

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-64244; File No. SR-Phlx-2011-46)

April 7, 2011

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by NASDAQ OMX PHLX LLC to Expand the Number of Components in the PHLX Gold/Silver Sector<sup>SM</sup> known as XAU<sup>SM</sup>, on Which Options are Listed and Traded

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup>, and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on March 31, 2011, NASDAQ OMX PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “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 Substance of the Proposed Rule Change

The Exchange is filing with the Commission a proposal to expand the number of components in the PHLX Gold/Silver Sector<sup>SM</sup> (the “Index” or “XAU<sup>SM</sup>”), on which options are listed and traded, and the Index weighting methodology.<sup>3</sup> No other changes are made to the Index or the options thereon.

The text of the proposed rule change is available on the Exchange’s Website at <http://nasdaqomxphlx.cchwallstreet.com/NASDAQOMXPHLX/Filings/>, at the principal office of the Exchange, and at the Commission’s Public Reference Room.

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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> PHLX Gold/Silver Sector<sup>SM</sup> may also be known as Gold/Silver Index.

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

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

The purpose of the proposal is to expand to thirty the number of components in the PHLX Gold/Silver Sector<sup>SM</sup> or XAU<sup>SM</sup>, on which options are listed and traded, and change the Index weighting methodology to modified capitalization-weighted.<sup>4</sup> No other changes are made to the Index or the options thereon.

XAU<sup>SM</sup> options subsequent to this proposal will be identical to XAU<sup>SM</sup> options that are currently listed and trading except for the number of components in the underlying Index; and will trade pursuant to similar contract specifications (updated regarding components and weighting methodology).<sup>5</sup> The only post-proposal difference in XAU<sup>SM</sup> options is that they will overly an Index with thirty components where the current Index has sixteen components, and the

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<sup>4</sup> The Exchange notes that changing the weighting of the Index from capitalization-weighting to modified capitalization-weighting does not by itself require a rule filing proposal because both weighting methodologies are acceptable per the current generic index listing standards found in Rule 1009A(b)(2). The weighting change is included in this proposal only in conjunction with increasing the number of Index components by more than the amount indicated in Rule 1009A(c)(2), which requires a rule filing proposal.

<sup>5</sup> The contract specifications for XAU<sup>SM</sup> options are available at <https://www.nasdaqtrader.com/micro.aspx?id=phlxsectorscontractspecs>.

Index will be modified capitalization-weighted where the current Index is capitalization-weighted.

### Background

The Gold/Silver Index is a P.M. settled capitalization-weighted index composed of the stocks of widely held U.S. listed companies involved in the gold/silver mining industry. Options on the Index have an American style expiration and the settlement value is based on the closing values of the component stocks on the day exercised, or on the last trading day prior to expiration.<sup>6</sup>

In 1983 XAU<sup>SM</sup> options were approved for listing and trading on the Exchange as the first options on a narrow-based index;<sup>7</sup> XAU<sup>SM</sup> options have been listed and have traded continuously on the Exchange since December 19, 1983.

In 1994, the Exchange established initial listing standards in Rule 1009A(b) and (d) for options on indexes that were designed to allow the Exchange to initially list and trade options on narrow-based indexes<sup>8</sup> and broad based indexes<sup>9</sup> pursuant to generic listing standards (the "Index

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<sup>6</sup> While the settlement value of a P.M. settled index such as XAU<sup>SM</sup> is based on closing prices of the component securities, the settlement value of A.M. settled securities is based on opening prices.

<sup>7</sup> See Securities Exchange Act Release No. 20437 (December 2, 1983), 48 FR 55229 (December 9, 1983)(order approving listing and trading options overlying the Gold/Silver Index and the Gaming/Hotel Index).

<sup>8</sup> A narrow-based index or industry index is defined as: An index designed to be representative of a particular industry or a group of related industries. The term "narrow-based index" includes indices the constituents of which are all headquartered within a single country. Rule 1000A(b)(12).

Currently, in addition to Gold/Silver Index, other narrow-based sector indexes on which options are listed and traded on the Exchange include: KBW Bank Index<sup>SM</sup> (BKX<sup>SM</sup>); PHLX Housing Sector<sup>SM</sup> (HGX<sup>SM</sup>); PHLX Utility Sector<sup>SM</sup> (UTY<sup>SM</sup>); SIG Energy MLP Index<sup>SM</sup> (SVO<sup>SM</sup>); SIG Oil Exploration & Production Index<sup>SM</sup> (EPX<sup>SM</sup>); PHLX Semiconductor Sector<sup>SM</sup> (SOX<sup>SM</sup>); PHLX Oil Service Sector<sup>SM</sup> (OSX<sup>SM</sup>); and NASDAQ Internet Index<sup>SM</sup> (QNET<sup>SM</sup>).

