

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-51718; File No. SR-Phlx-2004-65)

May 19, 2005

Self-Regulatory Organizations; Philadelphia Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change and Amendment Nos. 1, 2 and 3 Thereto Relating to Backup Trading Arrangements

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹, and Rule 19b-4² thereunder, notice is hereby given that on October 18, 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. On April 29, 2005, the Exchange submitted Amendment No. 1 to the proposal.³ On May 12, 2005, the Exchange submitted Amendment No. 2 to the proposal.⁴ On May 16, 2005, the Exchange submitted Amendment No. 3 to the proposal.⁵ The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, the Exchange substantially revised the proposed rule text and added a new paragraph (d), Member Proceedings, to establish disciplinary jurisdiction as between the Disabled Exchange and the Back-up Exchange in situations where there is an ongoing disciplinary action involving a member of the Disabled Exchange at the time of termination of the back-up period. The Exchange also proposed amendments to its fee schedules, which incorporate Rule 99.

⁴ In Amendment No. 2, the Exchange made minor revisions to the proposed rule text and corresponding description of the proposal. Phlx also refiled corrected versions of the exhibits submitted with the proposal. Amendment No. 2 replaces and supersedes Phlx’s earlier submissions in their entirety.

⁵ In Amendment No. 3, the Exchange submitted a revised Exhibit 5 to its amended Form 19b-4 to correctly identify the new rule text in the proposal, including Exchange Rule 99 and changes to the Phlx Fee Schedule.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Phlx proposes to adopt a rule that will permit Phlx to enter into arrangements with one or more other exchanges that would provide trading facilities for Phlx listed options at another exchange in the event that the functions of Phlx are severely and adversely affected by an emergency or extraordinary circumstances (a “Disabling Event”), and similarly provide trading facilities at Phlx for another exchange to trade its listed options if that exchange’s facility experiences a Disabling Event. Additionally, the Exchange has submitted a corresponding back-up trading agreement between itself and the Chicago Board Options Exchange, Incorporated (“CBOE”) as Exhibit B to its Form 19b-4 filing. This back-up trading agreement is available for viewing on the Commission’s Web site, www.sec.gov/rules/sro.shtml, and at the Exchange and the Commission.⁶

The Exchange also proposes an amendment to its Fee Schedule relative to the fees that shall apply to transactions in the options of a Disabled Exchange effected on a Back-up Exchange.

The text of the proposed rule change is set forth below. Proposed new language is in italics.

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Backup Trading Arrangements

Rule 99

(a) Phlx is Disabled Exchange.

(i) Exchange (“Phlx”) Exclusively Listed Options.

⁶ See infra note 10. The Commission notes that the text of the back-up trading agreement that appears on the Commission’s Web site was filed as part of Amendment No. 2.

(A) For purposes of this Rule 99, the term “exclusively listed option” means an option that is listed exclusively by an exchange (because such exchange has an exclusive license to use, or has proprietary rights in, the interest underlying the option).

(B) The Phlx may enter into arrangements with one or more other exchanges (each a “Backup Exchange”) to permit the Phlx and its members and associated persons and other personnel to use a portion of the Backup Exchange’s facilities to conduct the trading of some or all of the Phlx’s exclusively listed options in the event that the functions of the Phlx are, or are threatened to be, severely and adversely affected by an emergency or extraordinary circumstances (a “Disabling Event”). Such options shall trade as listings of Phlx. The facility of the Backup Exchange used by the Phlx for this purpose will be deemed to be a facility of the Phlx.

(C) Trading of Phlx exclusively listed options shall be conducted in accordance with the rules of the Backup Exchange, except that such trading shall be subject to Phlx rules with respect to doing business with the public, margin requirements, net capital requirements, listing requirements, and position limits. In addition, the Phlx and the Backup Exchange may agree that other rules of the Phlx will apply to such trading. The Phlx and the Backup Exchange have agreed to communicate to their respective members which rules apply in advance of trading. The Backup Exchange rules that govern trading on Phlx’s facility at the Back-up Exchange shall be deemed to be Phlx rules for purposes of such trading.

(D) The Back-up Exchange has agreed to perform the related regulatory functions with respect to trading of Phlx exclusively listed options on Phlx’s facility at the Back-up Exchange, in each case except as Phlx and the Back-up Exchange may specifically agree

otherwise. The Back-up Exchange and Phlx have agreed to coordinate with each other regarding surveillance and enforcement respecting trading of Phlx exclusively listed options on Phlx's facility at the Back-up Exchange. Phlx shall retain the ultimate legal responsibility for the performance of its self-regulatory obligations with respect to Phlx's facility at the Back-up Exchange.

