

Required fields are shown with yellow backgrounds and asterisks.

Proposed Rule Change by NASDAQ OMX PHLX LLC.  
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

<b>Initial *</b>	<b>Amendment *</b>	<b>Withdrawal</b>	<b>Section 19(b)(2) *</b>	<b>Section 19(b)(3)(A) *</b>	<b>Section 19(b)(3)(B) *</b>			
<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>			
			Rule					
<b>Pilot</b>	<b>Extension of Time Period for Commission Action *</b>	<b>Date Expires *</b>	19b-4(f)(1)	19b-4(f)(2)	19b-4(f)(3)	19b-4(f)(4)	19b-4(f)(5)	19b-4(f)(6)
<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="text"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>
---	---

**Description**  
Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked \*).  

A proposal to modify Exchange Rule 3307 to institute a five millisecond delay in the execution time of marketable orders on NASDAQ OMX PSX

**Contact Information**  
Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name \*  Last Name \*   
Title \*   
E-mail \*   
Telephone \*  Fax

**Signature**  
Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date   
By    
(Name \*) (Title \*)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFF website.

**Form 19b-4 Information (required)**

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change (required)**

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

Add Remove View

Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

Add Remove View

Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

(a) 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> NASDAQ OMX PHLX LLC (“Phlx” or “Exchange”) proposes to modify Exchange Rule 3307 to institute a five millisecond delay in the execution time of marketable orders on NASDAQ OMX PSX (“PSX”). The proposal will be implemented initially on a one-year pilot basis with respect to the trading of securities listed on the New York Stock Exchange (“Tape A Securities”).

A notice of the proposed rule change for publication in the Federal Register is attached hereto as Exhibit 1 and the text of the proposed Exchange Rule is attached hereto as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by the Board of Directors of the Exchange on July 10, 2012. No other action by the Exchange is necessary for the filing of the rule change. The Exchange proposes to implement the proposed rule change within 30 days of the date of Commission approval.

Questions and comments on the proposed rule change may be directed to John M. Yetter, Vice President and Deputy General Counsel, The NASDAQ OMX Group, at (301) 978-8497.

---

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

<sup>2</sup> 17 CFR 240.19b-4.

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

a. Purpose

The purpose of the proposed rule change is to modify Exchange Rule 3307 to institute a five millisecond delay in the execution time of marketable orders. The proposal will be implemented initially on a one-year pilot basis with respect to the trading of Tape A Securities. The Exchange introduced PSX, which features a unique price/size/pro-rata execution algorithm, in order to encourage market participants to display more liquidity in a transparent market environment. As among equally priced orders on the PSX book, PSX allocates execution opportunities in proportion to the size of the posted order, rather than its time of entry. Thus, the Exchange's market model is intended to deemphasize the importance of speed in realizing trading opportunities.

Although PSX has enjoyed a measure of success, the Exchange is concerned that slower liquidity providers that post on PSX are sometimes subject to suboptimal executions due to disparities in the speed with which market participants are able to react to market information. Thus, in a circumstance where a broker posts a large order on PSX and changes in market conditions render the price of the order stale, a market participant with superior capabilities to process information may be able to route an order before the broker can change its price, thereby obtaining a fill at a price that is out of line with the price that will prevail in the market generally once the changes in the market conditions are fully digested. While the potential for a posted order to interact with orders entered by market participants with faster reaction capabilities responding to short-term information – sometimes referred to as “toxic order flow” – exists on all markets, the larger posted sizes and pro rata allocation model on PSX may make the impact more

pronounced, since fills are allocated among all market participants posting orders at a particular price.

It should also be noted that liquidity providers face asymmetric risks as compared with firms that seek to access liquidity opportunistically. To illustrate this point, consider the following example. Firm A is providing liquidity in 1,000 securities while Firm B is seeking opportunistically to access liquidity if it perceives a quote is mispriced. Both firms receive information (e.g., index market data from a futures market) simultaneously that causes both to re-evaluate the fair value of all 1,000 securities quoted by Firm A. Firm A immediately seeks to update its quotes to reflect the change in fair value, while Firm B seeks to access those quotes before they are updated. If Firm B's orders are able to access a quote before it is updated, Firm A faces the risk of executing at stale prices in up to 1,000 securities. If, on the other hand, Firm A's updates are processed before Firm B's orders, Firm B faces the opportunity cost of failing to execute at the opportunistic price, but otherwise has no exposure as a result of its relative latency. As this illustrates, the risk of being technologically inferior is substantially higher for liquidity providers (Firm A is exposed to up to 1,000 mispriced executions) than for liquidity removers (Firm B has no executions).