Options Listing Standards”).<sup>10</sup> In the 1994 generic index options filing, the Exchange also established generic continued listing standards in Rule 1009A(c) for narrow-based and broad-based index options, which apply to index options once they are listed pursuant to generic listing standards (the “Index Options Maintenance Standards”).<sup>11</sup> Because the Index is P.M. settled, it does not meet the A.M. settlement requirement of the Index Options Listing Standards.<sup>12</sup> However, the index meets all of the applicable Index Options Maintenance Standards.

In 1996, the Exchange received approval to apply to the Index all the Index Options Maintenance Standards of Rule 1009A(c) except the requirement that an index option be designated as A.M. settled per subsection (b)(1).<sup>13</sup> Subsection (c) also requires, among other

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<sup>9</sup> A broad-based index or market index is defined as: An index designed to be representative of a stock market as a whole or of a range of companies in unrelated industries. Rule 1000A(b)(11).

<sup>10</sup> See Securities Exchange Act Release No. 34157 (June 3, 1994), 59 FR 30062-01 (June 10, 1994)(order approving File Nos. SR-Amex-92-35; SR-CBOE-93-59; SR-NYSE-94-17; SR-PSE-94-07; and SR-Phlx-94-10)(the “generic index options filing”).

<sup>11</sup> The generic listing standards in Rule 1009A pursuant to Rule 19b-4(e) of the Act, see Securities Exchange Act Release No. 40761 (December 8, 1998), 63 FR 70952 (December 22, 1998), are similar to those of other options exchanges such as, for example, Chicago Board Options Exchange, Incorporated; International Stock Exchange LLC; and The NASDAQ Stock Market LLC.

<sup>12</sup> Rule 1009A(b)(1) requires A.M. settlement.

<sup>13</sup> See Securities Exchange Act Release No. 37334 (June 19, 1996), 61 FR 33162(June 26, 1996)(SR-Phlx-96-03)(order approving use of modified Rule 1009A(c) generic maintenance standards in respect of options on the Index).

The maintenance provisions in subsection (c) of Rule 1009A state, in part, as applicable to XAU<sup>SM</sup>: (1) The conditions stated in subparagraphs (b)(1), (3), (6), (7), (8), (9), (10), (11) and (12), must continue to be satisfied, provided that the conditions stated in subparagraph (b)(6) must be satisfied only as to the first day of January and July in each year; (2) The total number of component securities in the index may not increase or decrease by more than 33 1/3% from the number of component securities in the index at the time of its initial listing, and in no event may be less than nine component securities; (3) Trading volume of each component security in the index must be at least 500,000 shares for each of the last six months, except that for each of the lowest weighted component securities in the index that in the aggregate account for no more than 10% of

things, that the Index comply with the concentration requirements specifically set forth in 1009A(b)(6) regarding the Gold/Silver Index.<sup>14</sup> The Index meets all of the subsection (c) Index Options Maintenance Standards (the A.M. settlement requirement is not applicable to the Index) for continued trading of options overlying the Index, with one exception as noted below.

The Gold/Silver Index composed of sixteen companies continues to be a prime index that provides exposure to the dynamic gold/silver sector. When investors want information and investment opportunities specific to the gold/silver sector they most often turn to the Index and the XAU<sup>SM</sup> options traded thereon.<sup>15</sup> The Index has served as a leading market indicator and XAU<sup>SM</sup> options as a viable trading and investing vehicle in respect of the gold/silver sector.<sup>16</sup> Recognizing the market-leading aspects of the Index, the Exchange is proposing a rule change to increase to thirty the number of components in XAU<sup>SM</sup><sup>17</sup> so that this narrow-based index may even more effectively represent this market sector.

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the weight of the index, trading volume must be at least 400,000 shares for each of the last six months; (4) In a capitalization-weighted index, the lesser of the five highest weighted component securities in the index or the highest weighted component securities in the index that in the aggregate represent at least 30% of the total number of stocks in the index each have had an average monthly trading volume of at least 1,000,000 shares over the past six months.