(E) If the Backup Exchange is unable to accommodate all Phlx members that desire to trade on Phlx's facility at the Backup Exchange pursuant to paragraph (a)(i)(A), the Phlx may determine which members shall be eligible to trade at that facility. Factors to be considered in making such determinations may include, but are not limited to, any one or more of the following: whether the member is a specialist in the applicable product(s), the number of contracts traded by the member or member organization in the applicable product(s), market performance, and other factors relating to a member's contribution to the market in the applicable product(s) during a specific period.

(F) Members of the Backup Exchange shall not be authorized to trade in any Phlx exclusively listed options, except that (i) Phlx may deputize willing floor brokers of the Back-up Exchange as temporary Phlx members to permit them to execute orders as brokers in Phlx exclusively options traded on Phlx's facility at the Back-up Exchange; and (ii) the Back-up Exchange has agreed that it will, at the instruction of Phlx, select members of the Back-up Exchange that are willing to be deputized by Phlx as temporary Phlx members authorized to trade Phlx exclusively listed options on Phlx's facility at the Back-up Exchange for such period of time following a Disabling Event as Phlx determines to be appropriate, and Phlx may deputize such members of the Back-up Exchange as temporary Phlx members for that purpose.

(ii) Phlx Singly Listed Options.

(A) For purposes of this Rule 99, the term “singly listed option” means an option that is not an “exclusively listed option” but that is listed by an exchange and not by any other national securities exchange.

(B) The Exchange may enter into arrangements with a Backup Exchange under which the Backup Exchange will agree, in the event of a Disabling Event, to list for trading singly listed options that are then singly listed only by the Phlx and not by the Backup Exchange. Any such options listed by the Backup Exchange shall trade on the Backup Exchange and in accordance with the rules of the Backup Exchange. Such options shall be traded by members of the Backup Exchange and by Phlx members selected by the Phlx to the extent the Backup Exchange can accommodate Phlx members in the capacity of temporary members of the Back-up Exchange. If the Back-up Exchange is unable to accommodate all Phlx members that desire to trade at the Back-up Exchange pursuant to paragraph (a)(i)(A), Phlx may determine which members shall be eligible to trade at the Back-up Exchange. Factors to be considered in making such determinations may include, but are not limited to, any one or more of the following: whether the member is a specialist in the applicable product(s), the number of contracts traded by the member or specialist unit in the applicable product(s), market performance, and other factors relating to a member’s contribution to the market in the applicable product(s).

Any Phlx member who is granted temporary access to the Backup Exchange pursuant to this paragraph shall only be permitted (i) to act in those Backup Exchange capacities that are authorized by the Backup Exchange and that are comparable to capacities in which

the temporary member has been authorized to act on the Phlx and (ii) to trade in those options in which the temporary member is authorized to trade on the Phlx.

(C) Any options listed by the Backup Exchange pursuant to paragraph (a)(ii)(B) that does not satisfy the standard listing and maintenance criteria of the Backup Exchange will be subject, upon listing by the Backup Exchange, to delisting (and, thus, restrictions on opening new series, and engaging in opening transactions in those series with open interest, as may be provided in the rules of the Backup Exchange).

(b) Phlx is Backup Exchange.

(i) Disabled Exchange Exclusively Listed Options.

(A) The Exchange may enter into arrangements with one or more other exchanges (each a “Disabled Exchange”) to permit the Disabled Exchange and its members to use a portion of the Phlx’s facilities to conduct the trading of some or all of the Disabled Exchange’s Exclusively Listed Securities in the event of a Disabling Event. The facility of the Phlx used by the Disabled Exchange for this purpose will be deemed to be a facility of the Disabled Exchange.

(B) Trading of the Disabled Exchange’s exclusively listed options on the Disabled Exchange’s facility at Phlx shall be conducted in accordance with Phlx rules, except that (1) such trading shall be subject to the Disabled Exchange’s rules with respect to doing business with the public, margin requirements, net capital requirements, listing requirements, and position limits, and (2) members of the Disabled Exchange that are trading on the Disabled Exchange’s facility at Phlx (not including Phlx members who become temporary members of the Disabled Exchange pursuant to paragraph (b)(i)(D))

will be subject to the rules of the Disabled Exchange governing or applying to the maintenance of a person's or a firm's status as a member of the Disabled Exchange. In addition, the Disabled Exchange and Phlx may agree that other Disabled Exchange rules will apply to such trading. The Disabled Exchange and Phlx have agreed to communicate to their respective members which rules apply in advance of trading.

(C) Phlx will perform the related regulatory functions with respect to trading of the Disabled Exchange's exclusively listed options on the Disabled Exchange's facility at Phlx, in each case except as the Disabled Exchange and Phlx may specifically agree otherwise. Phlx and the Disabled Exchange have agreed to coordinate with each other regarding surveillance and enforcement respecting trading of the Disabled Exchange's exclusively listed options on the Disabled Exchange's facility at Phlx. The Disabled Exchange has agreed that it shall retain the ultimate legal responsibility for the performance of its self-regulatory obligations with respect to the Disabled Exchange's facility at Phlx.

