

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-69194; File No. SR-Phlx-2013-24)

March 20, 2013

Self-Regulatory Organizations; NASDAQ OMX PHLX LLC; Notice of Filing of Proposed Rule Change to Adopt a Price/Display/Time Priority Algorithm, Permit the Registration of Market Makers, and Amend the Order Types Available on PSX

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on March 8, 2013, NASDAQ OMX PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change, which filing was amended and replaced in its entirety by Amendment No. 1 thereto on March 18, 2013, 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 proposes to modify certain aspects of the operation of NASDAQ OMX PSX (“PSX”). The text of the proposed rule change is available at <http://nasdaqomxphlx.cchwallstreet.com/nasdaqomxphlx/phlx/>, at the Exchange’s principal office, 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 Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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

In 2010, Phlx launched PSX as a new platform for trading NMS stocks,³ using a novel price/size pro rata model for allocating the execution of incoming orders against orders resting on the PSX book.⁴ Phlx anticipated that this market model would gain traction as an alternative to a national market structure in which the prevailing price/time model places an emphasis on the speed with which market participants can route and cancel orders as the means to optimize their executions. Unfortunately, the price/size execution model has been only marginally successful in garnering market share, primarily due to the risk of a large execution at a stale price that a market participant would face if unable to adjust the prices of its posted orders quickly. Accordingly, Phlx has decided to adopt a price/time model for PSX. In addition, Phlx is proposing to allow member organizations to register as market makers on PSX, provided they satisfy two-sided quoting and market quality requirements associated with that status. Finally, Phlx is proposing to introduce midpoint peg post-only orders, and price to comply post orders; to adjust the operation of minimum quantity orders and post-only orders; and to eliminate

³ Defined in SEC Rule 600 under Regulation NMS, 17 CFR 242.600, to mean any security or class of securities (other than an option) for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan.

⁴ Securities Exchange Act Release No. 62877 (September 9, 2010), 75 FR 56633 (September 16, 2010) (SR-Phlx-2010-79).

minimum life orders. In all material respects, the rules as adjusted by this proposed rule change will be identical to rules in effect at The NASDAQ Stock Market (“NASDAQ”) and/or NASDAQ OMX BX, Inc. (“BX”). Phlx proposes to implement the change as soon as practicable following Commission approval. This Amendment No. 1 to the original filing corrects several minor typographical errors in the original filing and provides additional explanation with respect to the purpose and effect of some of the proposed rule changes.

Order Processing Algorithm

The order processing algorithm currently in use at PSX allocates the execution of incoming orders against posted liquidity in following order:

(1) Price. Better priced orders are executed first.

(2) Pro-Rata Allocation to Size Among Displayed Orders with a Size of One Round Lot or More. As among equally priced Displayed Orders with a size of at least one round lot, PSX allocates the round lot portions of incoming executable orders pro rata based on the size of the Displayed Orders. Portions of an order that would be executed in a size other than a round lot if they were allocated pro rata are allocated on the basis of a random function that assigns probability of execution based on the size of displayed interest.

(3) Displayed Odd-Lot Orders. As among equally priced Displayed Orders with a size of less than one round lot, PSX allocates incoming orders based on the size of the Displayed Orders, but not in pro rata fashion. If there are two or more such orders of equal size, PSX determines the order of execution on the basis of a random function that assigns each order an equal probability of execution.

(4) Pro-Rata Allocation to Size Among Non-Displayed Interest with a Size of One Round Lot or More. As among equally priced Non-Displayed Orders and the reserve portion of Reserve Orders (collectively, “Non-Displayed Interest”) with a size of at least one round lot, PSX allocates round lot portions of incoming executable orders to Non-Displayed Interest pro rata based on the size of the Non-Displayed Interest. Portions of an order that would be executed in a size other than a round lot if they were allocated pro rata are allocated on the basis of a random function that assigns probability of execution based on the size of Non-Displayed Interest.

(5) Minimum Quantity Orders. As among equally priced Minimum Quantity Orders, PSX allocates incoming executable orders in the ascending order of the size of the minimum quantity conditions assigned to the orders. If there are two or more Minimum Quantity Orders with an equal minimum quantity condition, the System will determine the order of execution on the basis of a random function that assigns each order an equal probability of execution.

(6) Non-Displayed Odd-Lot Orders. As among equally priced Non-Displayed Interest with a size of less than one round lot, PSX allocates incoming orders based on the size of the Non-Displayed Interest, but not in pro rata fashion. If there are two or more such orders of equal size, PSX determines the order of execution on the basis of a random functions that assigns each order an equal probability of execution.

Phlx is amending Rule 3307, and making conforming changes to Rule 3306, to replace this algorithm with a straightforward price/display/time priority algorithm that is substantively identical to corresponding rules in effect at NASDAQ and BX. The modified algorithm is as follows:

(1) Price. Better priced orders are executed first.

(2) Displayed Orders. As among equally priced Displayed Orders, the first to arrive on the book is executed first.

(3) Non-Displayed Orders and the Reserve Portion of Quotes⁵ and Reserve Orders. As among equally priced Non-Displayed Orders and the reserve portion of Quotes and Reserve Orders, the first to arrive on the books is executed first.