<sup>14</sup> Id. Regarding concentration requirements, subsection (b)(6)(i) states that with respect to the Gold/Silver Index, no single component shall account for more than 35% of the weight of the Index and the three highest weighted components shall not account for more than 65% of the weight of the Index; and that if the Index fails to meet this requirement, the Exchange shall reduce position limits to 8000 contracts on the Monday following expiration of the farthest-out, then trading, non-LEAP series.

<sup>15</sup> Another currently available investment product that evaluates the gold sector (only) is the AMEX Gold BUGS Index.

<sup>16</sup> During 2010, XAU<sup>SM</sup> options traded an average of 55,432 contracts per month and traded as much as 13,581 contracts in a day (January 5, 2010). As of December 31, 2010, there were 3,787 contracts of open interest in XAU<sup>SM</sup> options.

<sup>17</sup> A listing of the component securities in XAU<sup>SM</sup> is available at <https://indexes.nasdaqomx.com/weighting.aspx?IndexSymbol=XAU&menuIndex=0>

The Exchange submits that in the proposed expanded form the Index would continue to meet the relevant Index Options Maintenance Standards in subsection (c) of Rule 1009A for listing XAU<sup>SM</sup> options. Specifically, all the applicable index maintenance requirements in subsection (c) applicable to options on narrow-based indexes would be met with one exception. The singular exception is the number of components. In particular, subsection (c)(2) of Rule 1009 indicates that the total number of component securities in the index may not increase or decrease by more than 33 1/3% from the total number of securities in the index at the time of its initial listing; adding components to equal thirty is outside the (c)(2) parameter, and is the reason why the Exchange is making the current filing.

#### Index Design and Index Composition

Currently, the Index is calculated using a capitalization-weighted index methodology. The value of the Index equals the aggregate value of the Index share weights, also known as the Index Shares, of each of the Index Securities (components) multiplied by each such security's Last Sale Price, and divided by the divisor of the Index. The divisor serves the purpose of scaling such aggregate index value to a lower order of magnitude which is more desirable for reporting purposes. If trading in an Index Security is halted on its primary listing market, the most recent Last Sale Price for that security is used for all index computations until trading on such market resumes. Likewise, the most recent Last Sale Price is used if trading in a security is halted on its primary listing market before the market is open.

The modified capitalization-weighted methodology is expected to retain, in general, the economic attributes of capitalization weighting, while providing enhanced diversification. To accomplish this, NASDAQ OMX, which maintains the Index, rebalances the Index quarterly and adjusts the weighting of Index components.

Index eligibility is limited to specific security types only. The security types eligible for the Index include common stocks, ordinary shares, ADRs, shares of beneficial interest or limited partnership interests and tracking stocks. Security types not included in the Index are closed-end funds, convertible debentures, exchange traded funds, preferred stocks, rights, warrants, units and other derivative securities.

As of December 31, 2010, the following were characteristics of the Index using a modified capitalization-weighting methodology:

- the total weighted capitalization of all components of the Index was \$354.60 billion;
- regarding component capitalization, (a) the highest weighted capitalization of a component was \$56.55 billion (Freeport-McMoRan Copper & Gold Inc.), (b) the lowest weighted capitalization of a component was \$0.44 billion (Endeavour Silver Corp.), (c) the mean capitalization of the components was \$11.82 billion, and (d) the median capitalization of the components was \$5.11 billion;
- regarding component price per share, (a) the highest price per share of a component was \$120.09 (Freeport-McMoRan Copper & Gold Inc.), (b) the lowest price per share of a component was \$6.94 (North American Palladium Ltd.), (c) the mean price per share of the components was \$33.39, and (d) the median price per share of the components was \$24.62;
- regarding component weightings, (a) the highest weighting of a component was 8% (Freeport-McMoRan Copper & Gold Inc., Barrick Gold Corporation, Southern Copper Corporation, Goldcorp Inc., Newmont Mining Corporation), (b) the lowest weighting of a component was 0.27% (Endeavour Silver Corp.), (c) the mean weighting of the components was 3.33%, (d) the median weighting of the components was 3.06%, and (e) the total weighting of the top five highest weighted components was 40% (Freeport-McMoRan

Copper & Gold Inc., Barrick Gold Corporation, Southern Copper Corporation, Goldcorp Inc., Newmont Mining Corporation);

