

change under Section 19(b) of the Act,²⁴ which has become effective.

The Board of Governors will not be permitted to adopt any amendment to the proposed By-laws described in the foregoing paragraph unless the Board of Governors has determined that: (i) Such acquisition of such ownership by such Person in question and/or its Related Persons will not impair the Exchange's ability to discharge its responsibilities under the Act and the rules and regulations thereunder and is otherwise in the best interests of the Exchange and its stockholders; (ii) such acquisition of such ownership by such Person and its Related Persons will not impair the Commission's ability to enforce the Act; and (iii) that Person and its relevant Related Persons are not subject to any applicable statutory disqualification. In making those determinations, the Board of Governors may impose on the Person in question and its Related Persons such conditions and restrictions as it may in its sole discretion deem necessary, appropriate or desirable in furtherance of the objectives of the Act and the governance of the Exchange.

In addition, no Member, either alone or together with its Related Persons, will be allowed to own, of record or beneficially, directly or indirectly, more than 20% of the then outstanding shares of common stock of the Phlx. To the extent any Member (or its Related Persons) purports to so own more than 20% of the then outstanding shares of common stock, that Member (and its Related Persons) will not be allowed to exercise any of the rights or privileges incident to the ownership of shares of common stock with respect to the shares exceeding the 20% limit.

In making those determinations, as in the case of a By-Law amendment expressly permitting the exercise of voting rights exceeding the 20% limit, the Board will be allowed to impose such conditions and restrictions on that Person and its Related Persons as it may in its sole discretion deem necessary, appropriate or desirable in furtherance of the objectives of the Act and the governance of the Phlx.

Unless the conditions specified above are met, if any Person exceeds the 40% threshold, either alone or together with its Related Persons, the Phlx will have the right, but not the obligation, to purchase from that Person and its Related Persons the shares of common stock that exceed the 40% threshold for a price equal to the par value of the shares of common stock.

If any Member exceeds the 20% threshold, either alone or together with

its Related Persons, the Phlx will have the right, but not the obligation, to purchase from that Member and its Related Persons the shares of common stock that exceed the 20% threshold for a price equal to the par value of the shares of common stock. Also, unlike ownership by non-Members in excess of 40%, the proposed Certificate of Incorporation does not contain a proviso allowing for Members to own shares in excess of 20% with appropriate notification and By-law amendment sanctioned by the Commission.

Pursuant to Article FOURTH(b)(iv) and (v) of the proposed Certificate of Incorporation, any Person, either alone or together with its Related Persons, that at any time owns (whether by acquisition or by a change in the number of shares outstanding) of record or beneficially, directly or indirectly, 5% or more of the then outstanding shares of common stock will be required, immediately upon so owning 5% or more of the then outstanding shares of common stock, to give the Board of Governors written notice of that ownership and will be required to update the notice promptly after any ownership change. However, an updated notice will not have to be provided to the Board of Governors in the event of an increase or decrease of less than 1% (of the then outstanding shares of common stock) in the ownership percentage so reported (for that purpose, the increase or decrease will be measured cumulatively from the amount shown on the immediately preceding report) unless such increase or decrease of less than 1% results in the Person's owning more than 20% or more than 40% of the shares of common stock then outstanding (at a time when the Person so owned less than those percentages) or results in the Person's owning less than 20% or less than 40% of the shares of common stock then outstanding (at a time when the Person so owned more than those percentages). These proposed notification requirements will allow the Exchange to fulfill its reporting obligations to the Commission and to better monitor the voting and ownership limitations in the proposed Certificate of Incorporation described above.

Transfer Restrictions. Pursuant to Section 29-1 of the proposed By-laws, no stockholder of the Exchange may sell, transfer (by operation of law or otherwise) or otherwise dispose of any shares of Class A Common Stock except in blocks of 100 shares per sale, transfer or disposition. This transfer restriction is intended to ensure that the number of holders of common stock of the Exchange will not exceed the threshold

for having to register the Exchange with the Commission under Section 12 of the Act.²⁵ The Exchange believes that, at least for some period of time after the Demutualization, the obligation of being a public reporting company would be overly burdensome on the Exchange as compared to the advantages conferred by that status.

In addition, Article XXIX of the proposed By-laws contains other restrictions typical for a Delaware stock corporation to ensure compliance with the Securities Act of 1933, as amended (the "Securities Act"),²⁶ and to allow for efficient future marketing of the capital stock by an underwriter in connection with and after a potential initial public offering of shares of capital stock of the Exchange.²⁷ Accordingly, Section 29-2 of the proposed By-laws provides that after the Demutualization, no sale, transfer or other disposition of the capital stock of the Exchange may be effected except: (i) Pursuant to an effective registration statement under the Securities Act and in accordance with all applicable state securities laws; (ii) upon delivery to the Exchange of an opinion of counsel satisfactory to the Board that such sale, transfer or other disposition may be effected pursuant to a valid exemption from the registration requirements of the Securities Act and all applicable state securities laws; (iii) upon delivery to the Exchange of such certificates or other documentation as counsel to the Exchange shall deem necessary or appropriate in order to ensure that such sale, transfer or other disposition complies with the Securities Act and all applicable state securities laws; or (iv) pursuant to such procedures as the Chairman of the Board (or his designee) may adopt from time to time with respect to such transactions. In addition, no sale, transfer or other disposition of the capital stock of the Exchange may be effected by any holder of such stock until all amounts due and owing by such holder to the Exchange (whether any such amounts relate to such holder's status as a stockholder, Member, participant or Member (or participant) Organization of the Exchange or otherwise) shall have been paid in full.

In addition, Section 29-3 of the proposed By-laws provides that no stockholders may, if requested by the Exchange or any underwriter of equity securities of the Exchange, sell or

²⁵ 15 U.S.C. 78l.

²⁶ 15 U.S.C. 77.

²⁷ It should be noted that no such transaction is currently contemplated at the time of this proposed rule change.

²⁴ 15 U.S.C. 78s(b).