

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-81630; File No. SR-PHLX-2017-56)

September 15, 2017

Self-Regulatory Organizations; NASDAQ PHLX LLC; Order Approving Proposed Rule Change to a proposal to amend Rule 1027, Discretionary Accounts, to conform it more closely to a comparable rule of the Chicago Board Options Exchange (“CBOE”) and to make minor corrections and clarifications

I. Introduction

On July 20, 2017, NASDAQ PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”)¹ and Rule 19b-4 thereunder,² proposed rule changes to amend Phlx Rule 1027 (Discretionary Accounts).

The proposed rule changes were published for comment in the Federal Register on August 4, 2017.³ The public comment period closed on August 25, 2017. The Commission received no comments on the proposed rule changes. This order approves the proposed rule changes.

II. Description of the Proposed Rule Changes⁴

Rule 1027 generally imposes restrictions and various requirements on members⁵ and partners and employees of member organizations⁶ regarding the exercise of discretionary power

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Exchange Act Release No. 81270 (Jul. 31, 2017), 82 FR 36469 (Aug. 4, 2017) (“Notice”).

⁴ The subsequent description of the proposed rule change is substantially excerpted from the Exchange’s description in the Notice. See Notice, 82 FR 36469-71.

⁵ Exchange Rule 1(n) defines “member” as a permit holder which has not been terminated in accordance with the By-Laws and Rules of the Exchange. The Exchange has issued

with respect to trading in options in a customer's accounts. The Exchange proposes to amend Rule 1027 in a number of respects to eliminate redundant rule text, clarify certain rule text, and conform parts of the rule more closely to CBOE Rule 9.10, Discretionary Accounts.⁷

Rule 1027(a) Authorization and Approval Required

Rules 1027(a)(i) and (ii) apply to stock or exchange-traded fund share options and foreign currency options, respectively. These provisions prohibit the exercise of any discretionary power with respect to trading in options contracts in a customer's account unless such customer has given prior written authorization with respect to such trading and the account

“Series A-1” permits, which confer on the holder rights and privileges, and impose on the holder the obligations, set forth in Exchange Rule 908. Under Exchange Rule 908(b), a Series A-1 permit may only be issued to an individual who is a natural person of at least twenty-one (21) years of age, or to a corporation meeting the eligibility and application requirements set forth in the By-Laws and Rules.

⁶ Rule 1(o) defines “member organization” as “a corporation, partnership (general or limited), limited liability partnership, limited liability company, business trust or similar organization, transacting business as a broker or a dealer in securities and which has the status of a member organization by virtue of (i) admission to membership given to it by the Membership Department pursuant to the provisions of Rules 900.1 or 900.2 or the By-Laws or (ii) the transitional rules adopted by the Exchange pursuant to Section 6-4 of the By-Laws.” Rule 901(a) provides in part that “[t]he Membership Department shall have jurisdiction over the issuance of memberships (in respect of members and member organizations) and permits and over applications by non-members for admission as members.” Rule 901(c) provides that “[a]ll applications to qualify and register a corporation or other entity as a member organization and all applications for reinstatement of any qualification or registration of a member organization shall be referred to the Membership Department which shall investigate and act thereon.”

⁷ CBOE Rule 9.10 was substantially amended in Securities Exchange Act Release No. 56492 (September 21, 2007), 72 FR 54952 (September 27, 2007) (SR-CBOE-2007-106) to create a supervisory structure for options that is similar to that required by New York Stock Exchange (“NYSE”) and National Association of Securities Dealers (“NASD”) rules. On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD's Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority Inc., or FINRA, in connection with the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. See Securities Exchange Act Release No. 56146 (July 26, 2007).

has been accepted in writing by a designated Registered Options Principal or, in the case of foreign currency options, a Foreign Currency Options Principal.

The Exchange proposes to amend Rule 1027(a)(i) to include index options, as their current exclusion from the rule is without a rational basis and was likely an oversight. The Exchange also proposes to expand the rule to cover member organizations, to be more consistent with the comparable CBOE rule which applies to CBOE Trading Permit Holder (“TPH”) organizations.⁸ References to Registered Options Principal “qualified persons” or “qualified individuals” in Rule 1027(a)(i) are proposed to be amended in order to refer only to “Registered Options Principals,” in order to eliminate needless ambiguity and lack of clarity as to who is a Registered Options Principal “qualified person” or “qualified individual.” Additionally, the last two sentences of Rule 1027(a)(i) currently provide that every discretionary order shall be identified as discretionary at the time of entry, and that discretionary accounts shall receive frequent review by a Registered Options Principal qualified person specifically delegated such responsibilities under Rule 1025, who is not exercising the discretionary authority. These sentences are largely duplicative of existing Rule 1027(a)(iii) and are therefore proposed to be deleted.