- regarding component shares, (a) the most available shares of a component was 1.13 billion shares (Kinross Gold Corporation), (b) the least available shares of a component was 0.05 billion shares (Royal Gold, Inc.), (c) the mean available shares of the components was 0.33 billion shares, and (d) the median available shares of the components was 0.19 billion shares;
- regarding the six-month average daily volumes (“ADVs”) of the components, (a) the highest six-month ADV of a component was 11.00 million shares (Freeport-McMoRan Copper & Gold, Inc.), (b) the lowest six-month ADV of a component was 0.52 million shares (Royal Gold, Inc.), (c) the mean six-month ADV of the components was 3.53 million shares, (d) the median six-month ADVs of the components was 2.20 million shares, (e) the average of six-month ADVs of the five most heavily traded components was 8.99 million shares (Freeport-McMoRan Copper & Gold Inc., Hecla Mining Company, Barrick Gold Corporation, Yamana Gold, Inc., Silver Wheaton Corp.), and (f) 100% of the components had a six-month ADV of at least 200,000; and
- regarding option eligibility, (a) 100% of the components were options eligible, as measured by weighting, and (b) 100% of the components were options eligible, as measured by number.

#### Index Calculation and Index Maintenance

The Index is maintained by NASDAQ OMX and index levels are calculated continuously, using the Last Sale Price for each component stock in the Index. Index values are publicly disseminated at least every fifteen seconds throughout the trading day through a major market data vendor, namely NASDAQ OMX’s index dissemination service. The Exchange



expects that such dissemination will continue through one or more (NASDAQ OMX-owned or unrelated) major market data vendors.<sup>18</sup>

Appurtenant to review of the Index for purposes of rebalancing, component securities are evaluated by NASDAQ OMX. In the event that an Index Security no longer meets the Continued Security Eligibility Criteria, it will be replaced with a security that is not currently in the Index that meets all of the Initial Security Eligibility Criteria and additional criteria which follows. Securities eligible for inclusion will be ranked ascending by market value, current price and percentage price change over the previous six months. The security with the highest overall ranking will be added to the Index provided that the Index then meets the following criteria: no single Index Security is greater than 25% of the weight of the Index and the top 3 Index Securities are not greater than 55% of the weight of the Index; no more than 15% of the weight of the Index is composed of non-U.S. component securities that are not subject to comprehensive surveillance agreements.<sup>19</sup> In the event that the highest-ranking security does not permit the Index to meet the above criteria, the next highest-ranking security will be selected and the Index criteria will again be applied to determine eligibility. The process will continue until a qualifying replacement security is selected.<sup>20</sup> Component changes will be publicly announced.

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<sup>18</sup> Rule 1009A(b)(12) states that should an underlying index be maintained by a broker-dealer, however, the index must be calculated by a third party who is not a broker-dealer, and the broker-dealer will have to erect a "Chinese Wall" around its personnel who have access to information concerning changes in and adjustments to the index.

<sup>19</sup> See Rule 1009A(c), which refers to subsections (b)(6) and (b)(9).

<sup>20</sup> Moreover, changes in the price and/or Index Shares driven by corporate events such as stock dividends, stock splits, and certain spin-offs and rights issuances will be adjusted on the ex-date. If the change in total shares outstanding arising from other corporate actions is greater than or equal to 10.0%, the change will be made as soon as practicable. Otherwise, if the change in total shares outstanding is less than 10%, then all such changes are accumulated and made effective at one time on a quarterly basis after the close of trading on the third Friday in each of March, June, September, and December.

In the event a class of index options listed on the Exchange fails to satisfy the maintenance listing standards, the Exchange shall not open for trading any additional series of options of that class unless such failure is determined by the Exchange not to be significant and the Commission concurs in that determination, or unless the continued listing of that class of index options has been approved by the Commission under Section 19(b)(2) of the Act.<sup>21</sup>

The Exchange represents that, if the Index ceases to be maintained or calculated, or if the Index values are not disseminated at least every fifteen seconds by a widely available source, the Exchange will promptly notify the Division of Trading and Markets of the Commission, and the Exchange will not list any additional series for trading and will limit all transactions in such options to closing transactions only for the purpose of maintaining a fair and orderly market and protecting investors.