(D) Phlx members shall not be authorized to trade in any exclusively listed options of the Disabled Exchange, except that: (1) the Disabled Exchange may deputize willing Phlx floor brokers as temporary members of the Disabled Exchange to permit them to execute orders as brokers in exclusively listed options of the Disabled Exchange traded on the facility of the Disabled Exchange at Phlx; and (2) at the instruction of the Disabled Exchange, the Phlx shall select Phlx members that are willing to be deputized by the Disabled Exchange as temporary members of the Disabled Exchange authorized to trade the Disabled Exchange's exclusively listed options on the facility of the Disabled Exchange at the Phlx for such period of time following a Disabling Event as the Disabled

Exchange determines to be appropriate, and the Disabled Exchange may deputize such Phlx members as temporary members of the Disabled Exchange for that purpose.

(ii) Disabled Exchange Singly Listed Options.

(A) The Phlx may enter into arrangements with a Disabled Exchange under which the Phlx will agree, in the event of a Disabling Event, to list for trading options that are then singly listed only by the Disabled Exchange and not by the Phlx. Any such options listed by the Phlx shall trade on the Phlx and in accordance with Phlx rules. Such options shall be traded by Phlx members and by members of the Disabled Exchange selected by the Disabled Exchange to the extent the Phlx can accommodate members of the Disabled Exchange in the capacity of temporary members of Phlx. Any member of a Disabled Exchange granted temporary access to conduct business on the Phlx under this paragraph shall only be permitted (i) to act in those Phlx capacities that are authorized by the Phlx and that are comparable to capacities in which the temporary member has been authorized to act on the Disabled Exchange and (ii) to trade in those options in which the temporary member is authorized to trade on the Disabled Exchange. The Phlx may allocate such options to a Phlx specialist in advance of a Disabling Event, without utilizing the allocation process under Phlx Rule 506, to enable the Phlx to quickly list such options upon the occurrence of a Disabling Event.

(B) Any class of options listed by the Phlx pursuant to paragraph (b)(ii)(A) that does not satisfy the listing and maintenance criteria under Phlx Rules 1009 and 1010 will be subject, upon listing by the Phlx, to delisting (and, thus, restrictions on opening new series, and engaging in opening transactions in those series with open interest, as may be provided in Phlx rules).

(c) Member Obligations.

(i) Temporary Members of a Disabled Exchange

(A) A Phlx member acting as a temporary member of the Disabled Exchange pursuant to paragraph (b)(i)(D) shall be subject to, and obligated to comply with, the rules that govern the operation of the facility of the Disabled Exchange at Phlx to the extent applicable during the period of such trading. Additionally, (1) such Phlx member shall be deemed to have satisfied, and the Disabled Exchange has agreed to waive specific compliance with, rules governing or applying to the maintenance of a person's or a firm's status as a member of the Disabled Exchange, including all dues, fees and charges imposed generally upon members of the Disabled Exchange based on their status as such; (2) such Phlx member shall have none of the rights of a member of the Disabled Exchange except the right to conduct business on the facility of the Disabled Exchange at Phlx to the extent described in this Rule; (3) the member organization associated with such Phlx member, if any, shall be responsible for all obligations arising out of that Phlx member's activities on or relating to the Disabled Exchange; and (4) the clearing member of such Phlx member shall guarantee and clear the transactions of such Phlx member on the Disabled Exchange.

(B) A member of a Back-up Exchange acting in the capacity of a temporary member of Phlx pursuant to paragraph (a)(i)(F) shall be subject to, and obligated to comply with, the rules that govern the operation of the facility of Phlx at the Back-up Exchange, including Phlx rules to the extent applicable during the period of such trading. Additionally, (1) such temporary member shall be deemed to have satisfied, and Phlx will waive specific compliance with, rules governing or applying to the maintenance of a person's or a firm's

status as a member of Phlx, including all dues, fees and charges imposed generally upon Phlx members based on their status as such; (2) such temporary member shall have none of the rights of a Phlx member except the right to conduct business on the facility of Phlx at the Back-up Exchange to the extent described in this Rule; (3) the member organization associated with such temporary member, if any, shall be responsible for all obligations arising out of that temporary member's activities on or relating to Phlx; and (4) the clearing member of such temporary member shall guarantee and clear the transactions on Phlx of such temporary member.

