

change, as amended, from interested persons.

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

The PHLX proposes to amend PHLX rule 1080, Philadelphia Stock Exchange Automated Options Market ("AUTOM") and Automatic Execution System ("AUTO-X"),⁶ to provide for the automatic execution of eligible inbound customer and off-floor broker-dealer limit orders⁷ against booked customer limit orders at the Exchange's disseminated price. Specifically, the Exchange is proposing to amend PHLX rule 1080(g) to reflect that the contra-side of an eligible inbound customer or off-floor broker-dealer limit order executed via AUTO-X may be a booked customer limit order. The text of the proposed rule change is set forth below. Proposed new language is in italics; proposed deletions are in brackets.

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Philadelphia Stock Exchange
Automated Options Market (AUTOM)
and Automatic Execution System
(AUTO-X)

Rule 1080. (a) No change

(b) (i)(A)—(B) No change.

(C) Off-floor broker-dealer limit orders, up to the minimum number of contracts permitted by the Exchange, subject to the restrictions on order entry set forth in Commentary .05 of this rule. Generally, orders up to 1,000 contracts, depending on the option, are eligible for AUTOM order delivery on an issue-by-

issue basis, subject to the approval of the Options Committee. The Options Committee may determine to increase the eligible order delivery size to an amount greater than 1,000 contracts, on an issue-by-issue basis. The following types of broker-dealer limit orders are eligible for AUTOM: day, GTC, Immediate or Cancel ("IOC"), simple cancel, simple cancel to reduce size (cancel leaves), cancel to change price, cancel with replacement order. *For purposes of this rule 1080, the term "off-floor broker-dealer" means either: (1) A broker-dealer that delivers orders from off the floor of the Exchange for the proprietary account(s) of such broker-dealer; or (2) a market maker located on an exchange or trading floor other than the Exchange's trading floor who elects to deliver orders via AUTOM for the proprietary account(s) of such market maker.*

(ii) The Exchange's Options Committee may determine to accept additional types of orders as well as to discontinue accepting certain types of orders.

(A) In accordance with this subparagraph (ii), the Options Committee has determined to allow a customer limit order to be submitted in conjunction with a proprietary contra-side order via AUTOM; these orders must be labeled with a "K" (for the customer limit order) and "L" (for the proprietary order which is an immediate-or-cancel order that is not eligible for automatic execution) indicator, respectively. The customer limit order labeled "K" may be executed by the specialist or crowd, except that it may not be executed against the proprietary order labeled "L" until the customer limit order labeled "K" has been exposed to the trading crowd for not less than 30 seconds.

(iii) No change.

(c) AUTO-X.—AUTO-X is a feature of AUTOM that automatically executes eligible market and marketable limit orders up to the number of contracts permitted by the Exchange for certain strike prices and expiration months in equity options and index options, unless the Options Committee determines otherwise. AUTO-X automatically executes eligible orders using the Exchange disseminated quotation (except if executed pursuant to the NBBO Feature in subparagraph (i) below) and then automatically routes execution reports to the originating member organization. AUTOM orders not eligible for AUTO-X are executed manually in accordance with Exchange rules. Manual execution may also occur when AUTO-X is not engaged, such as pursuant to subparagraph (iv) below.

An order may also be executed partially by AUTO-X and partially manually.

The Options Committee may for any period restrict the use of AUTO-X on the Exchange in any option or series provided that the effectiveness of any such restriction shall be conditioned upon its having been approved by the Securities and Exchange Commission pursuant to section 19(b) of the Securities Exchange Act of 1934 and the rules and regulations thereunder. Any such restriction on the use of AUTO-X approved by the Options Committee will be clearly communicated to Exchange membership and AUTOM users through an electronic message sent via AUTOM and through an Exchange information circular. Such restriction would not take effect until after such communication has been made.

Currently, the Exchange's maximum allowable AUTO-X guarantee is 250 contracts. With respect to options on the Nasdaq-100 Index Tracking Stock ("QQQ")SM, orders of up to 2,000 contracts in the first two (2) near term expiration months, and 1,000 contracts for all other expiration months, are eligible for AUTO-X.

For each option, there shall be a minimum guaranteed AUTO-X size and a maximum guaranteed AUTO-X size, as determined by the specialist and subject to the approval of the Options Committee.

The Exchange shall provide automatic executions for eligible customer and broker-dealer orders up to the Exchange's disseminated size as defined in Exchange rule 1082 (except with respect to orders eligible for "Book Match" as described in rule 1080(g)(ii) below), subject to a minimum guaranteed AUTO-X size and a maximum guaranteed AUTO-X size (up to a size of 250 contracts).

- If the Exchange's disseminated size is greater than the minimum guaranteed AUTO-X size, and less than the maximum guaranteed AUTO-X size, inbound eligible orders shall be automatically executed up to Exchange's disseminated size. Remaining contracts shall be executed manually by the specialist or placed on the limit order book.

- If the Exchange's disseminated size is less than the minimum guaranteed AUTO-X size for that option, inbound eligible orders shall be automatically executed up to such minimum guaranteed AUTO-X size. Remaining contracts shall be executed manually by the specialist or placed on the limit order book.

- If the Exchange's disseminated size is greater than the maximum guaranteed

⁶ AUTOM is the Exchange's electronic order delivery, routing, execution and reporting system, which provides for the automatic entry and routing of equity option and index option orders to the Exchange trading floor. Orders delivered through AUTOM may be executed manually, or certain orders are eligible for AUTOM's automatic execution feature, AUTO-X. Equity option and index option specialists are required by the Exchange to participate in AUTOM and its features and enhancements. Option orders entered by Exchange members into AUTOM are routed to the appropriate specialist unit on the Exchange trading floor. See Phlx rule 1080.

⁷ In April of 2002, the Commission approved, on a six-month pilot basis, the Exchange's proposal to allow off-floor broker-dealers to submit proprietary limit orders directly onto the limit order book via AUTOM (the "pilot"). See Securities Exchange Act Release No. 45758 (April 15, 2002), 67 FR 19610 (April 22, 2002) (SR-Phlx-2001-40). In the pilot, the Exchange defined "off-floor broker-dealer" as (a) a broker-dealer that delivers orders from "upstairs" for the proprietary account(s) of such broker-dealer, or (b) a market maker located on an exchange or trading floor other than the Exchange's trading floor who elects to deliver orders via AUTOM for the proprietary account(s) of such broker-dealer. The Commission approved the pilot on a permanent basis in October 2002. See Securities Exchange Act Release No. 46660 (October 15, 2002), 67 FR 64951 (October 22, 2002) (SR-Phlx-2002-50).