PSX rules currently provide for an anti-internalization exception to the algorithm, designed to allow a PSX Participant to prevent its own orders from interacting with each other. Phlx is modifying this exception so that it conforms to a similar exception in effect at NASDAQ and BX. Specifically, the rules of all three exchanges currently provide that a market participant may direct that orders not execute against orders entered under the same market participant identifier (“MPID”), or under the same MPID and with a unique group identification modifier (for example, by grouping all orders entered through a particular order entry port). In other words, the market participant may limit interaction among all orders under the MPID, or only an identified subset of orders. Under current PSX rules, if two orders that are not permitted to interact with each other are matched through the order execution algorithm, the orders are decremented by share amounts equal to the size of the portion of the incoming order that is designated to interact with a posted order. Thus, if 100 shares of an incoming order to buy 200 shares are designated to execute against a posted order to sell 1,000 shares, and the two orders have been marked not to execute against each other, the incoming order and the posted order will each be decremented by 100 shares. The orders are decremented to reflect that the

⁵ As discussed below, PSX will introduce quoting functionality in support of the introduction of market makers.

Participant, having adopted anti-internalization protection, does not intend to buy shares that it is simultaneously selling. The revisions to the rule retain this logic, but give the Participant additional choice as to how the conflict should be resolved. First, the Participant may opt for the same treatment as currently provided by PSX, although the revised rule text reflects the change in order execution algorithm by providing that if the two orders are the same size, they will both be cancelled, while if one is larger, the smaller of the two is cancelled and the larger is decremented and retained. This changed language reflects the fact that in a price/time algorithm, an incoming order will be executed to the maximum extent possible against orders on the book in price/time sequence, whereas under the current algorithm, an incoming order may be allocated across multiple resting orders based on their size. Alternatively, a Participant may opt to have the oldest of the two orders cancelled in full, regardless of the respective sizes of the orders. The Participant may make this election across an entire MPID, or may differentiate among order entry ports associated with the MPID.

Market Making

Phlx is proposing to adopt rules that are already in effect at NASDAQ and/or BX to allow member organizations that are PSX Participants to register and act as market makers. Following the effectiveness of the proposed changes, Phlx plans to introduce programs designed to encourage PSX Participants to register as market makers, with the goal of enhancing the liquidity and market quality of trading on PSX.

Proposed Rule 3212 provides that quotations and quotation sizes may be entered into PSX only by a member organization registered as a PSX Market Maker or other entity approved by the Exchange to function in a market-making capacity. A PSX

Market Maker may become registered in an issue by entering a registration request via an Exchange approved electronic interface with PSX's systems or by contacting PSX Market Operations. Registration shall become effective on the day the registration request is entered. A PSX Market Maker's registration in an issue shall be terminated by the Exchange if the market maker fails to enter quotations in the issue within five (5) business days after the market maker's registration in the issue becomes effective. The rule is intended to provide a flexible means by which member organizations may register as market makers, while ensuring that they make prompt use of such registration.

Proposed amendments to Rule 3217 provide that all PSX Market Makers must be open during regular market hours (9:30 a.m. through 4:00 p.m.).⁶ PSX Market Makers are also permitted to operate during pre-market (8:00 a.m. through 9:30 a.m.) and post-market (4:00 p.m. to 5:00 p.m.) hours. PSX Market Makers must comply with rules governing quotations at all times that their quotes are open, unless a rule is inapplicable to pre-market or post-market hours.

Proposed amendments to Rule 3213 impose quoting obligations on PSX Market Makers identical to those in effect at NASDAQ and BX. Under the amended rule, a member organization registered as a Market Maker is required to engage in a course of dealings for its own account to assist in the maintenance, insofar as reasonably practicable, of fair and orderly markets in accordance with this Rule. In accordance with the requirement, the rule specifically requires a member organization registered as a Market Maker in a particular security to be willing to buy and sell such security for its own account on a continuous basis during regular market hours and to enter and maintain

⁶ All times are Eastern Time.

a two-sided trading interest (“Two-Sided Obligation”) that is identified to the Exchange as the interest meeting the obligation and is displayed in PSX’s quotation montage at all times. Interest eligible to be considered as part of a Market Maker’s Two-Sided Obligation must have a displayed quotation size of at least one normal unit of trading⁷ (or a larger multiple thereof); provided, however, that a Market Maker may augment its Two-Sided Obligation size to display limit orders priced at the same price as the Two-Sided Obligation. After an execution against its Two-Sided Obligation, a Market Maker must ensure that additional trading interest exists in PSX to satisfy its Two-Sided Obligation either by immediately entering new interest to comply with this obligation to maintain continuous two-sided quotations or by identifying existing interest on the PSX book that will satisfy this obligation.

For NMS stocks a Market Maker shall adhere to certain pricing obligations established by the rule, which are premised on entering quotation prices that are not more than a “Designated Percentage”⁸ away from the National Best Bid or Best Offer⁹ (as applicable), and that must be refreshed if a change in the National Best Bid or Best Offer

⁷ Unless otherwise designated, 100 shares.

⁸ The “Designated Percentage” is: (i) 8% for securities included in the S&P 500[®] Index, Russell 1000[®] Index, and a pilot list of Exchange Traded Products (“Tier 1 Securities”); (ii) 28% for all NMS stocks that are not Tier 1 Securities with a price equal to or greater than \$1 (“Tier 2 Securities”); (iii) 30% for all NMS stocks that are not Tier 1 Securities with a price less than \$1 (“Tier 3 Securities”), except that between 9:30 a.m. and 9:45 a.m. and between 3:35 p.m. and the close of trading, the Designated Percentage is 20% for Tier 1 Securities, 28% for Tier 2 Securities, and 30% for Tier 3 Securities. The Designated Percentage for rights and warrants is 30%. The pilot list of Exchange Traded Products for Tier 1 Securities is attached as Exhibit 3 to this filing.

