SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-79805; File No. SR-Phlx-2016-82)

January 17, 2017

Self-Regulatory Organizations; NASDAQ PHLX LLC; Notice of Filing of Amendment No. 1, and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to Adopt a New Exception in Phlx Rule 1000(f) for Sub-MPV Split-Price Orders

I.    Introduction

On August 3, 2016, NASDAQ PHLX LLC (the "Exchange" or "Phlx") filed with the

Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the

Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] a proposed rule change to

provide an additional exception to the mandatory use of the Exchange's Floor Broker

Management System ("FBMS") pursuant to Rule 1000(f)(iii) to permit Floor Brokers to execute

certain sub-minimum price variation ("sub-MPV") split-price orders in the trading crowd.  The

proposed rule change was published for comment in the Federal Register on August 22, 2016.[3]

On October 3, 2016, the Commission extended the time period within which to approve the

proposed rule change, disapprove the proposed rule change, or institute proceedings to determine

whether to approve or disapprove the proposed rule change to November 20, 2016.[4]  On

November 17, 2016, the Commission instituted proceedings under Section 19(b)(2)(B) of the Act

to determine whether to approve or disapprove the proposed rule change.[5]  On December 9,

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

[2]    17 CFR 240.19b-4.

[3]    See Securities Exchange Act Release No. 78593 (August 16, 2016), 81 FR 56724 ("Notice").

[4]    See Securities Exchange Act Release No. 79023 (October 3, 2016), 81 FR 69877 (October 7, 2016).

[5]    See Securities Exchange Act Release No. 79345 (November 17, 2016), 81 FR 84629 (November 23, 2016).

2016, the Exchange filed Amendment No. 1 to the proposed rule change.[6] The Commission

received no comments on the proposed rule change. This order provides notice of filing of

Amendment No. 1 and approves the proposal, as modified by Amendment No. 1, on an

accelerated basis.

II.    Description of the Proposal[7]

    A.  Background

Currently, Phlx Rule 1000(f) requires that all Exchange options transactions be executed

in one of the following three ways:  "(i) [a]utomatically by the Exchange Trading System

pursuant to Rule 1080 and other applicable options rules; (ii) by and among members in the

Exchange's options trading crowd none of whom is a Floor Broker; or (iii) through the Options

[FBMS] for trades involving at least one Floor Broker."[8]  Although a Floor Broker may represent

orders in the trading crowd, a Floor Broker is not permitted to execute an order in the trading

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[6]    Amendment No. 1 updated the original filing to:  (1) reflect the implementation of the Exchange's new Floor Broker Management System ("FBMS 3") on November 3, 2016; (2) modify proposed Rule 1000(f)(iii)(D) to provide additional detail regarding how certain split- price orders will be rounded; and (3) offer three examples to illustrate how split-price orders will be handled pursuant to the proposed exception.  Amendment No. 1 replaced the original proposed rule change in its entirety.  To promote transparency of its proposed amendment, when Phlx filed Amendment No. 1 with the Commission, it also submitted Amendment No. 1 as a comment letter to the file, which the Commission posted on its website and placed in the public comment file for SR-Phlx- 2016-82 (available athttps://www.sec.gov/comments/sr-phlx-2016-82/phlx201682-1.pdfhttps://www.sec.gov/comments/sr-cboe-2016-071/cboe2016071.shtml).  The Exchange also posted a copy of its Amendment No. 1 on its website (http://nasdaqphlx.cchwallstreet.com/NASDAQPHLX/pdf/phlx-filings/2016/SR-Phlx-2016-82_Amendment_1.pdf) when it filed Amendment No.1 with the Commission.

[7]    A more detailed description of the proposal appears in the Notice and in Amendment No. 1.

