

written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 such filing will also be available for inspection and copying at the principal office of Nasdaq. All submissions should refer to File No. SR-NASD-2003-160 and should be submitted by December 19, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48816; File No. SR-Phlx-2003-10]

### Self-Regulatory Organizations; Order Granting Approval to Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to Remote Primary Specialists

November 20, 2003.

On February 26, 2003, the Philadelphia Stock Exchange, Inc. ("Phlx") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to permit "primary specialists" to trade away from the Phlx floor in limited circumstances. The proposed rule change was published for comment in the **Federal Register** on September 29, 2003.<sup>3</sup> The Commission received no comments on the proposal. This order approves the Phlx's proposed rule change.

Under Phlx Rule 460, multiple specialists, one of which is identified as the "primary specialist,"<sup>4</sup> currently may trade a particular security on the equity trading floor of the Phlx.<sup>5</sup> Prior to the adoption of Phlx Rules 460 and 229A, each equity security traded on the floor of the Phlx was allocated to only one specialist unit. Phlx Rule 460 allows approved specialist units to trade one or more securities as "competing specialists."<sup>6</sup> There must be a primary specialist in a particular security in order for there to be competing specialists in that security.<sup>7</sup> Competing specialists have the same affirmative and negative obligations under Phlx Rule 203 as primary specialists.

Pursuant to Phlx Rule 461, the Phlx also operates a program whereby competing Phlx specialist units conduct specialist trading activities off the Phlx trading floor using PACE<sup>8</sup> terminals and related equipment. The Commission granted approval of the Phlx's remote competing specialist program subject to the condition that the Phlx "have in place specific information barrier policies and surveillance policies that are consistent with the Exchange's existing rules and that are acceptable to the Commission's Office of Compliance Inspections and Examinations ('OCIE')."<sup>9</sup>

The Phlx now proposes to establish a similar program whereby primary specialists would be permitted to conduct specialist trading activities off

the Phlx trading floor.<sup>10</sup> The Phlx has represented that its current rules, policies, and practices with respect to information barriers and surveillance are adequate to support remote trading by primary specialists at the Phlx.<sup>11</sup> Moreover, the Phlx has represented that it will examine remote primary specialist locations to ensure adequate compliance with Phlx rules.<sup>12</sup> Thus, the Commission believes that Phlx has addressed confidentiality issues associated with allowing remote primary specialists to trade from remote locations in proximity to a diversified broker-dealer's other off-floor operations. Member firms' traders should not get a market advantage because of their physical proximity to a specialist trading unit, and *vice versa*. Based, in part, on the Phlx's representation that it has in place adequate information barrier policies and surveillance procedures, the Commission is approving the Phlx's remote primary specialist proposal.

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>13</sup> Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>14</sup> which requires, among other things, that the Phlx's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in, securities, to remove impediments to and perfect the mechanism of a free and open market and a national market

<sup>4</sup> Phlx Rule 229A(b)(5) defines "primary specialist" as follows:

"Primary Specialist" shall mean the primary specialist identified as such by the Equity Allocation, Evaluation, and Securities Committee. The Primary Specialist may be either the Directed Specialist or the Non-Directed Specialist in the case of any particular Directed Order. The Primary Specialist shall be deemed to be the Directed Specialist with respect to any Non-Directed Order.

<sup>5</sup> See Securities Exchange Act Release No. 45183 (December 21, 2001), 67 FR 118 (January 2, 2002) (order approving establishment of a competing specialist program at the Phlx) (SR-Phlx-2001-97).

<sup>6</sup> Phlx Rule 229A(b)(6) defines "competing specialist" as follows:

"Competing Specialist" shall mean any competing specialist identified as such by the Equity Allocation, Evaluation, and Securities Committee pursuant to [Phlx] Rule 460. A Competing Specialist may be either the Directed Specialist or the Non-Directed Specialist in the case of any particular Directed Order.

<sup>7</sup> A Phlx specialist may trade some securities on a primary basis and other securities on a competing basis, or made trade all its securities on either a primary or a competing basis.

<sup>8</sup> PACE is the electronic order routing, delivery execution, and reporting system used to access the Phlx Equity Floor. See Phlx Rules 229 and 229A.

<sup>9</sup> Securities Exchange Act Release No. 45184 (December 21, 2001), 67 FR 622 (January 4, 2002) (order approving the establishment of the Phlx's remote specialist program) (SR-Phlx-2001-98).

<sup>10</sup> The Commission reiterates that while the remote specialist program, which now includes primary specialists, may have the effect of attracting additional order flow to the Phlx, this must occur consistent with best execution principles. Accordingly, the broker-dealer must rigorously and regularly examine the executions likely to be obtained for customer orders in the different markets trading the security, in addition to any other relevant considerations in routing customer orders.

<sup>11</sup> Telephone conversation between Carla Behnfeldt, Director, Legal Department New Product Development Group, Phlx, and Patrick M. Joyce, Special Counsel, Division of Market Regulation, Commission, on November 19, 2003.

<sup>12</sup> Telephone conversation between Edith Hallahan, Deputy General Counsel, Phlx, and Florence Harmon, Senior Special Counsel, Division of Market Regulation, Commission, on November 20, 2003.

<sup>13</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

<sup>14</sup> 17 CFR 200.30-3(a)(12).

<sup>15</sup> 15 U.S.C. 78s(b)(1).

<sup>17</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 48515 (September 22, 2003), 68 FR 56031 (September 29, 2003).