the PSX book at 10 and an incoming sell order priced at 9 comes into the System, the orders

will execute at 10, with the seller getting $1.00 price improvement.

g.   Reporting, Clearance and Settlement; Anonymity

As provided by Rule 3309, executions occurring as a result of orders matched on PSX

shall be reported by PHLX to an appropriate consolidated transaction reporting system. The

System will identify trades executed pursuant to an exception to or exemption from Rule 611 of

Regulation NMS in accordance with specifications approved by the operating committee of the

relevant national market system plan for an NMS stock. If a trade is executed pursuant to both

the ISO exception of Rule 611(b)(5) or (6) of Regulation NMS and the self-help exception of

Rule 611(b)(1) of Regulation NMS, such trade shall be identified as executed pursuant to the

ISO exception. PHLX will promptly notify PSX Participants of all executions of their orders as

soon as the Exchange is notified that such executions have taken place.

For each execution, PSX will submit a transaction report using PHLX's existing "X"

market identifier. The transaction reports produced by the System will indicate the price and size

of the transaction, but will not reveal contra party identities.[44] PHLX will reveal a Participant's

identity in the following circumstances: (i) when National Securities Clearing Corporation

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[43]   Proposed Rule 3307(a)(3).

[44]   Proposed Rule 3310.

("NSCC") ceases to act for a Participant, or the Participant's clearing firm, and NSCC determines not to guarantee the settlement of the Participant's trades; (ii) for regulatory purposes or to comply with an order of an arbitrator or court; (iii) if both Participants to the transaction consent; or (iv) unless otherwise instructed by a member organization, PHLX will reveal to a member organization, no later than the end of the day on the date an anonymous trade was executed, when the member organization's order has been decremented by another order submitted by that same member organization.

Transactions will be cleared and settled through NSCC and Depository Trust Corporation ("DTC"), using an exchange omnibus account established at NSCC.[45] All Participants must be members of NSCC, or clear their trades through a clearing firm that is both a member organization of PHLX and a member of NSCC. Member organizations failing to maintain the required clearing arrangements may be removed from access to PSX until such time as a clearing arrangement is reestablished.[46] If a Participant, or a clearing member acting on a Participant's behalf, is reported as constituting a side of a System trade, the Participant or the clearing member must honor the trade on the scheduled settlement date.[47]

h.   Trading Halts and Clearly Erroneous Transactions

PSX's provisions on trading halts will mirror those of the NASDAQ Market Center, but will include only those provisions pertinent to securities traded on an unlisted trading privileges basis.

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[45]   Proposed Rule 3218. In the event that a registered clearing agency other than NSCC began offering continuous net settlement services, participants would also be permitted to use that clearing agency rather than NSCC.

[46]   Proposed Rule 3228.

[47]   Proposed Rule 3227.

- PSX may halt trading on PSX of a security listed on another exchange: (i) during a trading halt imposed by such exchange to permit the dissemination of material news; or (ii) when such exchange imposes a trading halt in that security because of an order imbalance or influx ("operational trading halt").[48]

- PSX may halt trading in an index warrant whenever regulatory staff concludes that such action is appropriate in the interests of a fair and orderly market and to protect investors. Among the factors that may be considered are the following: (i) trading has been halted or suspended in underlying stocks whose weighted value represents 20% or more of the index value; (ii) the current calculation of the index derived from the current market prices of the stocks is not available; or (iii) other unusual conditions or circumstances detrimental to the maintenance of a fair and orderly market are present.[49]

- In the case of trust shares, index fund shares, managed fund shares or trust issued receipts, a series of commodity-related securities, securities representing interests in unit investment trusts or investment companies, or any other derivative security (collectively, "Derivatives Security Products") for which an underlying index, indicative optimized portfolio value, intraday indicative value, net asset value, disclosed portfolio, or other comparable estimate of the value of a share is disseminated, PSX will halt trading if there is a temporary interruption in the calculation or wide dissemination of the value. PSX will maintain the trading halt until such time as trading resumes in the listing market.[50] Trading may continue in the case of interruptions that occur outside of regular market hours. However, if an interruption occurs or continues during regular market hours and a

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[48]   Proposed Rule 3100(a)(1).

[49]   Proposed Rule 3100(a)(2).