#### Contract Specifications

The contract specifications for the proposed expanded Index options (updated regarding components and weighting methodology) are, as previously noted, identical to the current narrow-based Index options that are currently listed and traded on the Exchange.<sup>22</sup> Options on the Index are American style and P.M. cash-settled. The Exchange's trading hours for index

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In the case of a special cash dividend, a determination will be made on an individual basis whether to make a change to the price of an Index Security in accordance with its Index dividend policy. If it is determined that a change will be made, it will become effective on the ex-date and advance notification will be made.

Ordinarily, whenever there is a change in Index Shares, a change in an Index Security, or a change to the price of an Index Security due to spin-offs, rights issuances, or special cash dividends, the divisor is adjusted to ensure that there is no discontinuity in the value of the Index, which might otherwise be caused by any such change. All changes are announced in advance and will be reflected in the Index prior to market open on the Index effective date.

<sup>21</sup> 15 U.S.C. 78s(b)(2).

<sup>22</sup> See supra note 5.

options (9:30 a.m. to 4:00 p.m. ET), will apply to options on XAU<sup>SM</sup>.<sup>23</sup> Exchange rules that are applicable to the trading of options on indexes will continue to apply to the trading of options on XAU<sup>SM</sup>.<sup>24</sup>

The strike price intervals for XAU<sup>SM</sup> options contracts will remain the same as those currently in use: \$2.50 or greater if the strike price is less than \$200.<sup>25</sup> The minimum increment size for series trading below \$3 will remain \$0.05, and for series trading at or above \$3 will remain \$0.10.<sup>26</sup> The Exchange's margin rules will be applicable.<sup>27</sup> The Exchange will continue to list options on XAU<sup>SM</sup> in up to three months from the March, June, September, December cycle plus two additional near-term months (that is, as many as five months at all times).<sup>28</sup> The trading of XAU<sup>SM</sup> options will continue to be subject to the same rules that govern the trading of all of the Exchange's index options, including sales practice rules, margin requirements, and trading rules.

#### Surveillance and Capacity

The Exchange represents that it has an adequate surveillance program in place for options traded on the Index and intends to apply those same program procedures that it applies to the Exchange's current XAU<sup>SM</sup> options and other index options. Additionally, the Exchange is a member of the Intermarket Surveillance Group ("ISG") under the Intermarket Surveillance

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<sup>23</sup> See Rule 101.

<sup>24</sup> For trading rules applicable to trading index options, see Rules 1000A et seq. For trading rules applicable to trading options generally, see Rules 1000 et seq.

<sup>25</sup> See Rule 1101A(a). Rule 1101A generally indicates that strike price intervals for index options may be \$5.00, \$2.50 and \$1.00

<sup>26</sup> See Rule 1034(a). However, the rule indicates that certain products (e.g. IWM options and Alpha Index options) may trade at \$0.01 minimum increments.

<sup>27</sup> See Rule 721 et seq.

<sup>28</sup> See Rule 1101A(b).

Group Agreement, dated June 20, 1994. ISG members generally work together to coordinate surveillance and investigative information sharing in the stock and options markets. In addition, the major futures exchanges are affiliated members of the ISG, which allows for the sharing of surveillance information for potential intermarket trading abuses.<sup>29</sup>

The Exchange represents that it has the necessary systems capacity to continue to support listing and trading XAU<sup>SM</sup> options.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>30</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>31</sup> in particular, in that it 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 facilitating transactions in securities, and to remove impediments to and perfect the mechanisms of a free and open market and a national market system. The Exchange believes that the proposal to expand the XAU<sup>SM</sup> index will allow the Exchange to seamlessly continue listing this premiere index and options thereon in a manner that even more effectively reflects the gold/silver sector.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

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

No written comments were either solicited or received.

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<sup>29</sup> A list of the current members and affiliate members of ISG can be found at <http://www.isgportal.org/isgportal/public/members.htm>.

<sup>30</sup> 15 U.S.C. 78f(b).

<sup>31</sup> 15 U.S.C. 78f(b)(5).

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

Within 45 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 Exchange consents, the Commission shall: (a) by order approve or disapprove 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-2011-46 on the subject line.

#### Paper comments:

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

All submissions should refer to File Number SR-Phlx-2011-46. 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 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 also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make publicly available. All submissions should refer to File Number SR-Phlx-2011-46 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>32</sup>

Cathy H. Ahn  
Deputy Secretary

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<sup>32</sup> 17 CFR 200.30-3(a)(12).