

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-54859; File No. SR-Phlx-2006-51)

December 1, 2006

Self-Regulatory Organizations; Philadelphia Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change Relating to Performance Evaluations for Streaming Quote Traders and Remote Streaming Quote Traders

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on November 22, 2006, 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, II, and III, below, which Items have been substantially prepared by the Phlx. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Phlx, pursuant to Section 19(b)(1) of the Act<sup>3</sup> and Rule 19b-4 thereunder,<sup>4</sup> proposes to adopt Phlx Rule 510, SQT and RSQT Performance Evaluation, to establish performance requirements for Streaming Quote Traders ("SQTs")<sup>5</sup> and Remote

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

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

<sup>3</sup> 15 U.S.C. 78s(b)(1).

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

<sup>5</sup> An SQT is an Exchange Registered Options Trader ("ROT") who has received permission from the Exchange to generate and submit option quotations electronically through an electronic interface with AUTOM via an Exchange approved proprietary electronic quoting device in eligible options to which such SQT is assigned. See Phlx Rule 1014(b)(ii)(A). AUTOM is the Exchange's electronic order delivery, routing, execution and reporting system, which provides for the automatic entry and routing of equity option and index option orders to the Exchange trading floor. Orders delivered through AUTOM may be executed

Streaming Quote Traders (“RSQTs”).<sup>6</sup> The text of the proposed rule change is available on the Phlx’s Web site at <http://www.phlx.com>, at the Phlx’s Office of the Secretary, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Phlx included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The 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 adopt new Phlx Rule 510 to (1) establish performance requirements for SQTs and RSQTs, (2) authorize the Exchange to conduct performance evaluations periodically, and (3) authorize the Exchange’s Options

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manually, or certain orders are eligible for AUTOM's automatic execution features, AUTO-X, Book Sweep and Book Match. AUTOM is today more commonly referred to as Phlx XL. See Securities Exchange Act Release No. 50100 (July 27, 2004), 69 FR 46612 (August 3, 2004) (SR-Phlx-2003-59) and Phlx Rule 1080.

<sup>6</sup> An RSQT is a participant in Phlx XL who has received permission from the Exchange to trade in options for his own account, and to generate and submit option quotations electronically from off the floor of the Exchange through AUTOM in eligible options to which such RSQT has been assigned. See Phlx Rule 1014(b)(ii)(B).

Allocation, Evaluation and Securities Committee (“OAESC”)<sup>7</sup> to take corrective action where minimum requirements are not met.

Proposed Phlx Rule 510 provides for monthly performance evaluations of SQTs and RSQTs to determine whether they have fulfilled performance standards relating to, among other things, quality of markets, efficient quote submission to the Exchange (including quotes submitted through a third party vendor), competition, observance of ethical standards, and administrative factors.

The proposal would permit the Exchange to consider requests for relief from established quote spread parameters on the Exchange<sup>8</sup> and efficiency of quote submission through the Specialized Quote Feed (“SQF”), as defined in Phlx Rule 1080, Commentary .01. Failure to meet established minimum performance requirements could result in restriction by the OAESC of additional options assignments; suspension, termination, or restriction of an existing assignment on one or more options; or suspension, termination, or restriction of an SQT’s or RSQT’s status as such.

New Phlx Rule 510 would establish specific criteria for each option assigned to an SQT or RSQT that would be regularly evaluated by the Exchange. First, the Exchange would evaluate the percentage of total quotes submitted by the SQT or RSQT that represent the NBBO. If the percentage of the total quotes that represent the NBBO is

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<sup>7</sup> See Phlx By-Law Article X, Section 10-7. OAESC has jurisdiction over, among other things: the appointment of specialists on the options and foreign currency options trading floors; allocation, retention and transfer of privileges to deal in options on the trading floors; and administration of the 500 series of the Phlx rules.

