

“second round” of bidding for or offering additional contracts in excess of the disseminated size (the “excess contracts”). This subset of willing crowd participants would be entitled to participate under the same rules applicable to the Remainder of the Order. Once all crowd participants have been satisfied in the original allocation up to the disseminated size, the “second round” would constitute a new parity situation respecting the willing crowd participants in the excess contracts. The excess contracts would be allocated among those crowd participants who wish to participate in additional contracts, in accordance with the proposed rule. Therefore, if the specialist is a willing participant in the excess contracts, the specialist would be entitled to receive an Enhanced Specialist Participation in such excess contracts.

Proposed Phlx rule 1014(g)(v)(C)(3) is intended to address this situation where an order is received via AUTOM and handled manually by the specialist for a number of contracts greater than the Exchange’s disseminated size, and the specialist executes the entire order manually prior to stating a size. The proposed rule would provide that, if the specialist has no Actual Size, the specialist would nonetheless be entitled to receive the Enhanced Specialist Participation for all contracts executed in excess of the disseminated size. The proposed rule limits the specialist’s entitlement if the specialist has an Actual Size. In such a situation, the specialist would be entitled to receive the Enhanced Specialist Participation, but not to exceed the specialist’s Actual Size in such excess contracts.

c. *Waiver*. The proposal is not intended to require, without exception, that crowd participants be allocated the number of contracts to which they would be entitled.³² The proposal would allow crowd participants, in their sole discretion, to offer to waive, in whole or in part, any part of a trade to which they were entitled to be allocated (an “Offer to Waive”), by stating so in a loud and audible voice to the other members of the trading crowd and the Allocating Participant.³³ In structuring the waiver provisions, the Exchange represents that it has incorporated basic

contract principles,³⁴ including communication of an offer, acceptance, and revocation.³⁵

For example, a crowd participant may make an Offer to Waive in situations in which hedging transactions become difficult or cumbersome due to lack of availability or liquidity in the underlying stock; additionally, a crowd participant may make an Offer to Waive to accommodate the execution of a particularly large sized order on the Exchange by larger crowd participants, or to accommodate a crowd participant closing out a position. At the same time, the proposed rule change would provide that a pattern or practice of waiving all or a portion of a crowd participant’s entitlement may be considered conduct inconsistent with just and equitable principles of trade.³⁶

If the Allocating Participant determines that the other crowd participant(s) then on parity is (are) willing to take the number of contracts that are subject to the Offer to Waive, the Allocating Participant may (but would not be required to), accept such Offer to Waive by (i) allocating the Remainder of the Order, taking into account the Offer to Waive, in accordance with proposed Phlx rule 1014(g)(v), or (ii) otherwise indicating, following the execution of the Initiating Order, that such Offer to Waive will be accepted.

The proposed rule addresses both a Total Waiver, in which a crowd participant effects a Waiver of his or her entire entitlement, and a Partial Waiver, in which a crowd participant effects a Waiver of a portion of his or her respective entitlement but not a Total Waiver. If a crowd participant effects a Total Waiver or a Partial Waiver, the number of contracts to which such participant would otherwise be entitled

would be reduced by the number of contracts waived. The entitlements of the other participants on parity (and who have not effected a Total or Partial Waiver) would be determined by redistributing the waived number of contracts to willing participants (including the specialist) based on the Defined Participation.³⁷

d. *Waiver and the Enhanced Specialist Participation*. The proposed rule would provide that, in the case of an option which is subject to an Enhanced Specialist Participation, and one or more ROTs effect Total Waivers leaving the specialist on parity (after giving effect to such Total Waivers) with three or more ROTs, the Enhanced Specialist Participation to which the specialist would be entitled is as if the specialist had been on parity with three ROTs; similarly, if one or more ROTs effect Total Waivers leaving the specialist on parity (after giving effect to such Total Waivers) with two or more ROTs, the Enhanced Specialist Participation to which the specialist would be entitled is as if the specialist had been on parity with two ROTs, and if one or more ROTs effect Total Waivers leaving the specialist on parity (after giving effect to such Total Waivers) with one ROT, the Enhanced Specialist Participation to which the specialist would be entitled is as if the specialist had been on parity with one ROT. In no event, however, would a specialist that is on parity with one ROT be entitled to receive a number of contracts that is greater than the Enhanced Specialist Participation, unless the one ROT has waived his entitlement or has been satisfied.

The proposed rule would make clear that, in no event would any non-waiving ROT be required to participate in fewer contracts than he/she would have received absent the Waiver(s). The purpose of this provision is to ensure that the ROT that remains on parity with the specialist does not receive fewer contracts than such ROT would have received if not for the Waivers.

e. *Partial Waiver*. The proposed rule would provide that, respecting options subject to the Enhanced Specialist Participation, in the event that one or more ROTs on parity with the specialist effect a Partial Waiver, the specialist would not be entitled to receive a number of contracts that is greater than 40% of the Remainder of the Order or, in the case of the specialist being on

³⁴ See Corbin, Contracts section 1515 and 13 Pa. C.S.A. section 1102 (corresponding to section 1–102 of the Uniform Commercial Code) regarding variation by agreement, stating the basic principles of commercial and contract law that parties may generally waive rights or benefits to which they would otherwise be entitled. In order to ensure that no waiver is coerced, the Exchange is proposing to codify that it would be inconsistent with “just and equitable principles of trade” for a participant to harass, coerce or intimidate another participant to waive any rights.

³⁵ The Exchange notes that waiver also appears in disciplinary and membership rules, as well as in the Act. Under the disciplinary processes of the exchanges, there is a right to a hearing, which can be waived. See, e.g., Amex rule 590(f) and Chicago Stock Exchange Article XII, rule 9. See also CBOE rule 3.9(b) permitting clearing firms to waive the membership posting period. The proposed provisions do not implicate the anti-waiver provisions of section 29(a) of the Act, 15 U.S.C. 78cc(a), which aims to prevent the waiver of the application of U.S. securities laws in certain situations where fraud is involved.

³⁶ See proposed rule 1014(g)(v)(F)(2).

³⁷ The proposal does not contemplate, and would not allow, a crowd participant to waive his/her entitlement to receive a given number of contracts to designate that the contracts subject to the Waiver be allocated to any other specific crowd participant or participants.

³² Telephone conversation with Phlx.

³³ Options Floor Procedure Advice (“Advice”) F–2 currently provides that, generally, the largest participant allocates the trade. The Exchange has proposed to modify Phlx rule 1014(g) and Advice F–2 governing who allocates trades. See Securities Exchange Act Release No. 47500 (March 13, 2003) (notice of File No. SR–Phlx–2001–28).