[8]    See Phlx Rule 1000(f).

crowd unless one of three exceptions applies.[9] The exceptions to the mandatory use of the

FBMS[10] are set forth in Phlx Rule 1000(f)(iii). These exceptions allow a Floor Broker to execute

a transaction in the trading crowd (rather than through the FBMS) if: (i) there is a problem with

Exchange's systems; (ii) the Floor Broker is executing the trade pursuant to Phlx Rule 1059

("Accommodation Transactions") or Phlx Rule 1079 ("Flex Index, Equity and Currency

Options"); or (iii) the transaction involves a multi-leg order with more than 15 legs.[11]

B. Split-Price Order Exception Proposal

Phlx Rule 1014(g)(i)(B) provides a priority rule regarding open outcry split-price

transactions in equity options and options overlying ETFs to permit a member who is responding

to an order for at least 100 contracts who buys (sells) at least 50 contracts at a particular price to

have priority over all others in purchasing (selling) up to an equivalent number of contracts of

the same order at the next lower (higher) price without being required to yield to existing

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[9]     See Phlx Rule 1000(f)(iii).

[10]    The original FBMS ("FBMS 1") began operating in 2005. The Exchange retired FBMS
       1 on March 31, 2016 after operating it concurrently with the Exchange's enhanced FBMS
       ("FBMS 2"), which was made available on March 7, 2014. As of April 1, 2016, the
       Exchange only operated FBMS 2. See Notice, supra note 3, at 56725. On November 3,
       2016, the Exchange implemented FBMS 3 and retired FBMS 2. According to the
       Exchange, FBMS 3 is currently the sole operating version of FBMS on the Exchange.
       See Amendment No. 1, supra note 6, at 3 and 8-10. References throughout this Order to
       "FBMS" refer to FBMS 3.

[11]    See Notice, supra note 3, at 56726. See also Phlx Rule 1000(f)(iii)(A)-(C). According to
       the Exchange, each time a Floor Broker uses one of the current exceptions to Phlx Rule
       1000(f)(iii), the Floor Broker is required by Phlx Rule 1063(e)(ii), to record the
       information required by Phlx Rule 1063(e)(i) on paper trade tickets. The Exchange
       further represents that a Floor Broker may only represent an order for execution that has
       been timestamped with the time of entry on the trading floor. In addition, according to
       the Exchange, once an execution occurs, the trade ticket must be stamped with the time
       of execution of such order. See Notice, supra note 3, at 56726 and Amendment No. 1,
       supra note 6, at 11.

customer interest in the limit order book.[12] Absent Phlx Rule 1014(g)(i)(B), such orders would be required to yield priority. The Exchange states that "[t]he purpose behind the split-price priority exception was 'to bring about the execution of large orders, which by virtue of their size and the need to execute them at multiple prices may be difficult to execute without a limited exception to the priority rules.'"[13]

According to the Exchange, split-price orders are currently processed using either FBMS or paper tickets. The use of FBMS or paper tickets depends on whether the split-price order can be evenly split using simple calculations or whether the split-price order involves non-even integers and sub-MPV price points, which requires a more complicated computation to determine the number of contracts to trade at two different price points.[14] The Exchange represents that FBMS does not have the capability to calculate specific volumes at two different MPV prices for split-price orders placed in a sub-MPV price.[15] To compensate for this system limitation, the Exchange is proposing to amend Phlx Rule 1000(f)(iii) to add a new exception from the mandatory use of the FBMS that would allow Floor Brokers to execute certain split-price orders in the trading crowd that would be validated by Phlx surveillance staff for compliance with applicable priority and trade-through rules.

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[12] See Notice, supra note 3, at 56726 (citing Securities Exchange Act Release No. 51820 (June 10, 2005), 70 FR 35759 (June 21, 2005) (SR-Phlx-2005-28)) (approving pilot). See also Securities Exchange Act Release No. 55993 (June 29, 2007), 72 FR 37301 (July 9, 2007) (SR-Phlx-2007-44) (permanent approval)).

