

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-77245; File No. SR-Phlx-2016-23)

February 26, 2016

Self-Regulatory Organizations; NASDAQ OMX PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Adopt a Kill Switch

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup>, and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 16, 2016, 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 the Substance of the Proposed Rule Change

The Exchange proposes to relocate language in current Rule 1035, entitled “Acceptable of Bid or Offer” [sic] to Phlx Rule 1019 and adopt an optional Kill Switch protection. The Kill Switch will allow Phlx members to remove quotes and cancel open orders and prevent new order submission.

The text of the proposed rule change is available on the Exchange’s website at <http://nasdaqomxphlx.cchwallstreet.com/>, 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

The Exchange proposes to adopt a new risk protection, a Kill Switch, applicable to all Phlx members and member organizations (hereinafter “member(s)”). The Kill Switch will allow Phlx members to remove quotes and cancel open orders and prevent new order submission. This feature provides firms with a powerful risk management tool for immediate control of their quote and order activity.

The Exchange proposes to relocate current Rule 1035, entitled “Acceptable of Bid or Offer” [sic] to currently reserved Rule 1019, title revised Rule 1019 “Acceptance of Bid or Offer,” and add a new section (b) to Rule 1019. The Phlx Options Kill Switch will be an optional tool that enables Phlx members to initiate a message(s)<sup>3</sup> to the Phlx XL system (“System”) to: (i) promptly remove quotes; and/or (ii) promptly cancel orders. Phlx members may submit a request to the System to remove/cancel quotes and/or orders based on certain identifiers on either a user or group level. Phlx members may elect to remove quotes and cancel

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<sup>3</sup> Phlx members will be able to utilize an interface to send a message to the Exchange to initiate the Kill Switch or they may contact the Exchange directly.

orders by Exchange account, port, and/or badge or mnemonic (“Identifier”) or by a group (one or more Identifier combinations),<sup>4</sup> which are provided by such Phlx member to the Exchange. Phlx members may not remove quotes/orders by symbol. The System will send an automated message to the Phlx member when a Kill Switch request has been processed by the Exchange’s System.

If the Phlx member selects quotes to be cancelled utilizing the Kill Switch, the Phlx member must send a message to the Exchange to request the removal of all quotes requested for the specified Identifier(s).<sup>5</sup> The Phlx member will be unable to enter any additional quotes for the affected Identifier(s) until re-entry has been enabled pursuant to proposed section (b)(iii).<sup>6</sup>

If the Phlx member selects orders to be cancelled utilizing the Kill Switch, the Phlx member must send a message to the Exchange to request the cancellation of all orders requested for the certain specified Identifier(s).<sup>7</sup> The Phlx member will be unable to enter additional orders for the affected Identifier(s) until re-entry has been enabled pursuant to section (b)(iii).

Proposed section (b)(iii) stipulates that after quotes and/or orders are removed/cancelled by the Phlx member utilizing the Kill Switch, the Phlx member will be unable to enter additional quotes and/or orders for the affected Identifier(s) until the Phlx member has made a request to the Exchange and Exchange staff has set a re-entry indicator to enable re-entry.<sup>8</sup> Once enabled

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<sup>4</sup> The type of group permissible would be within a broker-dealer. For example, this could be including but not limited to all market maker accounts or all order entry ports.

<sup>5</sup> See note 3.

<sup>6</sup> PIXL Orders will not be cancelled. PIXL<sup>SM</sup> is the Exchange’s price improvement mechanism known as Price Improvement XL or PIXL. See Rule 1080(n). Of note, sweeps will be cancelled. A sweep is a one-sided electronic quote submitted over the Specialized Quote Feed, which is the market making quoting interface.

<sup>7</sup> See note 3.

<sup>8</sup> The Phlx member must directly and verbally contact the Exchange to request the re-set.

for re-entry, the System will send a Re-entry Notification Message to the Phlx member. The applicable Clearing member for that Phlx member also will be notified of the re-entry into the System after quotes and/or orders are removed/cancelled as a result of the Kill Switch, provided the Clearing member has requested to receive such notification.

The Exchange offers many risk mitigation and management tools today including, but not limited to, certain rapid fire risk controls,<sup>9</sup> Rule 15c3-5 risk controls,<sup>10</sup> Order Price Protections,<sup>11</sup> and cancel on disconnect and purge functionality for Specialized Quote Feed (SQF). The Kill Switch offers members a means to control their exposure, through an interface which is not dependent on the integrity of the member's own systems, should the member experience a failure.