<sup>8</sup> See Phlx Rule 1014(c)(i)(A).

in the lowest quartile of all SQTs or RSQTs for two or more consecutive months, this may be considered sub-standard performance.

Second, the Exchange would evaluate the SQT or RSQT's adherence to the Exchange's established quoting requirements pursuant to Phlx Rule 1014.<sup>9</sup> If an SQT or RSQT fails to meet the quoting requirements as prescribed by the rule, this may be considered sub-standard performance.

Third, the Exchange would consider the number of requests for quote spread parameter<sup>10</sup> relief for the purposes of evaluating performance standards.

Finally, to evaluate efficient quote submission to the Exchange, the Exchange will consider how an SQT or RSQT optimizes the submission of quotes through the SQF, as defined in Phlx Rule 1080, by evaluating the number of individual quotes per quote "block" received by the Exchange.

A quote "block" is a component of the Exchange's SQF application that allows for delivery of a set of multiple quotations from the SQT or RSQT to the Exchange. Within a single "block," the SQT or RSQT can deliver quotes for any number of option series ranging from 1 to 99.

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<sup>9</sup> Phlx Rule 1014(b)(ii)(D)(1) provides that an SQT and an RSQT shall be responsible to quote continuous, two-sided markets in not less than 60% of the series in each option in which such SQT or RSQT is assigned, provided that, on any given day, a Directed SQT ("DSQT") or a Directed RSQT ("DRSQT") (as defined in Phlx Rule 1080(l)(i)(C)) shall be responsible to quote continuous, two-sided markets in not less than 99% of the series listed on the Exchange in at least 60% of the options in which such DSQT or DRSQT is assigned. Whenever a DSQT or DRSQT enters a quotation in an option in which such DSQT or DRSQT is assigned, such DSQT or DRSQT must maintain continuous quotations for not less than 99% of the series of the option listed on the Exchange until the close of that trading day.

<sup>10</sup> Phlx Rule 1034 establishes maximum allowable bid/ask differentials on the Exchange.

An SQT or RSQT is assigned a number of ports or lines on which they can send quote blocks. The number of lines assigned dictates the number of blocks that may be sent simultaneously by the SQT or RSQT. The number of lines assigned to an SQT or RSQT is generally a function of the number of products being quoted, taking into account the throughput required to minimize quote latency risk.

The Exchange intends to evaluate the average number of quotes (1-99) submitted within the SQT or RSQT's quote blocks. The number of quotes delivered in each block would generally be a measure of the SQT or RSQT's quoting efficiency. For example, a firm sending an average of 1 quote in each block may be considered inefficient while a firm sending an average of 99 quotes in each block would be considered very efficient.

In general, the expenditure of systemic resources required to process an inefficient block is nearly equal to the expenditure of systemic resources required to process an efficient block. Therefore, an efficient SQT or RSQT can achieve a much higher level of quote submission than an inefficient SQT or RSQT using nearly the same amount of exchange system resources. The Exchange believes that the regular monitoring of quoting efficiency in this fashion will result in more efficient quoting on the Exchange (i.e., more quotes submitted per block), thus preserving and maximizing Exchange system capacity for handling quote traffic.

In conclusion, the Exchange believes that the proposed performance requirements for SQTs and RSQTs should, among other things, promote quoting efficiency and preserve system capacity, increase competition, minimize requests for relief from quote spread parameters, and encourage efficient adherence to quoting obligations, to the benefit of customers and the marketplace in general.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>11</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>12</sup> in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest, by establishing performance standards for SQTs and RSQTs, which should, in turn, improve the quality of markets on the Exchange..

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

The Exchange does not believe that the proposed rule change will impose any burden on competition 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

Written comments on the proposed rule change were neither solicited nor received.

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<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) 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 Phlx 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. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-Phlx-2006-51 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-2006-51. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission

will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing also will be available for inspection and copying at the principal office of the Phlx. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-Phlx-2006-51 and should be submitted on or before [insert date 21 days from date of publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).