[13] See Notice, supra note 3, at 56726. Floor Brokers that avail themselves of the split-price priority rule are obligated to ensure compliance with Section 11(a) of the Exchange Act. See Amendment No. 1, supra note 6, at 12.

[14] See Notice, supra note 3, at 56726. Today, when the computation is more complicated, surveillance staff allows a Floor Broker to execute split-price orders involving non-even integers and sub-MPV price points in open outcry using paper tickets pursuant to Phlx Rule 1000(f)(iii)(A). See id.

[15] See id. at 56727. See Amendment No. 1, supra note 6, at 20.

Accordingly, the Exchange is proposing in Phlx Rule 1000(f)(iii)(D) to allow the following split-price orders to be executed in the trading crowd: (1) simple orders not expressed in the applicable sub-MPV and that cannot be evenly split into two whole numbers to create a price at the midpoint of the MPV; and (2) complex and multi-leg orders with at least one option leg with an odd-numbered volume that must trade at a sub-MPV price or one leg that qualifies under (1) above.[16]

The Exchange represents that this exception "is anticipated to be implemented infrequently and in the following [three] ways."[17] Under the first scenario, a Floor Broker knows that, due to a system limitation, a sub-MPV split-price order cannot be handled by FBMS.[18] In this case, the Floor Broker would comply with Phlx Rule 1063(e), expose the order in the trading crowd, and request the use of the proposed exception from the Options Exchange Official ("Official").[19] The Official would confirm his or her understanding of the order and the availability of the exemption, and if the Floor Broker's request is determined to be valid based on the split-price calculation, announce to application of the exemption to the Floor Broker and the trading crowd.[20] After the Floor Broker negotiates and consummates the trade in the trading crowd, the Floor Broker would timestamp the paper ticket at the time the trade is consummated in the trading crowd, which would become the time of execution for the trade.[21] The

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[16]    See Notice, supra note 3, at 56724.

[17]    See Amendment No. 1, supra note 6, at 13.

[18]    See id.

[19]    See id.

[20]    See id. at 13-14.

[21]    See id. at 14. The Exchange notes that, typically, the Official captures a timestamp reflecting the time the Official observed that the trade was consummated in the trading crowd and may, in its discretion, substitute this timestamp for the timestamp recorded by

consummated trade would then be submitted to the Official to validate for compliance with

priority and trade-through rules. If compliant, the Official would permit the Floor Broker to

submit the manual split-price trade, via paper ticket, for trade reporting.[22]

The second scenario involves a situation in which a Floor Broker submits a split-price

order to FBMS, but the Floor Broker does not realize that FBMS cannot handle the order

because the price is outside the MPV.[23] In this case, the Floor Broker would comply with Phlx

Rule 1063(e), expose the order in the trading crowd, and, upon consummation of the transaction,

submit the order to FBMS for execution. Because FBMS cannot calculate the split-price for the

order, FBMS would reject the submission and the Floor Broker would receive a rejection

message.[24] Upon the receipt of this message, the Floor Broker would inform the Official that

FBMS rejected the split-price order. The Official would then review the terms of the

consummated trade and, using the timestamp captured by the Floor Broker or Official,[25] validate

the consummated trade for compliance with priority and trade-through.[26] If the consummated

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the Floor Broker at the time of consummation. See id.

[22]  See Amendment No. 1, supra note 6 , at 14-15. According to the Exchange, the paper
      ticket will reflect the timestamp captured by the Floor Broker or (as described above) the
      Official, which will reflect the time the trade was consummated in the trading crowd.
      See id.

[23]  See id. at 15.

[24]  See id. According to the Exchange, this might occur if the order is not priced in the
      minimum price increment and consequently FBMS would reject the trade. See id.

[25]  According to the Exchange, the Floor Broker captures a timestamp for the time that the
      Floor Broker submitted the proposed execution in FBMS. The Exchange further
      represents that, as in scenario 1, the Official also would typically capture a timestamp
      reflecting the time that the Official observed the Floor Broker's attempt to execute the
      transaction in FBMS. Surveillance staff may, in its discretion, substitute this timestamp
      for the timestamp recorded by the Floor Broker as the time that the trade was
      consummated. See Amendment No. 1, supra note 6, at 15. See also supra note 21.