⁹ Determined by the Exchange in accordance with its procedures for determining Protected Quotations under SEC Rule 600 under Regulation NMS.

causes the quotation price to be more than a “Defined Limit”¹⁰ away from the National Best Bid or Best Offer.¹¹ As described below, the applicable Designated Percentage and Defined Limit depends [sic] on the specific security traded and the time of day. For bid quotations, at the time of entry of bid interest satisfying the Two-Sided Obligation, the price of the bid interest may not be more than the applicable Designated Percentage away from the then current National Best Bid, or if no National Best Bid, not more than the Designated Percentage away from the last reported sale from the responsible single plan securities information processor. In the event that the National Best Bid (or if no National Best Bid, the last reported sale) increases to a level that would cause the bid interest of the Two-Sided Obligation to be more than the Defined Limit away from the National Best Bid (or if no National Best Bid, the last reported sale), or if the bid is executed or cancelled, the Market Maker shall enter new bid interest at a price not more than the Designated Percentage away from the then current National Best Bid (or if no National Best Bid, the last reported sale), or identify to the Exchange current resting interest that satisfies the Two-Sided Obligation. Similarly, for offer quotations, at the time of entry of offer interest satisfying the Two-Sided Obligation, the price of the offer interest may not be more than the Designated Percentage away from the then current National Best Offer, or if no National Best Offer, not more than the Designated Percentage away from the last reported sale received from the responsible single plan

¹⁰ The “Defined Limit” is 9.5% for Tier 1 Securities, 29.5% for Tier 2 Securities, and 31.5% for Tier 3 Securities, except that between 9:30 a.m. and 9:45 a.m. and between 3:35 p.m. and the close of trading, the Defined Limit is 21.5% for Tier 1 Securities, 29.5% for Tier 2 Securities, and 31.5% for Tier 3 Securities.

¹¹ Nothing in the rule precludes a PSX Market Maker from quoting at price levels that are closer to the National Best Bid and Offer than the levels required by the rule.

securities information processor. In the event that the National Best Offer (or if no National Best Offer, the last reported sale) decreases to a level that would cause the offer interest of the Two-Sided Obligation to be more than the Defined Limit away from the National Best Offer (or if no National Best Offer, the last reported sale), or if the offer is executed or cancelled, the Market Maker shall enter new offer interest at a price not more than the Designated Percentage away from the then current National Best Offer (or if no National Best Offer, the last reported sale), or identify to the Exchange current resting interest that satisfies the Two-Sided Obligation.

The pricing obligations established by the Rule apply during regular trading hours (i.e., 9:30 a.m. to 4:00 p.m.); but do not commence during any trading day until after the first regular way transaction on the primary listing market in the security. Moreover, the obligations are suspended during a trading halt, suspension, or pause, and do not recommence until after the first regular way transaction on the primary listing market in the security following such halt, suspension, or pause, as reported by the responsible single plan processor.

The individual MPID assigned to a member organization to meet its Two-Sided Obligation pursuant to the Rule, or Rule 3223,¹² is referred to as the member organization's "Primary MPID." Market Makers and ECNs may request the use of additional MPIDs that shall be referred to as "Supplemental MPIDs." A Market Maker may request the use of Supplemental MPIDs for displaying Attributable Quotes/Orders¹³

¹² An existing rule governing the use of PSX by electronic communications networks ("ECNs") and other forms of alternative trading systems to display orders.

¹³ A Quote/Order whose price and size is displayed next to the Market Maker's MPID in the publicly disseminated quotation montage.

in the PSX Quotation Montage for any security in which it is registered and meets the obligations set forth in subparagraph (1) of this rule. An ECN may request the use of Supplemental MPIDs for displaying Attributable Quotes/Orders in the PSX Quotation Montage for any security in which it meets the obligations set forth in Rule 3223. A Market Maker or ECN that ceases to meet the obligations appurtenant to its Primary MPID in any security shall not be permitted to use a Supplemental MPID for any purpose in that security.¹⁴

As provided in new Rule 3213(c), if a PSX Market Maker's ability to enter or update quotations is impaired, the market maker must immediately contact PSX Market Operations to request a withdrawal of its quotations. If the market maker elects to remain in PSX when its ability to update quotations is impaired, it must nevertheless execute orders presented for execution against its disseminated quotations.

The procedures for withdrawal of quotations are governed by proposed new Rule 3219. In general, a market maker that wishes to withdraw quotations in a security must contact the Exchange's MarketWatch Department to obtain excused withdrawal status prior to withdrawing its quotations. Withdrawals of quotations shall be granted by MarketWatch only upon satisfying one of the conditions specified in this Rule. An exception to the requirement for prior approval will exist for withdrawal based on a PSX Market Maker's systemic equipment problems, such as defects in software or hardware systems or connectivity problems associated with the circuits connecting PSX systems

¹⁴ Market Makers and ECNs that are permitted the use of Supplemental MPIDs for displaying Attributable Quotes/Orders are subject to the same rules applicable to their first quotation, with two exceptions: (a) the continuous two-sided quote requirement and excused withdrawal procedures do not apply to Market Makers' Supplemental MPIDs; and (b) Supplemental MPIDs may not be used by Market Makers to enter stabilizing bids pursuant to Rule 3214.

with the PSX Market Maker's systems. In that case, the market maker must promptly contact Exchange Market Operations and may receive excused withdrawal status for up to five (5) business days (unless extended by Exchange Market Operations).

For other circumstances beyond the market maker's control, a PSX Market Maker that wishes to withdraw quotations must contact the Exchange's MarketWatch Department to obtain excused withdrawal status prior to withdrawing its quotations.¹⁵ Excused withdrawal status based on illness, vacations or physical circumstances beyond the PSX Market Maker's control may be granted for up to five (5) business days, unless extended by MarketWatch. Excused withdrawal status based on investment activity or advice of legal counsel, accompanied by a representation that the condition necessitating the withdrawal of quotations is not permanent in nature, may, upon written request, be granted for not more than sixty (60) days. The withdrawal of quotations because of pending news, a sudden influx of orders or price changes, or to effect transactions with competitors shall not normally constitute acceptable reasons for granting excused withdrawal status, unless the Exchange has initiated a trading halt for market makers in the security, pursuant to Rule 3100.

