

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-63967; File No. SR-Phlx-2011-27)

February 25, 2011

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by NASDAQ OMX PHLX LLC Relating to Amendments to Rules 200(g) and 201 of Regulation SHO Applicable to Complex Orders

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 February 23, 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 and II below, which Items have been substantially 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 proposes to amend Rule 1080.08 respecting complex orders to reflect the marking requirements of Regulation SHO and to address the handling of certain orders marked “short” in compliance with Rule 201 of Regulation SHO, as explained further below.

The text of the proposed rule change is available on the Exchange’s Web site at <http://www.nasdaqtrader.com/micro.aspx?id=PHLXRulefilings>, 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.

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

Recently, the Exchange received approval from the Commission to make various enhancements to its complex orders system, including to accept complex orders where one component is the underlying security of the options components.<sup>3</sup> Specifically, the underlying stock or ETF can now be one component of a complex order.<sup>4</sup> Nasdaq Options Services LLC (“NOS”), a registered broker-dealer and member of Financial Industry Regulatory Authority, is responsible for the execution of the stock or ETF component of a complex order as agent of the stock or ETF component.<sup>5</sup> This is described in Rule 1080.08(h). A complex order with one component that is a stock or

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<sup>3</sup> See Securities Exchange Act Release No. 63777 (January 26, 2011), 76 FR 5630 (February 1, 2011) (SR-Phlx-2010-157) (“Complex Order rule filing”).

<sup>4</sup> A complex order is a an order involving the simultaneous purchase and/or sale of two or more different options series in the same underlying security or a stock-option order, priced as a net debit or credit, based on the relative prices of the individual components, for the same account, for the purpose of executing a particular investment strategy. See Rule 1080.08(a).

<sup>5</sup> The NASDAQ OMX Group, Inc. owns both the Exchange and NOS; therefore, the Exchange and NOS are affiliates.

ETF is received by the Exchange with a net debit or credit price. The individual option leg(s) and stock/ETF component prices are not specified; rather, there is a single net debit or credit price on the order which is used by Phlx and NOS to determine the price of each component, including the stock/ETF. Specifically, although Phlx is calculating the price of the options components, a sophisticated algorithm is simultaneously causing NOS to calculate and execute the stock or ETF component of the Complex Order, which has been electronically communicated to NOS by the Exchange. Thus, because the execution of one component is contingent upon the execution of all others, the entire package is processed as a single transaction and both the option leg and stock/ETF components are simultaneously processed.

In the Complex Order rule filing, the Exchange explained that with respect to short sale regulation, the proposed handling of the stock/ETF component of a complex order did not raise any issues of compliance with the currently operative provisions of Regulation SHO.<sup>6</sup> When a complex order has a stock/ETF component, member organizations must mark, pursuant to Regulation SHO, whether that order involves a long or short sale.<sup>7</sup> The Phlx trading System will accept complex orders with a stock/ETF component marked to reflect either a long or short position; specifically, orders not currently marked as “long” or “short” are rejected by the Phlx trading System.

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<sup>6</sup> 17 CFR 242.200 et seq.

<sup>7</sup> 17 CFR 242.200(g).

In 2010, the Commission amended Rule 201 and Rule 200(g) of Regulation SHO under the Act.<sup>8</sup> The amendments to Rule 201 adopt a short sale-related circuit breaker that, if triggered, imposes a restriction on the prices at which covered securities may be sold short (“short sale price test restriction”).<sup>9</sup> Specifically, Rule 201 requires a trading center<sup>10</sup> to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the execution or display of a short sale order of a covered security<sup>11</sup> at a price that is less than or equal to the current national best bid<sup>12</sup> if the price of that covered security decreases by 10% or more from the covered security’s closing price as determined by the listing market<sup>13</sup> for the covered security as of the end of regular trading hours on the prior day;<sup>14</sup> and impose these requirements for the remainder of the day and the following day when a national best bid for the covered security is calculated and disseminated on a current and continuing basis by a plan processor pursuant to an

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<sup>8</sup> See Securities Exchange Act Release No. 61595 (February 26, 2010), 75 FR 11232 (March 10, 2010). See also Division of Trading and Markets: Responses to Frequently Asked Questions Concerning Rule 201 of Regulation SHO.

<sup>9</sup> 17 CFR 242.201.

<sup>10</sup> The term “trading center” is defined in Rule 201(a)(9) of Regulation SHO. 17 CFR 242.201(a)(9). Both the Exchange and NOS are “trading centers” within the definition of Rule 201(a)(9).

<sup>11</sup> The term “covered security” is defined in Rule 201(a)(1) as any NMS stock as defined in Rule 600(b)(47) of Regulation NMS. 17 CFR 242.201(a)(1). See also 17 CFR 242.600(b)(47).

<sup>12</sup> The term “national best bid” is defined in Rule 201(a)(4). 17 CFR 242.201(a)(4).

<sup>13</sup> The term “listing market” is defined in Rule 201(a)(3). 17 CFR 242.201(a)(3).

<sup>14</sup> 17 CFR 242.201(b)(1)(i).

effective national market system plan.<sup>15</sup> The amendments to Rule 200(g) provide that a broker-dealer may mark certain qualifying short sale orders “short exempt.”<sup>16</sup>

Thereafter, the Commission extended the compliance date for the amendments to Rule 201 and Rule 200(g) until February 28, 2011.<sup>17</sup> The Exchange is filing this proposed rule change to address the new amendments to Regulation SHO.