[26]  See id. at 15-16.

trade is compliant, the Official would permit the Floor Broker to submit the manual split-price trade, via paper ticket reflecting the timestamp captured by the Floor Broker (or Official), for trade reporting.[27]

The third scenario is similar to the second scenario; however, neither the Floor Broker nor the Official captures a reliable time that the consummated trade was submitted to FBMS for execution.[28] In this case, the Official would require the Floor Broker to "re-trade" the order using a paper ticket in the sequence described in the first scenario above.[29]

The Exchange also proposes that, in addition to split-price orders executed pursuant to proposed Phlx Rule 1000(f)(iii)(D), Phlx surveillance staff would approve all executions submitted under Phlx Rule 1000(f)(iii) to validate that such executions abide by applicable priority and trade-through rules.[30] The Exchange also proposes to round prices if necessary to execute the trade at the MPV, but only to the benefit of a customer order, or, where multiple customer orders are involved, for the customer order that is earliest in time.[31] Where no customer order is involved, the rounding of prices will be applied to the non-customer order that is earliest in time.[32]

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[27]   See id. at 16.

[28]   See id.

[29]   See id.

[30]   See proposed Phlx Rule 1000(f)(iii).

[31]   See proposed Phlx Rule 1000(f)(iii); see also Notice, supra note 3, at 56727.

[32]   See Amendment No. 1, supra note 6, at 3 and 7.

III.     Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of Section 6 of the Act[33] and the rules and regulations thereunder applicable to a national securities exchange.[34] Specifically, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,[35] which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, 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; and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Commission notes that the Exchange is proposing a new exception in Phlx Rule 1000(f)(iii)(D) that is designed to enable Floor Brokers to execute two types of split-price orders in the trading crowd that cannot be processed by FBMS because of a system limitation.[36] The

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[33]     15 U.S.C. 78f.

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

[35]     15 U.S.C. 78f(b)(5).

[36]     The Commission notes that the exception for split-price orders is similar in purpose to the current exceptions provided in Phlx Rule 1000(f)(iii)(B) and (C). See Securities Exchange Act Release No. 68960 (February 20, 2013), 78 FR 13132 (February 26, 2013) (SR-Phlx-2013-09) (recognizing exceptions for certain executions to occur manually in the trading crowd and not through FBMS. "[ ] FLEX orders will continue to be executable by Floor Brokers in the trading crowd pursuant to Rule 1079 and 1079A, rather than through FBMS. This is because FBMS will not be able to accept FLEX orders, which have varied and complicated terms. Similarly, accommodation transactions (also known as cabinet trades) will continue to be executable by Floor Brokers in the trading crowd pursuant to Rule 1059. Neither FLEX nor accommodation transactions are executed through Exchange systems today. Floor Brokers will also be

Exchange represents that its surveillance staff will oversee Floor Brokers' use of the proposed

Phlx Rule 1000(f)(iii)(D) exception, which they do today for current exceptions provided under

Phlx Rule 1000(f)(iii).[37]  The Exchange further represents that for each execution pursuant to

Phlx Rule 1000(f)(iii):  (1) Exchange surveillance staff will verify that the conditions of the

exception under Phlx Rule 1000(f)(iii) are met and will ensure that the proposed exception for

split-price orders will be used only rarely;[38] (2) Exchange surveillance staff will approve

executions pursuant to Phlx Rule 1000(f)(iii) and validate compliance with applicable priority

rules of the Exchange and trade-through rules of the Options Order Protection and

Locked/Crossed Market Plan;[39] and (3) all relevant trade data resulting from executions pursuant

to Phlx Rule 1000(f)(iii) will be recorded on both paper tickets and in FBMS to ensure a proper

audit trail for timely surveillance.[40]  The Commission notes that the activities of Phlx

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permitted to execute orders in the trading crowd if they are handling an order with more than 15 legs, because the Exchange determined to limit the complexity of FBMS functionality and does not believe that many orders fall into this category or that Floor Brokers will be adversely affected.").