Excused withdrawal status may also be granted to a PSX Market Maker that fails to maintain a clearing arrangement with a registered clearing agency or with a member of such an agency and is withdrawn from participation in the trade reporting service of PSX, thereby terminating its registration as a PSX Market Maker; provided, however, that if

¹⁵ It should be noted that because PSX does not currently, and does not at this time propose to list securities, the applicable rule does not establish different standards for excused withdrawals depending the listing venue of the security in question. Cf. NASDAQ Stock Market Rule 4619 (imposing different standards for excused withdrawal of quotations in NASDAQ-listed securities and securities listed on other exchanges).

the Exchange finds that the market maker's failure to maintain a clearing arrangement is voluntary, the withdrawal of quotations will be considered voluntary and unexcused. PSX Market Makers that fail to maintain a clearing relationship will have their PSX system status set to "suspend" and be thereby prevented from entering, or executing against, any quotes/orders in the system.

Proposed Rule 3220 will govern voluntary termination of a PSX Market Maker's registration. A market maker may voluntarily terminate its registration in a security by withdrawing its two-sided quotation from PSX. A PSX Market Maker that voluntarily terminates its registration in a security may not re-register as a market maker for one (1) business day.¹⁶

Notwithstanding the above, a PSX Market Maker that accidentally withdraws as a PSX Market Maker may be reinstated immediately if:

- the PSX Market Maker notified the Exchange's MarketWatch Department of the accidental withdrawal as soon as practicable under the circumstances, but within at least one hour of such withdrawal, and immediately thereafter provided written notification of the withdrawal and reinstatement request;
- it is clear that the withdrawal was inadvertent and the market maker was not attempting to avoid its market making obligations; and

¹⁶ By contrast, under the NASDAQ Stock Market's corresponding rule (NASDAQ Rule 4620), a market maker withdrawing from a NASDAQ-listed security may not re-register in that security for a period of 20 days, but is subject to a one-day exclusion for securities not listed on NASDAQ. Because PSX does not currently, and does not at this time propose to list securities, the proposed one-day exclusion period is comparable to the rule in effect at NASDAQ for securities traded on an unlisted trading privileges basis.

- the PSX Market Maker's firm would not exceed the following reinstatement limitations: (i) for firms that simultaneously made markets in less than 250 stocks during the previous calendar year, the firm can receive no more than two (2) reinstatements per year; (ii) for firms that simultaneously made markets in 250 or more but less than 500 stocks during the previous calendar year, the firm can receive no more than three (3) reinstatements per year; and (iii) for firms that simultaneously made markets in 500 or more stocks during the previous calendar year, the firm can receive no more than six (6) reinstatements per year.

Factors that the Exchange will consider in granting a reinstatement under the rule include, but are not limited to: the number of accidental withdrawals by the PSX Market Maker in the past, as compared with PSX Market Makers making markets in a comparable number of stocks; the similarity between the symbol of the stock that the PSX Market Maker intended to withdraw from and the symbol of the stock that the PSX Market Maker actually withdrew from; market conditions at the time of the withdrawal; whether, given the market conditions at the time of the withdrawal, the withdrawal served to reduce the exposure of the market maker's position in the security at the time of the withdrawal to market risk; and the timeliness with which the PSX Market Maker notified MarketWatch of the error.

A market maker will not be deemed to have voluntarily terminated its registration in a security by voluntarily withdrawing its two-sided quotation from PSX if the PSX Market Maker's two-sided quotation in the subject security is withdrawn by the Exchange's systems due to issuer corporate action related to a dividend, payment or

distribution, or due to a trading halt, and one of the following conditions is satisfied: the PSX Market Maker enters a new two-sided quotation prior to the close of the regular market session on the same day when the Exchange's systems withdrew such a quotation; the PSX Market Maker enters a new two-sided quotation on the day when trading resumes following a trading halt, or, if the resumption of trading occurs when the market is not in regular session, the PSX Market Maker enters a new two-sided quotation prior to the opening of the next regular market session; or upon request from the market maker, MarketWatch authorizes the market maker to enter a new two-sided quotation, provided that MarketWatch receives the market maker's request prior to the close of the regular market session on the next regular trading day after the day on which the market maker became eligible to re-enter a quotation and determines that the market maker was not attempting to avoid its market making obligations by failing to re-enter such a quotation earlier.

Under Rule [sic] 3219 and 3220, the Market Operations Review Committee will have jurisdiction over proceedings brought by market makers seeking review of the denial of an excused withdrawal, the conditions imposed upon a market maker's re-entry, and the denial of a reinstatement following an unexcused withdrawal.

With respect to securities that are the subject of offerings governed by SEC Regulation M,¹⁷ the Exchange is also proposing to adopt several rules. Proposed Rule 3214 governs the entry of stabilizing bids, providing that a PSX Market Maker that intends to stabilize the price of a security that is a subject or reference security under SEC

¹⁷ SEC Rules 100-105 under Regulation M, 17 CFR 242.100 - 242.105.

