

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53243; File No. SR-Phlx-2005-43)

February 7, 2006

Self-Regulatory Organizations; Philadelphia Stock Exchange, Inc.; Notice of Filing and Order Granting Accelerated Approval to a Proposed Rule Change and Amendments No. 1, 2, and 3 Thereto Relating to Index Option Strike Prices

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 22, 2005, the Philadelphia Stock Exchange, 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 substantially prepared by the Exchange. On December 8, 2005, the Exchange filed Amendment No. 1 to the proposed rule change. On December 9, 2005, the Exchange filed Amendment No. 2 to the proposed rule change. On January 12, 2006, the Exchange filed Amendment No. 3 to the proposed rule change.³ The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons. In addition, the Commission is granting accelerated approval of the proposed rule change, as amended.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Phlx Rule 1101A (Terms of Option Contracts) to indicate that the Exchange may set strike price intervals of \$5 or greater for options on indexes, and may set strike prices at \$2.50 or greater for listed index options or in response to customer

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 3 replaced and superseded the original filing and subsequent amendments in their entireties. Telephone conversation between Jruij Trypupenko, Director and Counsel, New Products Group and Legal Department, Phlx, and Theodore S. Venuti, Attorney, Division of Market Regulation, Commission, on January 26, 2006.

interest or specialist request. The proposal would also delete language that is no longer necessary. The text of the proposed rule change, as amended, is below. Proposed new language is in underlined; proposed deletions are in [brackets].

Rule 1101A.

Terms of Option Contracts

(a) The Exchange shall determine fixed point intervals of exercise prices for index options (options on indexes). Generally, the exercise (strike) price intervals ~~[shall]~~will be [\$2.50 for the three consecutive near-term months,] no less than \$5; provided, that for the fourth month and \$10 for the fifth. However,] the Exchange may determine to list strike prices at no less than \$2.50 intervals [in response to demonstrated customer interest or specialist request] for options on the following indexes (which may also be known as sector indexes):

- (i) PHLX Computer Box Maker Index, if the strike price is less than \$200,
- (ii) PHLX Defense Index, if the strike price is less than \$200,
- (iii) PHLX Drug Index, if the strike price is less than \$200,
- (iv) PHLX Europe Index, if the strike price is less than \$200,
- (v) PHLX Gold/Silver Index, if the strike price is less than \$200,
- (vi) PHLX Housing Index, if the strike price is less than \$200,
- (vii) PHLX Oil Service Index, if the strike price is less than \$200,
- (viii) PHLX Semiconductor Index, if the strike price is less than \$200,
- (ix) PHLX Utility Index, if the strike price is less than \$200,
- (x) PHLX World Energy Index, if the strike price is less than \$200,
- (xi) SIG Investment Managers Index™, if the strike price is less than \$200,
- (xii) SIG Cable, Media & Entertainment Index™, if the strike price is less than \$200,

- (xiii) SIG Casino Gaming Index™, if the strike price is less than \$200,
- (xiv) SIG Semiconductor Equipment Index™, if the strike price is less than \$200,
- (xv) SIG Semiconductor Device Index™, if the strike price is less than \$200,
- (xvi) SIG Specialty Retail Index™, if the strike price is less than \$200,
- (xvii) SIG Steel Producers Index™, if the strike price is less than \$200,
- (xviii) SIG Footwear & Athletic Index™, if the strike price is less than \$200,
- (xix) SIG Education Index™, if the strike price is less than \$200,
- (xx) SIG Restaurant Index™, if the strike price is less than \$200,
- (xxi) SIG Coal Producers Index™, if the strike price is less than \$200,
- (xxii) SIG Oil Exploration & Production Index™, if the strike price is less than \$200,
- (xxiii) PHLX/KBW Bank Index, if the strike price is less than \$200,
- (xxiv) KBW Capital Markets Index, if the strike price is less than \$200,
- (xxv) KBW Insurance Index, if the strike price is less than \$200,
- (xxvi) KBW Mortgage Finance Index, if the strike price is less than \$200,
- (xxvii) KBW Regional Banking Index, if the strike price is less than \$200,
- (xxviii) TheStreet.com Internet Sector, if the strike price is less than \$200,
- (xxix) Wellspring Bioclinical Trials Index™, if the strike price is less than \$200.

The Exchange may also determine to list strike prices at no less than \$2.50 intervals for options on indexes delineated in this rule in response to demonstrated customer interest or specialist request. For purposes of this paragraph, demonstrated customer interest includes institutional (firm) corporate or customer interest expressed directly to the Exchange or through the customer's floor brokerage unit, but not interest expressed by an ROT with respect to trading for

the ROT's own account. [The Exchange may also determine to list strike prices at wider intervals.]