[50]   Proposed Rule 3100(a)(3).

halt is called by the listing market, or if a halt occurs after the close of regular market hours and continues the following day, the affected security will be halted and remain halted until the listing market resumes trading.[51]

- PSX will halt trading in a Derivative Security Product for which a net asset value or disclosed portfolio is disseminated if staff becomes aware that the net asset value or disclosed portfolio is not being disseminated to all market participants at the same time. The halt will remain in effect until the listing market resumes trading.[52]

- Following the initiation of an operational trading halt, PSX Participants may immediately resume order entry and trading.[53] In other cases, Participants must wait until PSX releases the security for resumed trading, at a time announced by PSX through websites and wire services.[54]

- During a pilot period ending on December 10, 2010, if a primary listing market issues an individual stock trading pause in any of the securities covered by the pilot, the Exchange will pause trading in that security until trading has resumed on the primary listing market. If, however, trading has not resumed on the primary listing market and ten minutes have passed since the individual stock trading pause message has been received from the responsible single plan processor, the Exchange may resume trading in such stock. The securities covered by the pilot are those stocks included in the S&P 500® Index.

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[51]   Proposed Rule 3100(b).

[52]   Proposed Rule 3100(a)(3).

[53]   Proposed Rule 3100(a)(1).

[54]   Proposed Rule 3100(c)(2).

- PSX will also halt trading upon SEC request, including in accordance with standing requests for "circuit breaker" market-wide halts in the event of a major market break.[55] PHLX will adopt a rule to govern breaking of clearly erroneous transactions.[56]

As was true for XLE, PHLX's former cash equity trading platform, appeals from determination regarding trades made by PHLX staff will be made to the Options Trade Review Committee ("OTRC"), a committee of industry and non-industry experts established under the PHLX By-Laws. As reflected in Section 10-10 of the By-Laws, 20% of the members of the OTRC must represent PHLX member organizations, but no more than 50% of the committee's members may be employed by firms that are market makers or that derive more than 10% of their revenues from market making. This is identical to the compositional requirements of NASDAQ's Market Operations Review Committee, which performs a comparable function under NASDAQ rules.[57]

i. Regulation NMS Compliance

As provided in Rules 3301(a) and 3306(c)(4), with respect to the operation of PSX, PHLX will implement such systems, procedures, and rules as are necessary to render it capable

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[55] PLHX [sic] Rule 133. As a result of precipitous declines in the prices of certain securities on May 6, 2010, the Commission and the national securities exchanges are currently evaluating the advisability of modifying marketwide rules on trading halts due to extraordinary market volatility, such as those reflected in PHLX Rule 133. PHLX will modify Rule 133 to maintain consistency with corresponding rules of other exchanges as soon as consensus is reached concerning the appropriate marketwide standard.

[56] Proposed Rule 3312. The proposed PSX rule is identical to the rules recently adopted by NASDAQ and other exchanges to provide a consistent and comprehensive framework for reviewing and breaking trades. As a result of precipitous declines in the prices of certain securities on May 6, 2010, however, the Commission and the national securities exchanges are currently evaluating the advisability of further changes to clearly erroneous rules. PHLX will modify its clearly erroneous rule to maintain consistency with the corresponding NASDAQ Stock Market rule as soon as consensus is reached concerning the appropriate marketwide standard.

[57] By-Laws of The NASDAQ Stock Market LLC, Article III, Section 6.

of meeting the requirements for automated quotations,[58] and immediately to identify its quotations as manual whenever it has reason to believe it is not capable of displaying automated quotations. PHLX will adopt policies and procedures for notifying member organizations and other trading centers that it has reason to believe it is not capable of displaying automated quotations or, once manual, that it has restored the ability to display automated quotations and is preparing to identify its quotation as automated. In addition, PHLX will adopt policies and procedures for responding to notices that it receives from other trading centers indicating that they have elected to use the "self-help" exception of Rule 611(b)(1) of Regulation NMS under the Act.[59]

PSX will not route orders to other market centers. Rather, to ensure compliance with Regulation NMS, PSX Rule 3305 provides that in addition to such other designations as may be chosen by a Participant, all orders that are not entered with a time in force of "System Hours Immediate or Cancel"[60] must be designated as an Intermarket Sweep Order, a Pegged Order, a

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[58]   As defined in Rule 600(b) of Regulation NMS under the Act, 17 C.F.R. 242.600(b), the term "quotation" includes the "bid price or the offer price communicated by a member of a national securities exchange … to any broker or dealer, or to any customer, at which it is willing to buy or sell one or more round lots of an NMS security, either as principal or agent." Thus, the term "quotation" includes orders entered into the System by PSX Participants, notwithstanding the fact that PSX will not have market makers with obligations to maintain continuous two-sided quotations. Under Rule 602 of Regulation NMS, brokers and dealers are required to communicate to a national securities exchange or national securities association their best bids, best offers, and quotation sizes. By displaying orders communicated to it by its members and complying with the requirements for automation described in Rule 600(b)(3), PSX will display "automated quotations" within the meaning of that rule, and therefore its best bid and best offer will constitute "protected quotations" entitled to trade-through protection under Regulation NMS.