Rule 101 under Regulation M¹⁸ must submit a request to the Exchange’s MarketWatch Department for entry of a one-sided bid identified as a stabilizing bid. Proposed Rule 3219(e) governs excused withdrawals based on status as a distribution participant or affiliated purchaser within the meaning of Regulation M. The rule provides that a PSX Market Maker may be excused from two-sided quoting obligations in circumstances where a withdrawal of its quotations is necessary to comply with Regulation M by providing appropriate notice to the Exchange’s MarketWatch Department. Proposed Rule 3224 governs imposition of penalty bids or engaging in syndicate covering transactions, providing that a PSX Market Maker acting as a manager (or in a similar capacity) of a distribution of a security that is a subject or reference security under SEC Rule 101 under Regulation M¹⁹ must provide appropriate notice to the Corporate Financing Department of the Financial Industry Regulatory Authority (“FINRA”) of its transactions pursuant to SEC Rule 104 under Regulation M²⁰ prior to imposing the penalty bid or engaging in the first covering transaction. Proposed Rule 3203 adopts associated definitions of terms used in, or in reference to, Regulation M. Although the Exchange expects these rules to be used rarely, if at all, given the fact that the Exchange does not intend to list securities, the rules may have applicability in limited circumstances where an Exchange member organization is acting in support of an offering on another exchange or is affiliated with a member of another exchange that is participating in an offering. Accordingly, the Exchange is adopting rules on these topics that are materially identical to corresponding rules on NASDAQ and BX, with the exception of rules

¹⁸ 17 CFR 242.101.

¹⁹ Id.

²⁰ 17 CFR 242.104.

pertaining to compliance with SEC Rule 103 under Regulation M,²¹ which, by its terms, applies exclusively to the NASDAQ Stock Market.

Phlx is also amending Rule 3230, which governs trading in Commodity-Related Securities,²² to adopt provisions governing the activities of market [sic] makers in Commodity-Related Securities. The rule is designed to ensure that trading in a Commodity-Related Security by a market maker is not improperly influenced by information about trading in the underlying commodity from within the market maker's firm. Under the rule, which is identical to rules in effect [sic] NASDAQ and BX, a member organization acting as a registered market maker in a Commodity-Related Security must establish adequate information barriers when such market maker engages in inter-departmental communications.²³ For purposes of a Commodity-Related Security only, "inter-departmental communications" include communications to other departments within the same firm or the firm's affiliates that involve trading in commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying such Commodity-Related Security.

A member organization acting as a registered market maker in a Commodity-Related Security must file with the Exchange's Regulation Department in a manner

²¹ 17 CFR 242.103.

²² A "Commodity-Related Security" is a security that is issued by a trust, partnership, commodity pool or similar entity that invests, directly or through another entity, in an combination of commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives, or the value of which is determined by the value of commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives.

²³ Member organizations should refer to NASD/NYSE Joint Memo on Chinese Wall Policies and Procedures (NASD Notice to Members 91-45) for guidance on the "minimum elements' of adequate Chinese Wall policy and procedures."

prescribed by such Department and keep current a list identifying all accounts for trading in commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying such Commodity-Related Security, in which the market maker holds an interest, over which it may exercise investment discretion, or in which it shares in the profits and losses. Moreover, a member organization acting as a registered market maker in a Commodity-Related Security may not act or register as a market maker in any commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying such Commodity-Related Security.

A member organization acting as a registered market maker in a Commodity-Related Security must make available to the Exchange's Regulation Department such books, records or other information pertaining to transactions by such entity or registered or non-registered employees affiliated with such entity for its or their own accounts for trading commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying such Commodity-Related Security, as may be requested by the Regulation Department. Finally, in connection with trading a Commodity-Related Security or commodities, futures contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying a Commodity-Related Security, the member organization acting as a market maker in a Commodity-Related Security may not use any material nonpublic information received from any person associated with the member organization or employee of such person regarding trading by such person or employee in the commodities, futures

contracts, options on futures contracts, forward contracts, commodity swaps, or other related derivatives underlying such Commodity-Related Security.

In furtherance of allowing market making on PSX, Phlx is also amending Rule 3301 to provide for attributable quotes and orders (i.e., trading interest displayed with price and size next to a market maker's MPID); to specify that quotations may include a non-displayed reserve size in order to replenish the displayed portion of a quotation when it is reduced to a size of less than one round lot;²⁴ to add definitions of "PSX Market Maker" and "Quote"; and to provide that attributable trading interest will be displayed via PSX data feeds, with attribution to the Participant's MPID, along with non-attributable interest. As provided in proposed new Rule 3306(b), PSX Market Makers and Equities ECNs will be permitted to enter Quotes from 8:00 a.m. to 5 p.m. When open, Quotes will be processed as System Hours Day Orders (i.e., orders that remain open while the PSX System is open, but do not remain on the book overnight). Phlx is also making conforming changes to the following existing rules by adding references to quotations, quotes/orders, market makers, and/or certain activities or market makers, as appropriate to reflect the scope of PSX's rules to embrace market making and quoting activity in addition to order entry: Rule 3100 (Trading Halts on PSX); Rule 3201 (Scope); Rule 3213(b) (Firm Orders and Quotations); Rule 3221 (Suspension and Termination of Quotations and Order Entry); Rule 3225 (Obligation to Provide Information); Rule 3226 (Limitation of Liability); Rule 3301(g) (Order Size); Rule 3306 (Entry and Display of Quotes and Orders); and Rule 3310 (Anonymity).

Minimum Quantity Orders

²⁴ A new timestamp is applied when the order is replenished from reserve size.

Phlx is proposing minor modifications to the operation of PSX's Minimum Quantity Order, such that it will be fully consistent with the comparable orders of NASDAQ and BX. "Minimum Quantity Orders" are orders that will not execute unless a specified minimum quantity of shares can be obtained. A Minimum Quantity Order provides a means by which a market participant may avoid partial executions of orders at sizes that it considers inadequate to achieve its purposes. For example, a market participant seeking to sell a large position in a trading session with high volatility may use the order type to avoid selling only a small portion of the order at the price it considers acceptable. A Minimum Quantity Order that posts to [sic] PSX book will be a Non-Displayed Order, and upon entry must have a size and a minimum quantity condition of at least one round lot. In the event that the shares remaining in the size of the order following a partial execution thereof are less than the minimum quantity specified by the market participant entering the order, the minimum quantity value of the order will be reduced to the number of shares remaining.