Accordingly, the purpose of the proposed rule change is to explain the Exchange’s handling of stock/ETF sell components entered as part of a complex order in accordance with the amendments to Regulation SHO. In particular, the Exchange is proposing to provide that, if the stock/ETF leg of a complex order submitted to the Phlx trading System is a sell order, then the stock/ETF leg must be marked “long,” “short,” or “short exempt” in compliance with Rule 200(g) of Regulation SHO; if it is not so marked, the order will be rejected. Thus, the Exchange will now accept complex orders marked “short exempt” and Rule 1080.08(b)(iv) is being adopted to reflect this.<sup>18</sup> The Exchange and NOS, as trading centers, must comply with Rule 201(b)(1)(iii)(B), which provides that a trading center must establish, maintain, and enforce written policies and

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<sup>15</sup> 17 CFR 242.201(b)(1)(ii).

<sup>16</sup> 17 CFR 242.200(g)(2).

<sup>17</sup> See Securities Exchange Act Release No. 63247 (November 4, 2010), 75 FR 68702 (November 9, 2010) (extending the compliance date of the amendments to Rules 201 and 200(g) of Regulation SHO from November 10, 2010 until February 28, 2011).

<sup>18</sup> The Exchange notes that a broker or dealer may mark a sell order “short exempt” only if the provisions of Rule 201(c) or (d) are met. See 17 CFR 242.200(g)(2). Since NOS and the Exchange do not display the stock or ETF portion of a complex order, see *infra* note 20, a broker-dealer should not mark the short sale order “short exempt” under Rule 201(c). See also Division of Trading and Markets: Responses to Frequently Asked Questions Concerning Rule 201 of Regulation SHO, Q&A Nos. 4.2, 5.4 and 5.5.

procedures reasonably designed to permit the execution or display of a short sale order of a covered security marked “short exempt” without regard to whether the order is at a price that is less than or equal to the current national best bid.<sup>19</sup>

Furthermore, the Exchange proposes to amend Rule 1080.08(h) to describe the handling of short sales involving the stock/ETF leg of a complex order submitted to its Phlx trading System. When the short sale price test restriction is triggered for a covered security, NOS will not execute or display<sup>20</sup> a short sale order in the underlying covered security component of a complex order if the price is equal to or below the current national best bid. However, NOS will execute a short sale order in the underlying covered security component of a complex order if such order is marked “short exempt,” regardless of whether it is at a price that is equal to or below the current national best bid. If NOS cannot execute the underlying covered security component of a complex order in accordance with Rule 201 of Regulation SHO, the Exchange will cancel back the complex order to the entering member organization. When a short sale price test restriction is triggered in a covered security, orders in that security marked “short” may be executed by NOS if the order is at a price above the current national best bid at the time of execution. Thus, the proposal is narrowly tailored to address Rule 201 by only cancelling orders marked “short” when a short sale price test restriction is triggered in the covered security and the sell order is at a price equal to or below the current national best bid at the time of execution.

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<sup>19</sup> 17 CFR 242.201(b)(1)(iii)(B).

<sup>20</sup> The stock or ETF portion of a complex order is not displayed as an order, because the complex order as a whole is handled as a single order with multiple contingencies.

The Exchange believes that this approach is consistent with Rule 201. Under this proposal, the Exchange and NOS, as trading centers, will prevent the execution or display of a short sale of the stock/ETF component of a complex order priced at or below the current national best bid when the short sale price test restriction is triggered. Specifically, while the Exchange and NOS are determining, respectively, the prices of the options component and of the stock or ETF component of the complex order, as described above, NOS will check the current national best bid of the stock or ETF component at the time of execution. The execution of one component is contingent upon the execution of all other components and once a complex order is accepted and validated by the Phlx trading System, the entire package is processed as a single transaction and both the option leg and stock/ETF components are simultaneously processed.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>21</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>22</sup> in particular, in that it is designed to promote just and equitable principles of trade, and, in general to protect investors and the public interest, by providing clarity on the short sale order handling procedures of the stock/ETF component of a complex order when a short sale price test restriction is in effect for a covered security. Furthermore, the Exchange believes that the proposed rule change is consistent with Regulation SHO in that it provides for the handling of short exempt orders as well as short sale orders when the short sale price test restriction is triggered.

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

<sup>22</sup> 15 U.S.C. 78f(b)(5).

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.

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

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate, it has become effective pursuant to 19(b)(3)(A) of the Act<sup>23</sup> and Rule 19b-4(f)(6)<sup>24</sup> thereunder. The Exchange has requested that the Commission waive the 30-day pre-operative waiting period contained in Exchange Act Rule 19b-4(f)(6)(iii)<sup>25</sup> so that the Exchange may implement the change no later than February 28, 2011 to coincide with the compliance date for the amendments to Rules 200(g) and 201 of Regulation SHO. The Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest because the proposed rule change, among other things, implements the amendments to Rules 200(g)

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<sup>23</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>24</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

<sup>25</sup> 17 CFR 240.19b-4(f)(6)(iii).



and 201 of Regulation SHO which have a February 28, 2011 compliance date.<sup>26</sup> For this reason, the Commission designates the proposed rule change to be operative upon filing with the Commission.<sup>27</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or 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-2011-27 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.

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<sup>26</sup> See *supra* note 17.

<sup>27</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule change's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

All submissions should refer to File Number SR-Phlx-2011-27. 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 Web site 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 the 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 available publicly. All submissions should refer to File Number SR-Phlx-2011-27 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>28</sup>

Cathy H. Ahn  
Deputy Secretary

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<sup>28</sup> 17 CFR 200.30-3(a)(12).