(ii) Temporary Members of the Backup Exchange

(A) A Phlx member acting in the capacity of a temporary member of the Back-up Exchange pursuant to paragraph (a)(ii)(B) shall be subject to, and obligated to comply with, the rules of the Back-up Exchange that are applicable to the Back-up Exchange's own members. Additionally, (1) such Phlx member shall be deemed to have satisfied, and the Back-up Exchange has agreed to waive specific compliance with, rules governing or applying to the maintenance of a person's or a firm's status as a member of the Back-up Exchange, including all dues, fees and charges imposed generally upon members of the Back-up Exchange based on their status as such, (2) such Phlx member shall have none of the rights of a member of the Back-up Exchange except the right to conduct business on the Back-up Exchange to the extent described in this Rule; (3) the member organization associated with such Phlx member, if any, shall be responsible for all obligations arising out of that Phlx member's activities on or relating to the Back-up Exchange; (4) the clearing member of such Phlx member shall guarantee and clear the transactions of such Phlx member on the Back-up Exchange; and (5) such Phlx member

shall only be permitted (x) to act in those capacities on the Back-up Exchange that are authorized by the Back-up Exchange and that are comparable to capacities in which the Phlx member has been authorized to act on Phlx, and (y) to trade in those options in which the Phlx member is authorized to trade on Phlx.

(B) A member of a Disabled Exchange acting in the capacity of a temporary member of Phlx pursuant to paragraph (b)(ii)(A) shall be subject to, and obligated to comply with, Phlx rules that are applicable to Phlx's own members. Additionally, (1) such temporary member shall be deemed to have satisfied, and Phlx will waive specific compliance with, rules governing or applying to the maintenance of a person's or a firm's status as a member of Phlx, including all dues, fees and charges imposed generally upon Phlx members based on their status as such; (2) such temporary member shall have none of the rights of a Phlx member except the right to conduct business on Phlx to the extent described in this Rule; (3) the member organization associated with such temporary member, if any, shall be responsible for all obligations arising out of that temporary member's activities on or relating to Phlx; (4) the clearing member of such temporary member shall guarantee and clear the transactions of such temporary member on the Phlx; and (5) such temporary member shall only be permitted (x) to act in those Phlx capacities that are authorized by Phlx and that are comparable to capacities in which the temporary member has been authorized to act on the Disabled Exchange, and (y) to trade in those option classes in which the temporary member is authorized to trade on the Disabled Exchange.

(d) Member Proceedings.

(i) If the Phlx initiates an enforcement proceeding with respect to the trading during a back-up period of the singly or multiply listed options of the Disabled Exchange by a temporary member of the Phlx or the exclusively listed options of the Disabled Exchange by a member of the Disabled Exchange (other than a Phlx member who is a temporary member of the Disabled Exchange), and such proceeding is in process upon the conclusion of the backup period, the Phlx may transfer responsibility for such proceeding to the Disabled Exchange following the conclusion of the backup period. Arbitration of any disputes with respect to any trading during a backup period of singly or multiply listed options of the Disabled Exchange or of exclusively listed options of the Disabled Exchange on the Disabled Exchange's facility at the Phlx will be conducted in accordance with Phlx rules, unless the parties to an arbitration agree that it shall be conducted in accordance with Phlx rules.

(ii) If the Backup Exchange initiates an enforcement proceeding with respect to the trading during a backup period of Phlx singly or multiply listed options by a temporary member of the Backup Exchange or Phlx exclusively listed options by a Phlx member (other than a member of the Backup Exchange who is a temporary member of the Phlx), and such proceeding is in process upon the conclusion of the backup period, the Backup Exchange may transfer responsibility for such proceeding to the Phlx following the conclusion of the backup period. Arbitration of any disputes with respect to any trading during a backup period of Phlx singly or multiply listed options on the Backup Exchange or of Phlx exclusively listed options on the facility of the Phlx at the Backup Exchange will be conducted in accordance with the rules of the Backup Exchange, unless the parties to an arbitration agree that it shall be conducted in accordance with Phlx rules.

(e) Member Preparations.

Phlx members are required to take appropriate actions as instructed by the Exchange to accommodate Phlx's backup trading arrangements.

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SUMMARY OF EQUITY OPTION CHARGES (p. 1/6)

OPTION COMPARISON CHARGE (applicable to all trades – except specialist trades)^Ψ

Remainder unchanged.

OPTION TRANSACTION CHARGE^Ψ

Remainder unchanged.

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SUMMARY OF EQUITY OPTION CHARGES (p. 3/6)

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REAL-TIME RISK MANAGEMENT FEE^Ψ

Remainder unchanged.

EQUITY OPTION PAYMENT FOR ORDER FLOW FEES^{*Ψ}

Remainder unchanged.

See Appendix A for additional fees.

*Assessed on transactions resulting from customer orders, subject to a 500-contract cap, per individual cleared side of transaction

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^ΨIf Phlx exclusively listed options are traded at Phlx's facility on a Back-up Exchange pursuant to Phlx Rule 99, the Back-up Exchange has agreed to apply the per contract fees in this fee

schedule to such transactions. If any other Phlx listed options are traded on the Back-up Exchange (such as Phlx singly listed options) pursuant to Phlx Rule 99, the fee schedule of the Back-up Exchange shall apply to such trades.