[59]   17 C.F.R. 242.611(b)(1).

[60]   A "System Hours Immediate or Cancel" order is an immediate or cancel order that may be entered between 9:00 a.m. and 5:00 p.m. Eastern Time, PSX's hours of operation. If a System Hours Immediate or Cancel order (or a portion thereof) is not marketable, the order (or unexecuted portion thereof) is canceled and returned to the entering Participant.

Price to Comply Order, or a Post-Only Order, and all orders will be processed in a manner that avoids trading through protected quotations and avoids locked and crossed markets. Specifically, any orders that are entered into the System that would lock or cross another order in the System will be executed to avoid a lock or cross.[61]

- A System Hours Immediate or Cancel Order is compliant with Regulation NMS because it will not, by its terms, execute or post at a price that would result in a trade-through of a protected quotation or lock or cross another market.

- A Pegged Order is compliant with Regulation NMS because it is continually re-priced to avoid locking or crossing.

- In entering an Intermarket Sweep Order, the Participant represents that it is simultaneously routing one or more additional limit orders, as necessary, to execute against the full displayed size of any protected bid or offer (as defined in Rule 600(b) of Regulation NMS) in the case of a limit order to sell or buy with a price that is superior to the limit price of the order identified as an Intermarket Sweep Order.[62] These additional routed orders must also be identified as Intermarket Sweep Orders. As provided by Regulation NMS, PSX will automatically execute orders identified as Intermarket Sweep Orders. Member organizations will be responsible for ensuring that their use of Intermarket Sweep Orders complies with Regulation NMS, and PHLX's T+1 surveillance program, administered by the Financial Industry Regulatory Authority ("FINRA") under a regulatory services agreement (the "FINRA RSA") will monitor member organizations' use of Intermarket Sweep Orders.

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[61]   Proposed Rule 3213(c). In addition, as discussed below, members may enter orders that are re-priced if they would lock or cross so as to avoid executing.

[62]   Proposed Rule 3301(f)(6).

- If, at the time of entry, a Price to Comply Order would lock or cross the quotation of an external market, the order will be priced to the current low offer (for bids) or to the current best bid (for offers) but displayed at a price one minimum price increment lower than the offer (for bids) or higher than the bid (for offers). Thus, an incoming order priced to execute against the displayed price will receive the superior undisplayed price.[63] The displayed and undisplayed prices of a Price to Comply order may be adjusted once or multiple times depending upon the method of order entry and changes to the prevailing national best bid/best offer.[64]

- If, at the time of entry, a Post-Only Order would lock an order on the System, the order will be re-priced and displayed by the System to one minimum price increment (i.e., $0.01 or $0.0001) below the current low offer (for bids) or above the current best bid (for offers).[65]

By requiring all orders to be entered with one of these designations, PSX will ensure that all orders will either be priced or cancelled in a manner consistent with avoidance of trade-throughs and locked and crossed markets, or will execute as Intermarket Sweep Orders along with other Intermarket Sweep Orders sent to protected quotes. Because PSX will not route to

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[63] For example, if the national best bid and best offer is $9.97 x $10.00, and a participant enters a price to comply order to buy 10,000 shares at $10.01, the order will display at $9.99, but will reside on the System book at $10.00. If a seller then enters an order at $9.99, it will execute at $10.00, up to the full 10,000 shares of the order. Proposed Rule 3301(f)(8).

[64] Proposed Rule 3301(f)(8).

[65] For example, if the System best bid and best offer is $9.97 x $10.00, and a participant enters a Post-Only Order to buy at $10.01, the order will be repriced and displayed at $9.99. If a seller enters an order at $9.96, the order will be repriced and displayed at $9.98. Proposed Rule 3301(f)(10).

other market centers,[66] its policies and procedures under Rule 611(a) under Regulation NMS[67] will contemplate reliance on information provided by the NASDAQ Market Center for purposes of determining whether another trading center is experiencing a failure, material delay, or malfunction of its systems or equipment within the meaning of Rule 611(b)(1).[68]