Thus, for example, if a market participant entered a Minimum Quantity Order with a size of 1,000 and a minimum quantity of 500, and the order was marketable against a 600 share order on the book, the remaining 400 shares of the Minimum Quantity Order would post to the book with a minimum quantity restriction of 400 shares. Under current PSX rules, if the size of a Minimum Quantity Order is reduced to less than one round lot due to a partial execution, the minimum quantity condition on the order will be removed. PSX proposes to delete this condition, which was formerly necessary to ensure that the order would not have a higher execution priority under PSX's execution algorithm than other non-displayed odd-lot orders solely by virtue of its

minimum quantity condition. In all other respects, the operation of the order will remain unchanged.

Midpoint Peg Post-Only Order

Phlx is adopting as a new order type the Midpoint Peg Post-Only Order.²⁵ Like a regular Midpoint Peg Order, a Midpoint Peg Post-Only Order is a non-displayed order that is priced at the midpoint between the national best bid and best offer (“NBBO”) (as determined using the consolidated tape). However, like a Post-Only Order, the Midpoint Peg Post-Only Order does not remove liquidity from PSX upon entry if it would lock a non-displayed order on PSX. Rather, the Midpoint Peg Post-Only Order will post and lock the pre-existing order, but will remain undisplayed.²⁶ For example, if the NBBO is \$1.10 bid and \$1.11 offer, and there is a non-displayed Midpoint Peg Order to buy on the book at \$1.105, an incoming Midpoint Peg Post-Only Order to sell will also post to the book at \$1.105 and will not execute. By contrast, a regular Midpoint Peg Order would execute against the posted order at \$1.105. If the Midpoint Peg Post-Only Order would cross a pre-existing order, however, the crossing orders will execute.

Midpoint Peg Post-Only Orders that post to the book and lock a pre-existing non-displayed order will execute against an incoming order only if the price of the incoming buy (sell) order is higher (lower) than the price of the pre-existing order. This restriction ensures that the non-displayed Midpoint Peg Post-Only Order will not execute before an

²⁵ The order on PSX will be identical to the comparable order on NASDAQ. See Securities Exchange Act Release No. 64430 (May 6, 2011), 76 FR 27699 (May 12, 2011) (SR-NASDAQ-2011-059); Securities Exchange Act Release No. 68015 (October 9, 2012), 77 FR 63368 (October 16, 2012) (SR-NASDAQ-2012-111).

²⁶ SEC Rule 610(d) under Regulation NMS, 17 CFR 242.610(d), restricts displayed quotations that lock protected quotations in NMS Stocks, but does not apply to non-displayed trading interest.

order already on the book unless the incoming order against which it executes has price priority over the already posted order. For example, if the NBBO is \$1.10 bid and \$1.11 offer, and there is a non-displayed Midpoint Peg Order to buy on the book at \$1.105, an incoming Midpoint Peg Post-Only Order to sell will also post to the book at \$1.105 and will not execute. If another Midpoint Peg Order to buy is entered, it would also post to the book, rather than executing against the Midpoint Peg Post-Only Order. On the other hand, an order to buy at \$1.11 would execute against the Midpoint Peg Post-Only Order, receiving \$0.005 price improvement. Thus, the order provides a means by which a market participant may offer price improvement in exchange for receiving greater certainty with respect to its trading costs.

If a Midpoint Peg Order and a Midpoint Peg Post-Only Order are locked, and a Midpoint Peg Order is entered on the same side of the market as the Midpoint Peg Post-Only Order, the new order will execute against the original Midpoint Peg Order. Thus, in the above example, if a Midpoint Peg Order to buy at \$1.105 is locked by a Midpoint Peg Post-Only Order to sell at \$1.105, a subsequent Midpoint Peg Order to sell at \$1.105 would execute against the original buy order. This is the case because the market participant entering the Midpoint Peg Post-Only Order has expressed its intention not to execute against posted liquidity, and therefore cedes execution priority to the new order.

A Midpoint Peg Post-Only Order will only be posted to the book at a price of more than \$1. Accordingly, if the midpoint between the NBBO for a particular stock is \$1 or less, all Midpoint Peg Post-Only Orders for that stock will be rejected or cancelled, as applicable. This limitation reflects the fact that the difference between the inside market and the midpoint for stocks at this price level is likely to be extremely small, and

therefore the price improvement opportunities associated with the order in such stocks are unlikely to justify making the order available.²⁷

Phlx believes that the Midpoint Peg Post-Only Order will serve a valid purpose in the current market environment. Although SEC Rule 610²⁸ limits access fees, market participants remain focused on their trading costs, and in a pricing environment characterized by fees on one side of a trade being used to fund rebates on the other side,²⁹ it is entirely understandable that some market participants may wish to structure their trading activity in a manner that is more likely to avoid a fee and earn a rebate. In this respect, the order is conceptually similar to a limit order: just as a limit order allows market participants to control the price that they will pay or receive for a stock, the proposed new order will allow market participants to exercise greater control over the fees associated with order execution. Moreover, the order type will operate in a manner calculated to require Participants posting the order generally to provide price improvement in order to justify the ability to earn a rebate. Thus, as long as a Midpoint Peg Post-Only Order is locking a pre-existing Midpoint Order, the order can execute only if it offers price improvement. By means of price improvement, the market participant

²⁷ NASDAQ's corresponding rule includes language stipulating the treatment of posted Midpoint Peg Post-Only Orders for purposes of calculating the best bid and offer within NASDAQ under rules governing the opening cross (NASDAQ Rule 4752), halt and imbalance cross (NASDAQ Rule 4753), and closing cross (NASDAQ Rule 4754). Because PSX does not have comparable rules, this language is omitted from the proposed rule.