If the exclusively listed options of a Disabled Exchange are traded on the Disabled Exchange's facility at Phlx pursuant to Phlx Rule 99, Phlx will apply the per contract fees in the fee schedule of the Disabled Exchange to such transactions. If any other options classes of the Disabled Exchange are traded on Phlx (such as singly listed options of the Disabled Exchange) pursuant to Phlx Rule 99, the fees set forth in the Phlx fee schedule shall apply to such trades.

Remainder of Summary of Equity Options Charges: Unchanged.

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SUMMARY OF INDEX OPTION AND FXI OPTIONS CHARGES (p. 1/1)

OPTION COMPARISON CHARGE (applicable to all trades – except specialist trades)^Ψ

Remainder unchanged.

OPTION TRANSACTION CHARGE^Ψ

Remainder unchanged.

OPTION FLOOR BROKERAGE ASSESSMENT

Remainder unchanged.

REAL-TIME RISK MANAGEMENT FEE^Ψ

Remainder unchanged.

See Appendix A for additional fees.

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ΨIf Phlx exclusively listed options are traded at Phlx’s facility on a Back-up Exchange pursuant to Phlx Rule 99, the Back-up Exchange has agreed to apply the per contract fees in this fee schedule to such transactions. If any other Phlx listed options are traded on the Back-up Exchange (such as Phlx singly listed options) pursuant to Phlx Rule 99, the fee schedule of the Back-up Exchange shall apply to such trades.

If the exclusively listed options of a Disabled Exchange are traded on the Disabled Exchange’s facility at Phlx pursuant to Phlx Rule 99, Phlx will apply the per contract fees in the fee schedule of the Disabled Exchange to such transactions. If any other options classes of the Disabled Exchange are traded on Phlx (such as singly listed options of the Disabled Exchange) pursuant to Phlx Rule 99, the fees set forth in the Phlx fee schedule shall apply to such trades.

Remainder of Fee Schedule: Unchanged.

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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, as amended, 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

a. Introduction

The Exchange proposes to adopt new Rule 99, Backup Trading Arrangements, which would govern the arrangements with one or more other exchanges (each a “Back-up Exchange”) to permit Phlx and its members to use a portion of a Back-up Exchange’s facilities to conduct the trading of Phlx exclusively listed options⁷ in the event of a Disabling Event, and similarly will permit Phlx to provide trading facilities at Phlx for another exchange’s exclusively listed options if that exchange (a “Disabled Exchange”) is prevented from trading due to a Disabling Event. Proposed Rule 99 would also permit Phlx to enter into arrangements with a Back-up Exchange to provide for the listing and trading of Phlx singly listed options⁸ by the Back-up Exchange if Phlx’s facility becomes disabled, and conversely provide for the listing and trading by Phlx of the singly listed options of a Disabled Exchange.

To accord with the provisions of its new Rule 99 and negotiated back-up trading arrangements, Phlx also proposes changes to its fee schedule relative to the fees that shall apply to transactions in the options of a Disabled Exchange executed on a Back-up Exchange.

b. Background

The back-up trading arrangements contemplated by proposed Rule 99 represent Phlx’s immediate plan to ensure that Phlx’s exclusively listed and singly listed options will have a trading venue if a catastrophe renders its primary facility inaccessible or inoperable. The Commission has suggested measures that Phlx should undertake to expedite reopening of Phlx’s

⁷ Paragraph (a)(i)(A) of proposed Rule 99 would define the term “exclusively listed option” as an option that is listed exclusively by an exchange (because the exchange has an exclusive license to use, or has proprietary rights in, the interest underlying the option).

⁸ For purposes of proposed Phlx Rule 99, the term “singly listed option” means an option that is not an “exclusively listed option” but that is listed by an exchange and not by any other national securities exchange.

exclusively listed securities if a catastrophic event prevents trading at Phlx for an extended period of time.⁹ Proposed Rule 99 would permit Phlx to enter into back-up trading arrangements with other exchanges that would address the measures suggested by the Commission.

In September 2003, Phlx entered into separate Memoranda of Understanding with the American Stock Exchange LLC (“Amex”) and CBOE to memorialize their mutual understanding to work together to develop bi-lateral back-up trading arrangements in the event that trading is prevented at one of the exchanges due to a Disabling Event. Since then, Phlx has been working with each of these exchanges to put in place written agreements outlining essential commercial terms with respect to the arrangements as well as operational plans that describe the operational and logistical aspects of the arrangements.

Phlx and CBOE have signed an agreement relative to back-up trading arrangements and are in the process of completing the operational plan and systems testing for those arrangements. The Exchange submitted a copy of this agreement as Exhibit 3.A to its Form 19b-4 for the rule change proposal, together with a copy of a first amendment to the agreement as Exhibit 3.B.¹⁰

c. Proposed Rule 99

The Exchange proposes to adopt Rule 99 to make effective its back-up trading arrangements with other exchanges.