The Exchange proposes to delete from Rule 1027(a)(iii) a reference to “Compliance Registered Option Principal,” a term which the Exchange no longer uses, and proposes to substitute the term “Registered Options Principal.” It also proposes to amend that section by adding language requiring the Registered Options Principal providing appropriate supervisory

⁸ Rule 1027(a)(ii) addresses foreign currency options and has no counterpart in CBOE Rule 9.10(a). The Exchange is nevertheless proposing to revise Rule 1027(a)(ii) by expanding its scope to include member organizations for consistency with Rule 1027(a)(i) in terms of extent of coverage of the rule.

review to be specifically delegated such responsibilities under Rule 1025 and not be the Registered Options Principal exercising the discretionary review. These changes would conform Rule 1027(a)(iii) to the duplicative language deleted from Rule 1027(a)(i) as described above. The Exchange also proposes to delete the last sentence of Rule 1027(a)(iii), which provides that the provisions of paragraph (a) shall not apply to discretion as to the price at which or the time when an order given by a customer for the purchase or sale of a definite number of option contracts in a specified security or foreign currency shall be executed. This sentence is largely duplicative of existing language in Rule 1027(e), Discretion as to Time or Price Excepted. Rule 1027(e), however, is proposed to be amended by the addition of a reference to “foreign currency” which was present in the deleted sentence of Rule 1027(a)(iii).

The Exchange is proposing no changes to Rule 1027(a)(iv), which extends the provisions of Rule 1027 to index warrants, as no changes are required.

Rule 1027(c) Prohibited Transactions

Currently, Rule 1027(c) prohibits members as well as partners, officers and employees of a member organization having discretionary power over a customer's account from, in the exercise of such discretion, executing or causing to be executed therein any purchases or sales of option contracts which are excessive in size or frequency in view of the financial resources in such account. The prohibition is proposed to be reworded, to conform Phlx Rule 1027(c) more closely to CBOE Rule 9.10, Discretionary Accounts, section (c). Additionally, the rule would be expanded to cover member organizations as well as members and partners and employees of member organizations.

Rule 1027(d) Record of Transactions

Rule 1027(d) currently requires a record to be made of every transaction in option contracts in respect to which a member or a partner, officer or employee of a member organization has exercised discretionary authority, clearly reflecting such fact and indicating the name of the customer, the designation and number of the option contracts, the premium and the date and time when such transaction was effected. The Exchange proposes to reword the rule so that it applies to option transactions for an account in respect to which a member or member organization or a partner, officer or employee of a member organization is vested with any discretionary authority, and to detail the required content of the record. The revision proposed for Rule 1027(d) would conform the rule more closely to CBOE Rule 9.10, Discretionary Accounts, section (b), which extends to CBOE TPH organizations, except that the Exchange proposes to retain the existing requirement that the transaction record clearly reflect that the member (or, as the rule is proposed to be amended, member organization) or a partner, officer or employee of a member organization has exercised discretionary authority, as the Exchange believes this to be important information with respect to a transaction.

Rule 1027(e) Discretion as to Time or Price Excepted

As discussed above the Exchange proposes to amend Rule 1027(e), which generally excludes price and time discretion from the requirements of Rule 1027, to cover foreign currency options. The Exchange also proposes to correct an internal cross reference to “this paragraph (d)” which should read “this paragraph (e).”

III. Discussion and Commission Findings

After careful review of the proposed rule change, the Commission finds that the proposal is consistent with the requirements of the Exchange Act and the rules and regulations thereunder

that are applicable to a national securities exchange.⁹ Specifically, the Commission finds that the proposed rule changes are consistent with Section 6(b)(5) of the Exchange Act,¹⁰ 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. Section 6(b)(5) also requires that the rules of an exchange not be designed to permit unfair discrimination among customers, issuers, brokers, or dealers.

The proposal is designed to “remove impediments to and perfect the mechanism of a free and open market and a national market system, by eliminating redundant rule text, clarifying certain rule text, and conforming parts of the rule more closely to CBOE Rule 9.10, Discretionary Accounts.”¹¹ The Commission notes that Phlx believes that harmonizing its rule regarding discretionary accounts with its CBOE counterpart will create “more efficient regulatory compliance by members of both exchanges due to reduction of differences in wording and consequent potential for inadvertent regulatory noncompliance.”¹² The Commission further notes that Phlx believes that harmonizing Rule 1027 with its CBOE counterpart will “further the goal of harmonized examinations and enforcement of similar rules, thus reducing duplicative regulatory efforts” and thus lowering overall regulatory costs imposed on member organizations

⁹ In approving this rule change, the Commission has considered the rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁰ 15 U.S.C. 78f(b)(5).

¹¹ Notice, 82 FR at 36471.

¹² Id.

and, by extension, the general public.¹³ The Commission notes that the proposal received no comments from the public. Taking into consideration the Exchange's views about the proposed amendments, the Commission believes that the proposal will promote regulatory efficiency through more streamlined rule text that avoids unnecessary redundancy, clarification of the meaning and scope of the rule, and greater harmonization of regulatory requirements across national securities exchanges, thereby reducing regulatory burdens, without undermining strong regulatory protections for investors. The Commission believes that the approach proposed by the Exchange is appropriate and designed to protect investors and the public interest, consistent with Section 6(b)(5) of the Exchange Act. For these reasons, the Commission finds that the proposed rule change is consistent with the Exchange Act and the rules and regulations thereunder.

IV. Conclusion

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2)¹⁴ of the Exchange Act that the proposal (SR-PHLX-2017-56), be and hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁵

Eduardo A. Aleman
Assistant Secretary

¹³ See id.

¹⁴ 15 U.S.C. 78s(b)(2).

¹⁵ 17 CFR 200.30-3(a)(12).