²⁸ 17 CFR 242.610.

²⁹ It should be noted that some markets, such as NASDAQ OMX BX, the BATS-Y Exchange, the EDGA Exchange, and CBSX, feature fees for liquidity providers and rebates for liquidity takers, while all other cash equities markets now have a taker fee/maker rebate structure.

effectively shares a portion of its rebate with the counterparty with whom it is matched, thereby reducing its trading costs as well.

Post-Only Orders

Phlx proposes to modify the functionality associated with its existing Post-Only Order on PSX.³⁰ Currently, if a Post-Only Order would lock or cross an order on PSX at the time of entry, the order is re-priced and displayed by the System to one minimum price increment (i.e., \$0.01 or \$0.0001) below the current low offer (for bids) or above the current best bid (for offers). Thus, if the best bid and best offer on the PSX book were \$10.00 x \$10.05, and a market participant entered a Post-Only Order to buy at \$10.05, the order would be re-priced and displayed at \$10.04. This aspect of the functionality of the order is not changing.³¹ Under the proposed change, if a Post-Only Order would cross an order on the System, the order will be repriced as described above unless the value of price improvement associated with executing against a resting order

³⁰ An identical change was mistakenly filed by Phlx (Securities Exchange Act Release No. 64563 (May 27, 2011), 76 FR 32255 (June 3, 2011) (SR-Phlx-2011-70)) at the same time as the change was made by NASDAQ (Securities Exchange Act Release No. 64552 (May 26, 2011), 76 FR 31998 (June 2, 2011) (SR-NASDAQ-2011-070)), with the error being corrected through a subsequent filing (Securities Exchange Act Release No. 67351 (July 5, 2012), 77 FR 40922 (July 11, 2012) (SR-Phlx-2012-84)). The prior filing to make this change was mistaken because the proposed change was incompatible with PSX's price/size/pro rata algorithm. With PSX's move to a price/time algorithm, the change to the functioning of the Post-Only Order is now possible.

³¹ In addition, if the order would lock or cross a protected quotation of another market center, the order will be accepted at the locking price (i.e., the current low offer (for bids) or to [sic] the current best bid (for offers)) and displayed by the System to one minimum price increment (i.e., \$0.01 or \$0.0001) below the current low offer (for bids) or above the current best bid (for offers). Thus, if the national best bid and offer, as displayed on another market center, was \$10 x \$10.05, an order to buy at \$10.05 or higher would be accepted at the locking price of \$10.05, but would be displayed at \$10.04. Subsequently, an incoming order to sell at \$10.05 or lower would be matched against the Post-Only buy order. In this case, the incoming sell order would receive price improvement.

equals or exceeds the sum of fees charged for such execution and the value of any rebate that would be provided if the order posted to the book and subsequently provided liquidity, in which case the order will execute.

As provided by Rule 3307, in such an instance the price improvement accrues to the party entering the order that takes liquidity. Thus, if a sell order is on the book at \$10 and a Post-Only Order to buy at \$10.01 is entered, the Post-Only Order will execute at \$10.

The modified Post-Only Order will serve to allow the market participant entering the order to post its order at its desired price, unless the amount of price improvement makes execution of the order economically advantageous to the entering participant. Thus, the revised order type is designed to provide market participants with better control over their execution costs and to provide them with a means to offer price improvement opportunities to other market participants.

Minimum Life Order

Phlx is proposing to eliminate PSX's Minimum Life Order. The Minimum Life Order is a Displayed Order that may not be cancelled for a period of 100 milliseconds following its receipt. The order type was not used by the vast majority of PSX's market participants, and is not currently offered by any other national securities exchange. Accordingly, PSX believes that its elimination will not have any material effect on market participants or on the cash equities markets in general.

Price to Comply Post Order

Phlx is proposing to introduce the Price to Comply Post Order on PSX, with terms and conditions identical to those found on NASDAQ and BX. The Price to Comply Post

Order provides a straightforward means by which market makers and others may post liquidity at or near the inside market in compliance with the restrictions on locked and crossed markets and trade-throughs under Rules 610(d) and 611 under Regulation NMS.³² If, at the time of its entry, a Price to Comply Post Order would lock or cross the Protected Quotation of another trading center or would execute at a price inferior to the Protected Quotation of another trading center, the order will be re-priced and displayed to one minimum price increment (i.e., \$0.01 or \$0.0001, depending on the price of the security being traded) below the current low offer (for bids) or to one penny above the current best bid (for offers). Price to Comply Post Orders are not routable.³³

2. Statutory Basis

Phlx believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,³⁴ in general, and with Section 6(b)(5) of the Act³⁵ in particular, in that the proposal 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 regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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.

The proposed adoption of [sic] price/time execution algorithm will allow PSX to operate in a manner consistent with every other national securities exchange that trades

³² 17 CFR 242.610(d), 611.

³³ With respect to the foregoing changes to the availability of order types, Phlx is amending Rule 3305 to reflect the changes in a list of available order types.

³⁴ 15 U.S.C. 78f.