Rule 3213(c)(2) contains PSX's rules adopted pursuant to SEC Rule 610(d) under Regulation NMS[69] with respect to inter-market locks and crosses. Although the System-enforced requirements with respect to order entry and execution generally prevent locked and crossed markets, adoption of the rule is needed to comply with the requirements of Rule 610(d) and to provide a clear rule barring conduct that could evade the System-enforced requirements, such as entry of an incorrectly marked Intermarket Sweep Order. Terms used in the rule have the meanings assigned to them by Rule 600 under Regulation NMS.[70] Subject to certain exceptions, the Rule 3213(c) provides that member organizations shall reasonably avoid displaying, and shall not engage in a pattern or practice of displaying any quotations[71] that lock or cross a protected quotation, and any manual quotations that lock or cross a quotation previously disseminated pursuant to an effective national market system plan. Exceptions exist for instances where (i) the locking or crossing quotation was displayed at a time when the trading center displaying the locked or crossed quotation was experiencing a failure, material delay, or malfunction of its systems or equipment; (ii) the locking or crossing quotation was displayed at a time when a protected bid was higher than a protected offer in the NMS stock; (iii) the locking or

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66   Proposed Rule 3305(b).

67   17 C.F.R. 242.611(a).

68   17 C.F.R. 242.611(b)(1).

69   17 C.F.R. 242.610(d).

70   17 C.F.R. 242.600.

71   As defined in SEC Rule 600, the term "quotation" includes an order.

crossing quotation was an automated quotation, and the Exchange member organization displaying such automated quotation simultaneously routed an Intermarket Sweep Order to execute against the full displayed size of any locked or crossed protected quotation; and (iv) the locking or crossing quotation was a manual quotation that locked or crossed another manual quotation, and the Exchange member organization displaying the locking or crossing manual quotation simultaneously routed an Intermarket Sweep Order to execute against the full displayed size of the locked or crossed manual quotation. If a member organization displays a manual quotation that locks or crosses a quotation previously disseminated pursuant to an effective national market system plan, such member organization shall promptly either withdraw the manual quotation or route an Intermarket Sweep Order to execute against the full displayed size of the locked or crossed quotation.

j.   Regulatory Framework

Under the FINRA RSA, FINRA will provide a range of regulatory services, including T+1 surveillance, investigation, and enforcement with respect to PHLX rules, arbitration services, and membership services. PHLX will perform other regulatory services, such as real-time market surveillance, using personnel employed by NASDAQ OMX or one of its subsidiaries, including PHLX. NASDAQ OMX, PHLX, NASDAQ, and NASDAQ OMX BX (PHLX, NASDAQ, and NASDAQ OMX BX collectively, the "SRO Subsidiaries") are parties to a regulatory services agreement (the "Intercompany RSA") pursuant to which employees and contractors of each party ("Personnel") may perform regulatory services for each of the SRO Subsidiaries. All regulatory services performed for PHLX under the Intercompany RSA are subject to the direction, authority, and oversight of PHLX's chief regulatory officer ("CRO") and the regulatory oversight committee ("ROC") of its Board of Governors. All Personnel are

subject to the jurisdiction, authority and oversight of the CRO and ROC of PHLX to the extent of the services that they provide to PHLX. Notwithstanding the FINRA RSA and the Intercompany RSA, PHLX retains ultimate legal responsibility for, and control of, functions performed for PHLX under such agreements.

Under the FINRA RSA, FINRA will conduct T+1 market surveillance and examine member organizations to monitor compliance with applicable PHLX and SEC rules. Moreover, many aspects of compliance with PSX rules, such as avoidance of locked and crossed markets and trade throughs, will be enforced by the System itself. PHLX will periodically test operations of PSX to determine that the System is operating in accordance with applicable rules.

PSX will operate out of the same New York metropolitan data center as the NASDAQ Market Center and the NASDAQ OMX BX Equities System, but will use equipment that is separate from the equipment used by those exchanges. In addition, PSX will have a backup data center in the Washington, D.C. metropolitan area. To ensure sufficient capacity with respect to the System, PHLX developed a baseline forecast of volume of usage, which will be updated regularly based on actual volumes. The System will use NASDAQ OMX's flexible INET technology, which is easily scalable to higher volumes through the addition of more equipment in the data center. The System will be protected from unauthorized access through the same robust firewall protections already in use at NASDAQ OMX's data centers.