[37]　See Notice, supra note 3, at 56726.  See also Amendment No. 1, supra note 6, at 17.  The Exchange notes its belief that it is "necessary and appropriate for the surveillance Staff to exercise independent judgment with respect to the proper timestamp for the consummation of trades on the floor of the Exchange."  See Amendment No. 1, supra note 6, at 14, n.17.  According to the Exchange, "[t]he surveillance Staff is trained to observe objectively the conduct of floor participants, to detect conduct that improperly advantages floor participants, and to enforce Exchange rules."  Id.  Finally, the Exchange notes that it believes that "[t]he absence of engaged and empowered surveillance Staff would undermine the integrity of the trading floor on the Exchange."  Id.

[38]　See Notice, supra note 3, at 56728.  See also Amendment No. 1, supra note 6, at 23.

[39]　See Notice, supra note 3, at 56727.  See also Amendment No. 1, supra note 6, at 22.  The Options Order Protection and Locked/Crossed Market Plan is available at http://www.optionsclearing.com/components/docs/clearing/services/options_order_protection_plan.pdf.

[40]　See Notice, supra note 3, at 56727.  See also Amendment No. 1, supra note 6, at 22.

Surveillance under Rule 1000(f)(iii), including the substitution of timestamps, should be carried out in an objective manner and with due regard to the Exchange's obligations under the Act.[41]

For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with Section 6(b)(5) of the Act and the rules and regulations thereunder applicable to national securities exchanges.

IV.     Solicitation of Comments on Amendment No. 1 to the Proposed Rule Change

Interested persons are invited to submit written data, views, and arguments concerning whether Amendment No. 1 to the proposed rule change is consistent with the Act.  Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or

- Send an e-mail to rule-comments@sec.gov.  Please include File No. SR-Phlx-2016-82 on the subject line.

Paper comments:

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

All submissions should refer to File No. SR-Phlx-2016-82.  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

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[41]     The Commission notes that Phlx surveillance staff might substitute the timestamp it captures for the timestamp captured by a Floor Broker if necessary to prevent conduct that would improperly advantage floor participants or to enforce compliance with the Exchange's rules.  It is the Commission's understanding that such a substitution would happen only rarely and only if consistent with the authority conferred upon surveillance staff by the Exchange's rules.  See Amendment No. 1., supra note 6, at 14, n.17.

comments on the Commission's Internet website (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 website 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-2016-82 and should be submitted on or before [insert date 21 days from

publication in the Federal Register].

V.     Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1

        The Commission finds good cause to approve the proposed rule change, as modified by

Amendment No. 1, prior to the thirtieth day after the date of publication of notice of the amended

proposal in the Federal Register. As described above, in Amendment No. 1, Phlx updated its

proposal to reflect the implementation of FBMS 3 and the retirement of FBMS 2; clarified how

prices may be rounded for non-customer split-price orders; and provided three examples that

explain how split-price orders will be handled by the Exchange under the proposed exception.[42]

The Commission believes that Amendment No. 1 provided additional specificity regarding the

operation of the new proposed exception in Phlx Rule 1000(f)(iii)(D). Accordingly, the

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[42]     See Amendment No. 1, supra note 6, at 3-4.

Commission finds good cause, pursuant to Section 19(b)(2) of the Act, [43] to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

VI.    Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[44] that the proposed rule change (SR-Phlx-2016-82), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[45]


Eduardo A. Aleman
Assistant Secretary

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[43]    15 U.S.C. 78s(b)(2)

[44]    See id.

[45]    17 CFR 200.30-3(a)(12).