The Exchange proposes to implement this rule within ninety (90) days of the implementation date. The Exchange will issue an Options Trader Alert in advance to inform market participants of such date.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>12</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>13</sup> in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect

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<sup>9</sup> See Phlx Rule 1095.

<sup>10</sup> See §240.15c3-5.

<sup>11</sup> See Phlx Rule 1084.

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

<sup>13</sup> 15 U.S.C. 78f(b)(5).

investors and the public interest, by enhancing the risk protections available to Exchange members. The proposal promotes policy goals of the Commission which has encouraged execution venues, exchange and non-exchange alike, to enhance risk protection tools and other mechanisms to decrease risk and increase stability.

The individual firm benefits of enhanced risk protections flow downstream to counter-parties both at the Exchange and at other options exchanges, thereby increasing systemic protections as well. Additionally, because the Exchange offers this risk tool to all Phlx members, the Exchange believes this will allow Phlx members to enter quotes and orders without fear of inadvertent exposure to excessive risk, which in turn will benefit investors through increased liquidity for the execution of their orders, thereby protecting investors and the public interest.

This optional risk tool as noted above will be offered to all Phlx members. The Exchange further represents that its proposal will operate consistently with the firm quote obligations of a broker-dealer pursuant to Rule 602 of Regulation NMS and that the functionality is not mandatory. Specifically, any interest that is executable against a Phlx member's quotes and orders that are received<sup>14</sup> by the Exchange prior to the time the Kill Switch is processed by the System will automatically execute at the price up to the Phlx member's size. The Kill Switch message will be accepted by the System in the order of receipt in the queue and will be processed in that order so that interest that is already accepted into the System will be processed prior to the Kill Switch message.

A Market Makers' obligation to provide continuous two-sided quotes on a daily basis is not diminished by the removal of such quotes and/or orders by utilizing the Kill Switch. Market Makers will be required to provide continuous two-sided quotes on a daily basis. Market Makers

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<sup>14</sup> The time of receipt for an order or quote is the time such message is processed by the Exchange Order Book.

that utilize the Kill Switch will not be relieved of the obligation to provide continuous two-sided quotes on a daily basis, nor will it prohibit the Exchange from taking disciplinary action against a Market Maker for failing to meet the continuous quoting obligation each trading day.

With respect to providing information regarding the removal of quotes and/or cancellation of orders as a result of the Kill Switch to the Clearing Member, each Member that transacts through a Clearing Member on the Exchange executes a Letter of Guarantee wherein the Clearing Member accepts financial responsibility for all Exchange transactions made by the Phlx member on whose behalf the Clearing Member submits the Letter of Guarantee. The Exchange believes that because Clearing Members guarantee all transactions on behalf of a member, and therefore bear the risk associated with those transactions, it is appropriate for Clearing members to have knowledge of the utilization by the member of the Kill Switch, should the Clearing member request such notification.

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. The proposal does not impose an undue burden on intra-market competition because all Phlx members may avail themselves of the Kill Switch. The Kill Switch functionality is optional. The proposed rule change is meant to protect Phlx members in the event the Phlx member is suffering from a systems issue or from the occurrence of unusual or unexpected market activity that would require them to withdraw from the market in order to protect investors. The ability to control risk at either the user or group level will permit the Phlx member to protect itself from inadvertent exposure to excessive risk at each level. Reducing such risk will enable Phlx members to enter quotes and orders without fear of inadvertent exposure to excessive risk, which in turn will

benefit investors through increased liquidity for the execution of their orders. Such increased liquidity benefits investors because they receive better prices and because it lowers volatility in the options market. For these reasons, the Exchange does not believe this proposal imposes an undue burden on inter-market competition because other exchanges offer the same functionality.

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 from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>15</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>16</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: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) 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.

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

<sup>16</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.

#### 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-2016-23 on the subject line.

##### Paper comments:

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

All submissions should refer to File Number SR-Phlx-2016-23. 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 available publicly. All submissions should refer to File Number SR-Phlx-2016-23, 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>17</sup>

Robert W. Errett  
Deputy Secretary

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