(b) through (c), Commentary - No change.

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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 had received on the proposed rule change. The text of these statements may be examined at the places specified in Item III below. The Phlx 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 provide the Exchange with the ability to set strike price intervals for options on indexes at \$2.50 or greater if the strike price is less than \$200, in keeping with Exchange needs, specialist and customer requests, and market conditions and practices.

Phlx Rule 1101A currently indicates the Exchange generally shall determine set strike intervals for options on indexes, which are also known as index options or sector index options, as follows: \$2.50 for three consecutive near-term months, \$5.00 for the fourth month, and \$10.00 for the fifth month.

The Exchange has found that the index strike pricing formulation, which generally requires set pricing intervals according to whether options are in the first three consecutive

months, the fourth month, or the fifth month, does not afford the flexibility to set strike prices at appropriate intervals commensurate with market conditions and index prices set by other exchanges, often for similar products.⁴ Moreover, Phlx specialists and customers have expressed on numerous occasions that the current index strike pricing approach is too restrictive and does not allow for efficient pricing of index options, thereby putting them at a competitive disadvantage.

The Exchange therefore proposes to amend Phlx Rule 1101A to indicate that the Exchange would be permitted to determine fixed point strike price intervals for index options (also known as sector index options) as follows:

- no less than \$5.00,
- provided that the Exchange may list strike prices at no less than \$2.50 intervals (a) in those index options delineated in Phlx Rule 1101A(a) where the strike prices are less than \$200, and (b) in the same index options delineated in this rule in response to demonstrated customer interest or specialist request.

For purposes of Phlx Rule 1101A, “demonstrated customer interest or specialist request” includes institutional (firm) corporate or customer interest expressed directly to the Exchange or through the customer's floor brokerage unit, but does not include interest expressed by a registered options trader (“ROT”) with respect to trading for the ROT's own account.

The Exchange believes that proposed Phlx Rule 1101A, as amended, would provide the flexibility needed for more efficient index options pricing, would tend to maximize trading

⁴ The Exchange has recently amended current Phlx Rule 1101A in an attempt to gain needed flexibility. See Securities Act Release No. 49311 (February 24, 2004), 69 FR 9673 (March 1, 2004) (SR-Phlx-2003-72).

opportunities, and would be analogous in function to index strike pricing rules of other option exchanges.⁵

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with Section 6(b) of the Act,⁶ in general, and furthers the objectives of Section 6(b)(5) of the Act,⁷ in particular, in that it is designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transaction 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. The Exchange believes that the proposed rule should allow the Exchange to set strike prices at levels that would maximize pricing efficiency and trading opportunities.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change would impose any burden on competition that is 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.

⁵ See e.g., Chicago Board Options Exchange Rule 24.9 and International Securities Exchange Rule 2009.

⁶ 15 U.S.C. 78f(b).

⁷ 15 U.S.C. 78f(b)(5).

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, 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-2005-43 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-Phlx-2005-43. 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, 100 F Street, NE, 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 publicly available. All submissions should refer to File Number SR-Phlx-2005-43 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

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder, applicable to a national securities exchange.⁸ In particular, the Commission believes that the proposed rule change is consistent with Section 6(b)(5) of the Act,⁹ which requires among other things, that the rules of the Exchange are designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transaction 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. The Commission believes that the proposed rule change should provide the Exchange with the flexibility to efficiently price index options by allowing the Exchange to list \$2.50 strike price intervals only on certain index options delineated in this rule.

The Phlx has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after publication of notice thereof in the Federal Register. The Commission notes that other option exchanges have similar rules permitting the listing of

⁸ In approving this proposal, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁹ 15 U.S.C. 78f(b)(5).

\$2.50 strike price intervals on certain delineated index options.¹⁰ The Commission believes that granting accelerated approval of the proposal should allow the Phlx to conform its rules to those of other option exchanges without delay. Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,¹¹ for approving the proposed rule change, as amended, prior to the thirtieth day after the date of publication of notice thereof in the Federal Register.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹² that the proposed rule change (SR-Phlx-2005-43) and Amendments No. 1, 2, and 3 thereto be, and hereby are, approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹³

Nancy M. Morris
Secretary

¹⁰ See supra note 5.

¹¹ 15 U.S.C. 78s(b)(2).

¹² 15 U.S.C. 78s(b)(2).

¹³ 17 CFR 200.30-3(a)(12).