³⁵ 15 U.S.C. 78f(b)(5).

cash equities securities, a market model that the Commission has repeatedly determined to be consistent with the Act.³⁶ Thus, the change with regard to the execution algorithm will remove impediments to and perfect the mechanism of a free and open market and a national market system by making PSX's functionality more consistent with that of other exchanges. Similarly, the proposed rules regarding maker [sic] making, including the obligations of market makers to adhere to specific quoting and pricing obligations, have previously been determined by the Commission to be consistent with the Act.³⁷

Specifically, in approving rules governing market maker quoting and pricing obligations such as those proposed by Phlx, the Commission found that "the proposed rule should assure that quotations submitted by market makers to an exchange or FINRA's ADF, and displayed to market participants, bear some relationship to the prevailing market price, and thus should promote fair and orderly markets and the protection of investors."³⁸

The proposed changes to order type functionality will remove impediments to and perfect the mechanism of a free and open market and the national market system because

³⁶ See, e.g., Securities Exchange Act Release No. 54155 (July 14, 2006), 71 FR 41291 (July 20, 2006) (SR-NASDAQ-2006-001); Securities Exchange Act Release No. 59154 (December 23, 2008), 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48).

³⁷ See, e.g., Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006) (File No. 10-131) (approving NASDAQ market maker rules as part of its registration as a national securities exchange); Securities Exchange Act Release No. 59154 (December 23, 2008), 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48); Securities Exchange Act Release No. 63255 (November 5, 2010), 75 FR 69484, 69485 (November 12, 2010) (SR-BATS-2010-025, SR-BX-2010-66, SR-CBOE-2010-087, SR-CHX-2010-22, SR-FINRA-2010-049, SR-NASDAQ-2010-115, SR-NSX-2010-12, SR-NYSE-2010-69, SR-NYSEAmex-2010-96, SR-NYSEArca-2010-83) (approving corresponding marketwide rules with respect to market maker quoting and pricing obligations) ("2010 Order").

³⁸ 2010 Order, 75 FR at 69485.

they will conform PSX's rules to functionality that is already in use and accepted by market participants at other exchanges. Specifically, with regard to the change to the Minimum Quantity Order, the proposed change will allow the operation of the order to better reflect the intention of the market participants entering the order, since it will allow a minimum quantity condition to continue to attach to an order at a size below one round lot. The change will also make the operation of the order conform to functionality that was implemented on an immediately effective basis on NASDAQ and BX.³⁹

Similarly, the proposed Midpoint Peg Post-Only Order is identical to the order that is operative on NASDAQ, and which was introduced and modified through immediately effective filings.⁴⁰ As described in the original NASDAQ filing with respect to the order, the Midpoint Peg Post-Only Order is designed to provide market participants with better control over their execution costs and to provide a means to offer price improvement opportunities.

The modified Post Only Order, which adopts changes filed by NASDAQ and BX on an immediately effective basis,⁴¹ is similarly designed to provide market participants with better control over their execution costs. Specifically, the changes will ensure that a Post Only Order will post to the PSX book only in circumstances where an immediate

³⁹ Securities Exchange Act Release No. 65536 (October 12, 2011), 76 FR 64411 (October 18, 2011) (SR-NASDAQ-2011-140); Securities Exchange Act Release No. 65535 (October 12, 2011), 76 FR 64416 (October 18, 2011) (SR-BX-2011-069).

⁴⁰ See Securities Exchange Act Release No. 64430 (May 6, 2011), 76 FR 27699 (May 12, 2011) (SR-NASDAQ-2011-059); Securities Exchange Act Release No. 68015 (October 9, 2012), 77 FR 63368 (October 16, 2012) (SR-NASDAQ-2012-111).

⁴¹ Securities Exchange Act Release No. 64552 (May 26, 2011), 76 FR 31998 (June 2, 2011) (SR-NASDAQ-2011-070); Securities Exchange Act Release No. 64615 (June 7, 2011), 76 FR 34284 (June 13, 2011) (SR-BX-2011-033).

execution of the order would not be more economically advantageous to the market participant that entered it.

The proposed Price to Comply Post Order is consistent with the Act because it provides market makers and other market participants with a straightforward mechanism to enter an order that reprices to ensure that it does not lock or cross or trade through the Protected Quotation of another market center. The rule has previously been approved for use at NASDAQ and BX.⁴²

Finally, Phlx believes that the proposed elimination of the Minimum Life Order is consistent with the Act because the order has not been widely used and has not been adopted at any other exchange. Accordingly, Phlx believes that offering an order of this nature is not a required aspect of the operation of a national securities exchange.

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

Phlx does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. Specifically, since its introduction with a price/size execution algorithm, PSX has not been a significant competitor in the market for execution of cash equities orders, with a market share generally below 1 percent of total consolidated volume. By means of the changes proposed in this rule filing, Phlx hopes to enhance PSX's competitiveness by offering functionality that is more consistent with that offered by other national securities exchanges. In light of the highly competitive nature of these markets, however, PSX will be successful in attracting additional order flow only if its

⁴² Securities Exchange Act Release No. 54155 (July 14, 2006), 71 FR 41291 (July 20, 2006) (SR-NASDAQ-2006-001); Securities Exchange Act Release No. 59154 (December 23, 2008), 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48).

overall offering of functionality and pricing is successful in convincing market participants to direct order flow to it, rather than the larger number of exchanges and alternative trading systems that compete with it. Accordingly, Phlx does not believe that the changes proposed herein will impose any burden on competition, because they do not provide any means through which PSX may diminish the free choice with regard to order routing decisions that exists in the market. To the extent, however, that the changes make PSX a more attractive trading venue, they have the potential to enhance competition by providing market participants with additional choices when making such decisions.

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

Written comments were neither solicited nor received.

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. Please include File Number SR-Phlx-2013-24 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-2013-24. 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 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-2013-24 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.⁴³

Kevin M. O'Neill
Deputy Secretary

⁴³ 17 CFR 200.30-3(a)(12).