If Phlx Is the Disabled Exchange

Section (a) of proposed Rule 99 describes the back-up trading arrangements that would apply if Phlx were the Disabled Exchange. Under proposed paragraph (a)(i)(B), the facility of

⁹ See letter from Annette L. Nazareth, Director, Division of Market Regulation, Commission, to Meyer S. Frucher, Chairman and Chief Executive Officer, Phlx, dated April 17, 2003. Comparable letters were also sent to other exchanges.

¹⁰ These exhibits are available for viewing on the Commission’s Web site, www.sec.gov/rules/sro.shtml, and at the Exchange and the Commission.

the Back-up Exchange used by Phlx to trade some or all of Phlx's exclusively listed options will be deemed to be a facility of Phlx, and such option classes shall trade as listings of Phlx. This approach of deeming a portion of the Back-up Exchange's facilities to be a facility of the Disabled Exchange is an approach approved by the Commission in previous emergency situations.¹¹

Since the trading of Phlx exclusively listed options will be conducted using the systems of the Back-up Exchange, proposed paragraph (a)(i)(C) provides that the trading of Phlx exclusively listed options on Phlx's facility at the Back-up Exchange would be conducted in accordance with the rules of the Back-up Exchange, except that (i) such trading would be subject to Phlx rules with respect to doing business with the public, margin requirements, net capital requirements, listing requirements and position limits. In addition, Phlx and the Back-up Exchange may agree that other Phlx rules will apply to such trading.¹² The Back-up Exchange rules that govern trading on Phlx's facility at the Back-up Exchange would be deemed to be Phlx rules for purposes of such trading.

¹¹ The Commission approved a similar approach when options listed on the Pacific Stock Exchange were physically moved to other exchanges in October 1989 due to an earthquake (See Exchange Act Release No. 27365 (October 19, 1989), 54 FR 43511 (October 25, 1989) (SR-Amex-89-26; SR-CBOE-89-21; SR-PSE-89-28; SR-Phlx-89-52)), and when Dell options were relocated from Phlx to Amex on a temporary basis in June 1998 (See Exchange Act Release No. 40088 (June 12, 1998), 63 FR 33426 (June 18, 1998) (SR-Phlx-98-25)).

¹² As stated above, Phlx's back-up trading arrangements with CBOE contemplate that the operation of the Disabled Exchange's facility at the Back-up Exchange will be conducted in accordance with the rules of the Back-up Exchange except that (i) the rules of the Disabled Exchange will apply with respect to doing business with the public, margin requirements, net capital requirements and listing requirements, and (ii) the members of the Disabled Exchange that are trading on the facility of the Disabled Exchange at the Back-up Exchange (not including members of the Back-up Exchange who become temporary members of the Disabled Exchange) will be subject to the rules of the Disabled Exchange governing or applying to the maintenance of a person's or a firm's status as a member of the Disabled Exchange.

Proposed paragraph (a)(i)(D) reflects that the Back-up Exchange has agreed to perform the related regulatory functions with respect to trading of Phlx exclusively listed options on Phlx's facility at the Back-up Exchange, in each case except as Phlx and the Back-up Exchange may specifically agree otherwise. The Back-up Exchange and Phlx will coordinate with each other regarding surveillance and enforcement respecting such trading. Phlx would retain the ultimate legal responsibility for the performance of its self-regulatory obligations with respect to Phlx's facility at the Back-up Exchange.

Under proposed paragraph (a)(i)(E), if the Back-up Exchange is unable to accommodate all Phlx members that desire to trade on Phlx's facility at the Back-up Exchange, Phlx would have the right to determine which members would be eligible to trade at that facility by considering factors such as whether the member is the specialist in the applicable product(s), the number of contracts traded by the member in the applicable product(s), market performance, and other factors relating to a member's contribution to the market in the applicable product(s).

Under proposed paragraph (a)(1)(F), members of the Back-up Exchange would not be authorized to trade in any Phlx exclusively listed options, except that (i) Phlx may deputize willing floor brokers of the Back-up Exchange as temporary Phlx members to permit them to execute orders as brokers in Phlx exclusively listed options traded on Phlx's facility at the Back-up Exchange,¹³ and (ii) the Back-up Exchange has agreed that it will, at the instruction of Phlx, select members of the Back-up Exchange that are willing to be deputized by Phlx as temporary Phlx members authorized to trade Phlx exclusively listed options on Phlx's facility at the Back-up Exchange for such period of time following a Disabling Event as Phlx determines to be appropriate, and Phlx may deputize such members of the Back-up Exchange as temporary Phlx

¹³ The exchanges that acted as Back-up Exchanges in the emergency situations noted above also deputized floor brokers in this manner. See supra note 11.

members for that purpose. The second of the foregoing exceptions would permit members of the Back-up Exchange to trade Phlx exclusively listed options on the Phlx facility on the Back-up Exchange if, for example, circumstances surrounding a Disabling Event result in Phlx members being delayed in arriving at the Back-up Exchange in time for prompt resumption of trading.

