

number of contracts not to exceed the size associated with the quotation that locks or crosses a limit order on the book. The purpose of this provision is to make automatic executions in the Book Sweep function consistent with the Exchange's rules relating to AUTO-X, the automatic execution feature of AUTOM. The Exchange no longer has an artificial "AUTO-X guarantee" applicable to an option. Instead, the Exchange currently provides automatic executions for eligible orders¹¹ delivered via AUTOM at the Exchange's disseminated price, up to the disseminated size, for both customer and broker-dealer orders.¹² Because the Exchange's disseminated size (and thus its guaranteed AUTO-X size) is fluid, in order to achieve consistency, the Exchange proposes that the number of contracts to be executed via Book Sweep be equal to the size associated with the quote that locks or crosses the limit order on the book.¹³

When a quote generated by Auto-Quote or SQF locks or crosses a limit order on the book, there are three possible scenarios that may occur. First, if such a quote is for a number of contracts that is equal to the size associated with the limit order on the book, the entire limit order would be executed. For example, if a limit order is resting on the book with a size of 200 contracts, and the size associated with the quote that locks or crosses such a limit order is 200 contracts, the entire limit order on the book would be executed, and Auto-Quote or SQF would refresh the quote (including the size associated with such a quote).

The second possible scenario is that the size associated with a quote that locks or crosses a limit order on the book could be for a greater number of

contracts than the size associated with the booked limit order. In such a situation, the entire size of the limit order would be executed. For example, if a limit order is resting on the book with a size of 200 contracts, and size associated with the quote that locks or crosses such a limit order is 300 contracts, the entire limit order would be executed. Following the execution, Auto-Quote or SQF would refresh the quote (including the size associated with such a quote).

Finally, the third possible scenario is that the size associated with the quote that locks or crosses a limit order on the book would be for fewer contracts than the size associated with the booked limit order. In this situation, the limit order would be partially executed automatically at the size associated with the quote that locks or crosses the limit order,¹⁴ and Auto-Quote or SQF would refresh the quotation. For example, if a limit order is resting on the book with a size of 200 contracts, and the size associated with the quote that locks or crosses such a limit order is 100 contracts, Book Sweep would generate an automatic execution for 100 contracts, leaving 100 contracts resting on the limit order book, and Auto-Quote or SQF would refresh the quote. If the refreshed quote locks or crosses the remaining contracts in the limit order resting on the book, Book Sweep would initiate an automatic execution for the size associated with the refreshed quote. If the refreshed bid or offer is for a price that is inferior to the remaining contracts in the limit order on the book, such that the limit order represents the Exchange's best bid or offer, the price and size of the limit order would be disseminated by the Exchange. If the refreshed bid or offer is for a price that is superior to the price of the remaining limit order, the Exchange would disseminate the refreshed bid or offer, and the remaining limit order would rest on the limit order book until it becomes due for execution or is cancelled.

Manual Book Sweep. Book Sweep would be engaged when AUTO-X is engaged, and would be disengaged when AUTO-X is disengaged.¹⁵

¹⁴ Under Exchange Rule 1082(b) all quotations made available by the Exchange and displayed by quotation vendors shall be firm for customer and broker-dealer orders at the disseminated price in an amount up to the disseminated size. See also Rule 11Ac1-1 under the Act, 17 CFR 240.11Ac1-1.

¹⁵ Exchange Rule 1080(c)(iv) provides that an order otherwise eligible for AUTO-X will instead be manually handled by the specialist in the following situations:

(A) The Exchange's disseminated market is crossed (*i.e.*, 2½ bid, 2 offer), or crosses the disseminated market of another options exchange;

However, the Exchange proposes to allow specialists to engage Book Sweep manually when orders are received when AUTO-X is disengaged, and Auto-Quote or SQF matches or crosses the Exchange's best bid or offer in a particular series as established by an order on the limit order book. The purpose of this provision is to enable the specialist to execute limit orders on the book that are due for execution more efficiently by manually initiating Book Sweep (rather than executing such orders individually), thus providing more efficient executions and ensuring that the specialist may maintain a fair and orderly market when such orders become due for execution.

The Exchange expects to deploy Book Sweep as supporting systems become available, on an issue-by-issue basis over a period to be determined.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act¹⁶ in general and furthers the objectives of Section 6(b)(5)¹⁷ in particular, in that it is designed to perfect the mechanisms of a free and open market and a national market system, and to protect investors and the public interest. The Exchange believes that Book Sweep should help provide

(B) One of the following order types: Stop, stop limit, market on closing, market on opening, or an all-or-none order where the full size of the order cannot be executed;

(C) The AUTOM System is not open for trading when the order is received (which is known as a pre-market order);

(D) The disseminated market is produced during an opening or other rotation;

(E) When the specialist posts a bid or offer that is better than the specialist's own bid or offer;

(F) If the NBBO Feature, described in Exchange Rule 1080(c)(i), is not engaged, and the Exchange's bid or offer is not the NBBO;

(G) When the price of a limit order is not in the appropriate minimum trading increment pursuant to Exchange Rule 1034;

(H) When the bid price is zero respecting sell orders; and

(I) When the number of contracts automatically executed within a 15 second period in an option (subject to a pilot program until November 30, 2003) exceeds the specified disengagement size, a 30 second period ensues during which subsequent orders are handled manually.

The Exchange notes that Rule 1080(c)(iv) was adopted to address the requirement in the *Order Instituting Public Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Sanctions*, Securities Exchange Act Release No. 43268 (September 11, 2000) and Administrative Proceeding File 3-10282 (the "Order") that the Exchange adopt new, or amend existing, rules concerning automatic quotation and execution systems which specify the circumstances, if any, under which automated execution systems be disengaged or operated in any manner other than the normal manner.

¹⁶ 15 U.S.C. 78f(b).

¹⁷ 15 U.S.C. 78f(b)(5).

¹¹ For a list of circumstances in which orders otherwise eligible for AUTO-X are instead manually handled by the specialist, see Exchange Rule 1080(c)(iv). See also Securities Exchange Act Release No. 45927 (May 15, 2002), 67 FR 36289 (May 23, 2002) (SR-Phlx-2001-24).

¹² See Securities Exchange Act Release No. 47646 (April 8, 2003), 68 FR 17976 (April 14, 2003) (SR-Phlx-2003-18).

¹³ The Exchange notes that the Chicago Board Options Exchange ("CBOE") currently has rules and systems in place regarding its "Trigger" mechanism, which includes a functionality similar to that set forth in the instant proposal. See CBOE Rule 6.8(d)(v). See also Securities Exchange Act Release No. 44462 (June 21, 2001), 66 FR 34495 (June 28, 2001) (SR-CBOE-00-22) (Order approving the CBOE Autoquote Triggered EBook Execution). The Exchange notes that, by rule, the CBOE "Trigger" function will not automatically execute a number of contracts in excess of the RAES guaranteed size. While the instant proposal is based in part on the CBOE "Trigger," it is distinguished from that function in that an order executed via Book Sweep would be executed for a number of contracts up to the size associated with the quote that locks or crosses a booked limit order.