

**SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50901; File No. SR-Phlx-2004-84)**

December 21, 2004

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. to Eliminate the Public Order Exposure System Functionality from Phlx Rule 229

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on November 26, 2004, the Philadelphia Stock Exchange, Inc. (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. 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 Phlx proposes to eliminate the Public Order Exposure System (“POES”) functionality from Phlx Rule 229. The text of amended Exchange Rule 229 is set forth below. Brackets indicate deletions; italics indicate additions.

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Rule 229. Philadelphia Stock Exchange Automated Communication and Execution System (PACE)

Supplementary Material: ...

.01-.04 No Change.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

.05 [Public Order Exposure System --]Subject to Supplementary Material Section .07, all round-lot market orders up to 500 shares and PRL market orders up to 599 shares entered after the opening will be automatically executed at the PACE Quote. [will be stopped at the PACE Quote at the time of entry into the system ("Stop Price") and be subject to a delay of up to 30 seconds from being executed in order to receive an opportunity for price improvement. If such market order is not executed within the 30 second window, the order will be automatically executed at the Stop Price. If the PACE Quote at the time of order entry into the system reflects a point spread (the difference between the best bid and offer) of \$.05 or less for equities trading in decimals, pursuant to Rule 134 or 125, that order will be executed immediately without the 30 second delay.]

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.06 No Change

.07 (a)-(b) No Change

(c) Price Improvement for PACE Orders

(i) Automatic Price Improvement --Where the specialist voluntarily agrees to provide automatic price improvement to all customers and all eligible market orders in a security, automatically executable market and marketable limit orders in New York Stock Exchange and American Stock Exchange listed securities received through PACE for 599 shares or less shall be provided with automatic price improvement from the PACE Quote when received either \$.01 or a percentage of the PACE Quote when the order is received for equities trading in decimals beginning at 9:30 A.M., except where:

(A) a buy order would be improved to a price less than the last sale (except as provided in ([F]E) below) or a sell order would be improved to a price higher than the last sale (except as provided in ([E]D) below); or

(B) a buy order would be improved to the last sale price which is a downtick (except as provided in ([F]E) below) or a sell order would be improved to the last sale price which is an uptick (except as provided in ([E]D) below). The PACE System will determine whether the last sale price is a downtick or an uptick. The PACE System does not recognize changes from the previous day's close.

In these situations, the order is not eligible for automatic price improvement, and is, instead, automatically executed at the PACE Quote. A specialist may voluntarily agree to provide automatic price improvement to larger orders in a particular security to all customers under this provision.

A specialist may choose to provide automatic price improvement of: (i) \$.01 where the PACE Quote is either \$.05 or greater, or \$.03 or greater, or (ii) where the PACE Quote is \$.02 or greater, a percentage of the PACE Quote when the order is received, up to 50%, rounded to the nearest penny, and at least \$.01, in a particular security to all customers.

(C) Automatic price improvement will not occur for odd-lot orders, nor where the execution price before or after the application of automatic price improvement would be outside the primary market high/low range for the day, if so elected by the entering member organization.

(D) [The POES window of Supplementary Material .05 above does not apply where an order is subject to automatic price improvement or manual price protection.

(E)]Sell Order Enhancement I --A specialist may choose to give automatic price improvement to all sell orders of 100 shares or more, as determined by the specialist, in a particular security which would be improved to the last sale on an uptick; or

Sell Order Enhancement II --A specialist may choose to give automatic price improvement to all sell orders of 100 shares or more, as determined by the specialist, in a particular security which would be improved to a price higher than the last sale.

([F]E) Buy Order Enhancement - A specialist may choose to give automatic price improvement to all buy orders, as determined by the specialist, in any security that is exempted from or otherwise not subject to Securities Exchange Act Rule 10a-1.

(c)(ii)-(iv) No Change

.08-.22 No Change

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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 Phlx 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 Phlx has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

The purpose of the proposed rule change is to reduce the time between order receipt and execution for market orders, thereby improving order turnaround time, and to reduce the number of manual orders. Currently, Phlx Rule 229, Supplementary Material .05, provides that if the PACE³ Quote⁴ at the time of order entry into the system reflects a point spread (the difference between the best bid and offer) of more than \$.05, round-lot market orders up to 500 shares and PRL⁵ market orders up to 599 shares will be stopped at the PACE Quote at the time of entry into the system ("Stop Price") and be subject to a delay of up to 30 seconds from being executed in order to receive an opportunity for price improvement. During that time, specialists may, but are not required to, improve the execution price of the order to a price better than the Stop Price. If such market order is not executed within the 30-second window, the order will be automatically executed at the Stop Price. If the PACE Quote at the time of order entry into the system reflects a point spread of \$.05 or less, that order would be executed immediately without the 30-second delay.

Since the creation of POES,⁶ the Exchange has adopted other means of price

³ PACE is the Exchange's automated order routing, delivery, execution and reporting system for equities. See Phlx Rule 229.

⁴ The PACE Quote means the best bid/ask quote among the American, Boston, National, Chicago, New York, Pacific, or Philadelphia Stock Exchanges, or the Intermarket Trading System/Computer Assisted Execution System ("ITS/CAES") quote, as appropriate. See Phlx Rule 229.

⁵ PRL means a combined round-lot and odd-lot order. See Phlx Rule 229.

⁶ See Securities Exchange Act Release No. 35283 (January 26, 1995), 60 FR 6333 (February 1, 1995) (SR-Phlx-94-58).

improvement known as automatic price improvement (“API”) and manual price protection that may apply in certain situations.⁷ Pursuant to Phlx Rule 229, Supplementary Material .07(c)(i)(D), the POES window does not apply where an order is subject to API or manual price protection. However, some orders are still subject to the window, which means that these otherwise automatically executable orders drop to manual for a period of 30 seconds waiting for specialists to manually price improve them, after which they are executed. Eliminating the POES functionality will eliminate the 30 second waiting time for automatic execution and allow such orders to be automatically executed at the PACE quote. Specialists who are interested in offering automatic price improvement will still have the Exchange’s API available to them on a symbol-by-symbol basis, as they do today.⁸

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act⁹ in general, and furthers the objectives of Section 6(b)(5) of the Act¹⁰ in particular, in that it should promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market, and protect investors and the public interest by improving order turnaround time and reducing the number of manual orders.

⁷ See Securities Exchange Act Release No. 39548 (January 13, 1998), 63 FR 3596 (January 23, 1998) (SR-Phlx-97-23).

⁸ Additionally, manual price improvement will continue to be available to specialists when certain conditions are met. See Phlx Rule 229, Supplementary Material .07(c)(ii). According to the Phlx, because of the existence of these other means of price improvement (API and manual), the POES system is rarely used by the specialists as a method of price improvement. Telephone conversation between John Dayton, Assistant Secretary and Counsel, Phlx, and Angela Muehr, Attorney, Division of Market Regulation, Commission, on December 9, 2004.

⁹ 15 U.S.C. 78f(b).

¹⁰ 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 inappropriate burden on competition.

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

Within 35 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 will:

- (A) by order approve 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, as amended, 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-2004-84 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-Phlx-2004-84. 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 inspection and copying in the Commission's Public Reference Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the Phlx. 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-2004-84 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹¹

Margaret H. McFarland
Deputy Secretary

¹¹ 17 CFR 200.30-3(a)(12).