Section (a)(ii) of the proposed rule provides for the continued trading of Phlx singly listed options at a Back-up Exchange in the event of a Disabling Event at Phlx. Proposed paragraph (a)(ii)(B) provides that Phlx may enter into arrangements with a Back-up Exchange under which the Back-up Exchange will agree, in the event of a Disabling Event, to list for trading options that are then singly listed only by Phlx. Such options would trade on the Back-up Exchange as listings of the Back-up Exchange and in accordance with the rules of the Back-up Exchange.

Phlx singly listed options would be traded by members of the Back-up Exchange and by Phlx members selected by Phlx to the extent the Back-up Exchange can accommodate Phlx members in the capacity of temporary members of the Back-up Exchange. If the Back-up Exchange is unable to accommodate all Phlx members that desire to trade Phlx singly listed options at the Back-up Exchange, Phlx may determine which members would be eligible to trade such options at the Back-up Exchange by considering the same factors used to determine which Phlx members are eligible to trade Phlx exclusively listed options at the Phlx facility at the Back-up Exchange.

Under proposed paragraph (a)(ii)(C), any such option listed by the Back-up Exchange that does not satisfy the standard listing and maintenance criteria of the Back-up Exchange would be subject, upon listing by the Back-up Exchange, to delisting (and, thus, restrictions on opening new series, and engaging in opening transactions in those series with open interest, as may be provided in the rules of the Back-up Exchange).

If Phlx Is the Back-up Exchange

Section (b) of proposed Rule 99 describes the back-up trading arrangements that would apply if Phlx were the Back-up Exchange. In general, the provisions in Section (b) are the converse of the provisions in Section (a). With respect to the exclusively listed options of the Disabled Exchange, the facility of Phlx used by the Disabled Exchange to trade some or all of the Disabled Exchange's exclusively listed options would be deemed to be a facility of the Disabled Exchange, and such options would trade as listings of the Disabled Exchange. Trading of the Disabled Exchange's exclusively listed options on the Disabled Exchange's facility at Phlx would be conducted in accordance with Phlx rules, except that (i) such trading would be subject to the Disabled Exchange's rules with respect to doing business with the public, margin requirements, net capital requirements, listing requirements, and position limits, and (ii) members of the Disabled Exchange that are trading on the Disabled Exchange's facility at Phlx (not including Phlx members who become temporary members of the Disabled Exchange pursuant to paragraph (b)(i)(D)) would be subject to the rules of the Disabled Exchange governing or applying to the maintenance of a person's or a firm's status as a member of the Disabled Exchange. In addition, the Disabled Exchange and Phlx may agree that other Disabled Exchange rules will apply to such trading.

Section (b)(ii) describes the arrangements applicable to trading of the Disabled Exchange's singly listed options at Phlx, and is the converse of Section (a)(ii). One difference is the last sentence in paragraph (b)(ii)(A), which provides that Phlx may allocate singly listed option classes of the Disabled Exchange to a Phlx Specialist in advance of a Disabling Event, without utilizing the allocation process under Phlx Rule 506, to enable Phlx to quickly list such option classes upon the occurrence of a Disabling Event.

Member Obligations

Section (c) describes the obligations of members and member organizations with respect to the trading by “temporary members” on the facilities of another exchange pursuant to Rule 99. Section (c)(i) sets forth the obligations applicable to Phlx members who act in the capacity of temporary members of the Disabled Exchange on the facility of the Disabled Exchange at the Back-up Exchange.

Section (c)(i) provides that a Phlx member acting as a temporary member of the Disabled Exchange would be subject to, and obligated to comply with, the rules that govern the operation of the facility of the Disabled Exchange at Phlx. This would include the rules of the Disabled Exchange to the extent applicable during the period of such trading, including the rules of the Disabled Exchange limiting its liability for the use of its facilities that apply to members of the Disabled Exchange. Additionally, (1) such Phlx member acting as a temporary member of the Disabled Exchange would be deemed to have satisfied, and the Disabled Exchange has agreed to waive specific compliance with, rules governing or applying to the maintenance of a person’s or a firm’s status as a member of the Disabled Exchange, including all dues, fees and charges imposed generally upon members of the Disabled Exchange based on their status as such; (2) such Phlx member acting as a temporary member of the Disabled Exchange would have none of the rights of a member of the Disabled Exchange except the right to conduct business on the facility of the Disabled Exchange at the Back-up Exchange to the extent described in the Rule; (3) the member organization associated with such Phlx member acting as a temporary member of the Disabled Exchange, if any, would be responsible for all obligations arising out of that Phlx member’s activities on or relating to the Disabled Exchange, and (4) the clearing member of such

Phlx member would guarantee and clear the transactions of such temporary member on the Disabled Exchange.