As provided in proposed Rules 3401-3407, PSX will adopt rules implementing a version of the Order Audit Trail System ("OATS"). PHLX believes that as an affiliate of NASDAQ, it should ensure that its regulatory requirements are generally consistent with those of NASDAQ. Accordingly, PHLX member organizations that are also FINRA members must comply with the FINRA OATS rules requiring daily reporting of audit trail information for transactions in

securities listed on NASDAQ. In addition, as provided in NASDAQ rules, PHLX member

organizations that are not FINRA members must compile and maintain audit trail information for

securities listed on NASDAQ, but are required to transmit this information to FINRA only if

requested.[72] Similarly, if PHLX resumes operations as a listing market in the future, the rule will

require all member organizations to maintain audit trail information for securities listed on

PHLX, and to transmit the information to FINRA upon request, but would not require daily

OATS reporting for such securities. As is true with respect to NASDAQ, OATS data will be

used by PHLX for regulatory purposes only.[73]

Finally, PHLX is adopting rules addressing recommendations to customers (also known

as suitability) and best execution and interpositioning, based on NASD Rules 2310 and 2320.[74]

Member organizations would become subject to these rules by virtue of having public customers,

and brokers with public customers are required to be members of FINRA; accordingly, adoption

of these rules by PHLX could be seen as unnecessary. However, PHLX believes that the

requirements of these rules are sufficiently important that they should be reinforced through

explicit inclusion in the PHLX rulebook.

k. Affiliation with NASDAQ Execution Services, LLC

Although PSX will not route to other market centers, it will receive orders routed to it by

other market centers, including NASDAQ. Nasdaq Execution Services, LLC ("NES") is the

approved outbound routing facility of NASDAQ for cash equities. Rules 4751 and 4758 of

NASDAQ establish the conditions under which NASDAQ is permitted to own and operate NES

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[72]   Proposed Rule 3405.

[73]   See Securities Exchange Act Release No. 53128 (January 13, 2006); 71 FR 3350
         (January 23, 2006) (File No. 10-131).

[74]   Proposed Rules 763 and 764.

in its capacity as a facility of NASDAQ that routes orders from NASDAQ to other market centers. These conditions include requirements that: (1) NES is operated and regulated as a facility of NASDAQ; (2) NES will not engage in any business other than as an outbound router for NASDAQ and any other activities as approved by the Commission;[75] (3) the primary regulatory responsibility for NES lies with an unaffiliated self-regulatory organization; (4) use of NES for outbound routing is optional for other NASDAQ members; and (5) NASDAQ will not route orders to an affiliated exchange, such as PHLX, unless they check the NASDAQ book prior to routing.

In connection with PHLX's resumption of equity trading pursuant to this filing, NASDAQ will file a proposed rule change to modify the last of these conditions to allow it to route all forms of orders, including Directed Orders, to PSX during a twelve-month pilot period. Directed Orders are orders that route directly to other exchanges on an immediate-or-cancel basis without first checking the NASDAQ book for available liquidity. In order to appropriately address concerns previously raised by the Commission regarding the potential for conflicts of interest and informational advantages that may arise from the use of affiliated members to route orders between exchanges owned by a common parent, PHLX is proposing certain restrictions and undertakings.

In order to manage the concerns raised by the Commission regarding conflicts of interest in instances where a member firm is affiliated with an exchange to which it is routing orders, PHLX notes that, with respect to orders routed to PHLX by NES in its capacity as a facility of NASDAQ, NES is subject to independent oversight and enforcement by FINRA, an unaffiliated SRO that is NES's designated examining authority. In this capacity, FINRA is responsible for

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[75]   Because only NASDAQ members may enter orders into NASDAQ, it also follows that routing by NES is conducted only with respect to orders of NASDAQ members.

examining NES with respect to its books and records and capital obligations and also has the

responsibility for reviewing NES's compliance with intermarket trading rules such as SEC

Regulation NMS. In addition, under the FINRA RSA, FINRA staff will review NES's

compliance with PHLX's rules through FINRA's examination program. FINRA and PHLX[76]

will also monitor NES for compliance with PHLX's trading rules, subject, of course, to SEC

oversight of the regulatory program of PHLX and FINRA. PHLX will, however, retain ultimate

responsibility for enforcing its rules with respect to NES.

