

which is then multiplied by the specialist unit's current transaction charge of \$0.21.<sup>10</sup>

In both cases, for requests after September 1, 2003, if the equity or index option book does not have a complete two months' volume, the then-current transaction charge is used until that option book trades for two full calendar months nationally, after which the above-methodology is applied.

A specialist unit may, by the 15th day of the current billing month, select the fixed monthly fee for the following month,<sup>11</sup> provided the specialist unit has been an active Phlx equity or index specialist unit for one year from September 1, 2002.<sup>12</sup> In the case where a specialist unit has operated for less than one year, that unit is eligible for the fixed monthly fee on the first business day of the next full calendar month following its one-year anniversary.<sup>13</sup>

The fixed monthly fee will be in effect through February 29, 2004. If a specialist unit elects the fixed monthly fee, it must remain in the fixed monthly fee program through February 29, 2004.<sup>14</sup>

#### *D. QQQ Equity Option License Fee of \$0.10 Per Contract Side for Equity Option When the Specialist Unit Elects a Fixed Monthly Rate*

A charge of \$0.10 per contract side for all specialist unit transactions in the QQQ equity options is proposed if the

<sup>10</sup> The 12% represents the Exchange's shortfall target, the 21% represents the average contract sides to which specialists are a party, and the \$0.21 represents the current specialist equity option transaction charge.

<sup>11</sup> For example, if a specialist unit wishes to select the fixed monthly fee beginning on October 1, 2003, it must notify the Exchange by September 15, 2003. The fixed monthly fee will not be implemented retroactively. If the 15th of a month is not a business day, then the specialist unit may select the fixed monthly fee method by the next business day. The Exchange intends to distribute to the specialist units administrative procedures to follow in connection with choosing the fixed monthly fee methodology. The requirement that a specialist unit elect the fixed rate by the 15th of the month will be waived for the first month. Therefore, due to the fact that this proposal is scheduled to become effective for transactions settling on or after September 1, 2003, specialists will have the opportunity to select the fixed monthly fee until 9:00 a.m. on September 2, 2003.

<sup>12</sup> Specialist units must elect to participate in the monthly fixed fee program. Therefore, if no election is made, the specialist unit would continue to pay the rate currently in effect for equity and index option transaction charges and equity option specialist deficit (shortfall) fee.

<sup>13</sup> For example, if the one-year anniversary is on October 4, the specialist unit is eligible to select the fixed monthly fee by October 15 and the fixed monthly fee will then be in effect beginning November 1.

<sup>14</sup> See Exhibit 3 to Phlx's Form 19b-4, which is available for review at the Phlx and the Commission.

specialist unit elects to pay a fixed monthly fee.<sup>15</sup> This fee is in addition to the fixed monthly fee.

The above-referenced proposals are scheduled to become effective for transactions settling on or after September 1, 2003. In connection with the specialist fixed monthly fee proposal and the related QQQ license fee proposal, the proposals will be in effect through February 29, 2004.<sup>16</sup>

The text of the proposed rule change is available at the Phlx and the Commission.

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

In its filing with the Commission, 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. 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**

In general, the purpose of the proposed rule change is to promote equity option and index option business on the Phlx. Specifically, in connection with the \$50,000 "firm-related" cap, the Exchange believes this proposal offers an incentive for firms to transact more volume on the Phlx floor. An increase in firm orders should provide more trading opportunities for floor members, thereby increasing revenue potential to the membership, in addition to

<sup>15</sup> As previously discussed, under this proposal, specialist units may elect to pay a fixed monthly fee in lieu of specialist equity and index option transaction charges and equity option shortfall fees. Therefore, this \$0.10 fee would be in addition to the fixed monthly fee, but does not apply if specialist units elect to pay the current equity option and index option transaction charges, and equity option specialist deficit (shortfall) fees.

<sup>16</sup> Therefore, for transactions settling on or after March 1, 2004, the fixed monthly fee and the charge of \$0.10 per contract side to specialists for transactions in the QQQ equity options when the specialist unit elects to pay the fixed monthly fee will no longer be available and will be removed from the Phlx fee schedule unless a separate proposed rule change is filed to the contrary. The \$50,000 "firm-related" equity option and index option cap and the related QQQ license fee charge of \$0.10 per contract side for equity option firm/proprietary and firm/proprietary facilitation transactions that is imposed after the \$50,000 firm equity and index option comparison and transaction cap is reached, will remain in effect.

increasing revenue to the Exchange. In connection with the firm-related equity option and index option cap, the purpose of including the footnote related to equity option and index option "firm" transactions is to clarify to whom the firm-related charges apply.<sup>17</sup>

The purpose of the QQQ license fee is to adopt a fee for trading in the QQQ options to defray licensing costs associated with the trading of this product. Also, in connection with the specialist fixed fee, this proposal offers the opportunity for a specialist unit to choose a fixed monthly fee in lieu of paying the rate currently in effect for equity and index option transaction charges and the equity option Shortfall Fee. The Exchange staff has noted that some specialist units prefer knowing the exact cost of their equity and index option transactions; thus, allowing them to budget accordingly, and adjust their business models and strategies to meet these fixed costs. In addition, the fixed fee should create an incentive to bring in more business, above the fixed amount, which would be free of additional transaction charges assessed on specialist units. Additional order flow may generate transaction fees on the contra side that, in turn, may generate additional revenue for the Exchange.

#### **2. Basis**

The Exchange believes the proposed rule change is consistent with Section 6(b) of the Act,<sup>18</sup> in general, and with Section 6(b)(4) of the Act,<sup>19</sup> in particular, in that it is designed to provide for the equitable allocation of reasonable dues, fees, and other charges among its members.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

Phlx 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 solicited or received with respect to the proposed rule change.

## **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

The foregoing proposed rule change has become effective pursuant to

<sup>17</sup> See note 4 *infra*.

<sup>18</sup> 15 U.S.C. 78f(b).

<sup>19</sup> 15 U.S.C. 78f(b)(4).