Section (c)(ii) sets forth the obligations applicable to Phlx members who act in the capacity of temporary members of the Back-up Exchange for the purpose of trading singly and multiply listed options of the Disabled Exchange. Such Phlx members would be subject to, and obligated to comply with, the rules of the Back-up Exchange that are applicable to the Back-up Exchange's own members, including the rules of the Back-up Exchange limiting its liability for the use of its facilities that apply to members of the Back-up Exchange. Phlx members who act in the capacity of temporary members of the Back-up Exchange have the same obligations as those set forth in Section (c)(i) that apply to temporary members of the Disabled Exchange, except that, in addition, Phlx members who act in the capacity of temporary members of the Back-up Exchange would only be permitted (1) to act in those capacities on the Back-up Exchange that are authorized by the Back-up Exchange and that are comparable to capacities in which the temporary member has been authorized to act on the Disabled Exchange, and (2) to trade in those options in which the temporary member is authorized to trade on the Disabled Exchange.

Member Proceedings

As noted above, proposed Rule 99 provides that the rules of the Back-up Exchange shall apply to the trading of the singly and multiply listed options of the Disabled Exchange traded on the Back-up Exchange's facilities, and (with certain limited exceptions) the trading of exclusively listed options of the Disabled Exchange traded on the facility of the Disabled Exchange at the Back-up Exchange. The Back-up Exchange will perform the related regulatory functions with

respect to such trading (except as the Back-up Exchange and the Disabled Exchange may specifically agree otherwise).

Section (d) of proposed Rule 99 provides that if a Backup Exchange initiates an enforcement proceeding with respect to the trading during a backup period of singly or multiply listed securities of the Disabled Exchange by a temporary member of the Backup Exchange or exclusively listed securities of the Disabled Exchange by a member of the Disabled Exchange (other than a member of the Backup Exchange who is a temporary member of the Disabled Exchange), and such proceeding is in process upon the conclusion of the backup period, the Backup Exchange may transfer responsibility for such proceeding to the Disabled Exchange following the conclusion of the backup period. This approach to the exercise of enforcement jurisdiction is also consistent with past precedent.¹⁴

With respect to arbitration jurisdiction, proposed Section (d) provides that arbitration of any disputes with respect to any trading during a backup period of singly or multiply listed securities of the Disabled Exchange or of exclusively listed securities of the Disabled Exchange on the Disabled Exchange's facility at the Backup Exchange will be conducted in accordance with the rules of the Backup Exchange, unless the parties to an arbitration agree that it shall be conducted in accordance with the rules of the Disabled Exchange.

The purpose of these provisions is to permit a Backup Exchange to confer its temporary enforcement jurisdiction over a member or member organization of the Disabled Exchange back to the Disabled Exchange once the backup period has expired.

¹⁴ See supra note 11.

Member Preparations

To ensure that members are prepared to implement Phlx 's back-up trading arrangements, proposed Section (e) of Proposed Rule 99 requires Phlx members to take appropriate actions as instructed by Phlx to accommodate Phlx 's back-up trading arrangements.

d. Fee Schedule

The Exchange proposes to add a footnote to its Fee Schedule to inform its members regarding what fees will apply to transactions in the listed options of a Disabled Exchange effected on a Backup Exchange under Rule 99. The footnote provides that if Phlx is the Disabled Exchange, the Backup Exchange will apply the per contract and per contract side fees in the Phlx fee schedule to transactions in Phlx exclusively listed options traded on the Phlx facility on the Backup Exchange.¹⁵ If any other Phlx listed options are traded on the Backup Exchange (such as Phlx singly listed options) pursuant to Phlx Rule 99, the fee schedule of the Backup Exchange shall apply to such trades. The footnote contains a second paragraph stating the converse if Phlx is the Backup Exchange under Rule 99.

2. Statutory Basis

The Exchange states that the proposed rule change is intended to ensure that Phlx's exclusively listed and singly listed products will have a trading venue in the event that trading at Phlx is prevented due to a Disabling Event, thus minimizing potential disruptions for the markets and investors under those circumstances. The Exchange thus believes that the proposed rule change is consistent with Section 6(b) of the Act¹⁶ in general, and furthers the objectives of

¹⁵ When Phlx Dell options relocated to Amex in June 1998, Phlx fees applied to transactions in Dell options on the Amex. See supra note 11.

¹⁶ 15 U.S.C. 78f(b).

Section 6(b)(5) of the Act¹⁷ in particular, in that it is designed to perfect the mechanisms of a free and open market and to protect investors and the public interest.

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 self-regulatory organization 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

¹⁷ 15 U.S.C. 78f(b)(5).

- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-Phlx-2004-65 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-2004-65. 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 Room. Copies of the 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-2004-65 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.¹⁸

Margaret H. McFarland
Deputy Secretary

¹⁸ 17 CFR 200.30-3(a)(12).