Furthermore, in order to minimize the potential for conflicts of interest, PHLX and

FINRA will collect and maintain all alerts, complaints, investigations and enforcement actions in

which NES (in its capacity as a facility of NASDAQ, routing orders to PSX) is identified as a

participant that has potentially violated applicable SEC or PHLX rules. PHLX and FINRA will

retain these records in an easily accessible manner in order to facilitate any potential review

conducted by the SEC's Office of Compliance Inspections and Examinations. FINRA will then

provide a report to the PHLX's CRO, on at least a quarterly basis, which (i) quantifies all alerts

(of which PHLX and FINRA become aware) that identify NES as a participant that has

potentially violated PHLX or SEC rules and (ii) quantifies the number of all investigations that

identify NES as a participant that has potentially violated PHLX or SEC rules.[77]

In order to address the Commission's concerns about potential for information

advantages that could place an affiliated member of an exchange at a competitive advantage vis-

à-vis other non-affiliated members, PHLX is proposing Rule 985(c)(2). Rule 985(c)(2) will

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[76]   Personnel performing real-time oversight of equity trading on NASDAQ will also
        perform similar functions with respect to PSX. Such work is performed pursuant to the
        Intercompany RSA under the direction, authority, and oversight of PHLX's CRO and the
        ROC of its Board of Governors.

[77]   PHLX, FINRA, and SEC staff may agree going forward to reduce the number of
        applicable or relevant surveillances that form the scope of the agreed upon report.

require the implementation of policies and procedures that are reasonably designed to prevent

NES from acting on non-public information regarding PHLX systems prior to the time that such

information is made available generally to all members of such entity performing inbound

routing functions. These policies and procedures would include systems development protocols

to facilitate an audit of the efficacy of these policies and procedures.

Specifically, new Rule 985(c)(2) shall provide as follows:

The NASDAQ OMX Group, Inc., which owns NASDAQ Execution Services, LLC and the Exchange, shall establish and maintain procedures and internal controls reasonably designed to ensure that NASDAQ Execution Services, LLC does not develop or implement changes to its system on the basis of non-public information regarding planned changes to Exchange systems, obtained as a result of its affiliation with the Exchange, until such information is available generally to similarly situated members and member organizations of the Exchange in connection with the provision of inbound routing to the Exchange.

In addition, NASDAQ Rule 4758 provides that NES will establish and maintain

procedures and internal controls reasonably designed to adequately restrict the flow of

confidential and proprietary information between NASDAQ and its facilities (including the

NES), and any other entity (including PHLX). The Exchange believes these measures will

effectively address the concerns identified by the Commission regarding the potential for

informational advantages favoring NES vis-à-vis other non-affiliated PHLX members.

2.   Statutory Basis

The Exchange believes that the proposed rule change is consistent with the provisions of

Section 6 of the Act,[78] in general, and with Section 6(b)(1) and (b)(5) of the Act,[79] in particular,

in that the proposal enables the Exchange to be so organized as to have the capacity to be able to

carry out the purposes of the Act and to comply with and enforce compliance by members,

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[78]   15 U.S.C. 78f.

[79]   15 U.S.C. 78f(b)(1), (5).

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member organizations, and persons associated with members and member organizations with provisions of the Act, the rules and regulations thereunder, and the rules of the Exchange; and is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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. PSX will operate in accordance with the high standards that PHLX believes to be in evidence at all of NASDAQ OMX's exchanges, providing its Participants with opportunities to trade NMS stocks through a fair, open, and well-regulated market. Furthermore, PHLX believes that PSX's price-size allocation methodology will promote further development of the national market system by encouraging Participants to display liquidity, thereby contributing more fully to price discovery and providing a counterbalance to increased use of dark trading venues.

        B.   <u>Self-Regulatory Organization's Statement on Burden on Competition</u>

PHLX 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. As a new entrant into the market for executions of NMS stocks, PSX will further enhance competition in this space.

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

Written comments were neither solicited nor received.

III.   <u>Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action</u>

Within 35 days of the date of publication of this notice in the <u>Federal</u> <u>Register</u> or within such longer period (1) as the Commission may designate up to 90 days of such date if it finds

such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which

the self-regulatory organization consents, the Commission will:

      A.   by order approve such proposed rule change, or

      B.   institute proceedings to determine whether the proposed rule change should be

disapproved.

IV.   <u>Solicitation of Comments</u>

Interested persons are invited to submit written data, views and arguments concerning the

foregoing, including whether the proposal is consistent with the Act. Comments may be

submitted by any of the following methods:

<u>Electronic Comments</u>:

- 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 No. SR-Phlx-

  2010-79 on the subject line.

<u>Paper Comments</u>:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities

  and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File No. SR-Phlx-2010-79. 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 Web site viewing

and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC

20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such

filing will also 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 No. SR-Phlx-2010-79 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.[80]

Florence E. Harmon
Deputy Secretary

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[80]   17 CFR 200.30-3(a)(12).