In an effort to address these issues, the Exchange is proposing to institute a five millisecond delay in the time between when a marketable order is received by the PSX system and when it is presented for execution against the PSX book.<sup>3</sup> No information about the receipt of an incoming marketable order will be provided to any market

---

<sup>3</sup> Post-only orders and non-marketable orders with a time-in-force other than "Immediate-or-Cancel" will not be subject to the five millisecond delay.

participant before the order is presented for execution.<sup>4</sup> However, any updates or cancellations of resting orders that are received during the five millisecond period will be processed before the incoming order is presented for execution. After an order has been presented for execution, any unexecuted shares will be cancelled back to the member, routed, or posted to the book as applicable. As is the case with all orders on PSX, any price improvement will be allocated to the party that entered the incoming order. If the incoming order becomes non-marketable while it is being held, it will nevertheless continue to be held until the end of the five-millisecond period. In addition, the market participant entering the order may not cancel or modify it until the order has been presented at the end of the period.

With the change, the overall processing time for incoming marketable orders will still be extremely rapid – in most cases, about 5.075 milliseconds – and will be faster than the processing time for several existing exchange markets. However, the Exchange believes that the additional time will be sufficient to allow liquidity providers to make adjustments if they believe them to be warranted. Accordingly, the change will “level the playing field” between liquidity providers and opportunistic traders, consistent with the Exchange’s goal of making PSX a market that rewards investors for the size of their trading interest rather than the speed of their trading algorithms.

Although the proposal will allow liquidity providers to adjust their quotes during the delay period after an order is received by PSX, the Exchange does not believe that the

---

<sup>4</sup> Because the incoming order will not be presented for execution against the resting quote until after the end of the five millisecond period, and no market participants will receive notice of the existence of the order during that time, the delay will not cause any compliance issues under SEC Rule 602(b), 17 CFR 242.602(b).

proposal presents any issues under the provisions of SEC Rule 602(b),<sup>5</sup> generally known as the “firm quote rule.” Subject to certain exceptions, paragraph (b)(2) of the rule provides:

[E]ach responsible broker or dealer shall be obligated to execute any order to buy or sell a subject security, other than an odd-lot order, presented to it by another broker or dealer, or any other person belonging to a category of persons with whom such responsible broker or dealer customarily deals, at a price at least as favorable to such buyer or seller as the responsible broker's or dealer's published bid or published offer (exclusive of any commission, commission equivalent or differential customarily charged by such responsible broker or dealer in connection with execution of any such order) in any amount up to its published quotation size.

However, paragraph (b)(3) provides that “[n]o responsible broker or dealer shall be obligated to execute a transaction for any subject security as provided in paragraph (b)(2) of this section if ... [b]efore the order sought to be executed is presented, such responsible broker or dealer has communicated to its exchange or association pursuant to paragraph (b)(1) of this section, a revised bid or offer.” The application of these provisions to the proposed rule change hinges on the word “presented”: if an order executable against a quote is presented to a broker-dealer, it must be executed unless a revised quote has been communicated to the exchange before the order is presented. The rule does not define the term “presented,” nor do the relevant proposing and adopting releases shed extensive light on its interpretation.<sup>6</sup> The relevant dictionary definition of

---

<sup>5</sup> 17 CFR 242.602(b).

<sup>6</sup> Securities Exchange Act Release No. 12670 (July 29, 1976), 41 FR 32856 (August 5, 1976); Securities Exchange Act Release No. 13626 (June 14, 1977), 42 FR 32418 (June 24, 1977); Securities Exchange Act Release No. 14415 (January 26, 1978), 43 FR 4342 (February 1, 1978).

“present” – to “show or offer (something) for others to scrutinize or consider”<sup>7</sup> – suggests the need for awareness of a recipient of the thing that is presented. As a matter of logic, moreover, a broker-dealer should not be held responsible for executing an order of which it is not aware. Indeed, this would appear to be the purpose of the exception provided by paragraph (b)(3): a broker-dealer that has updated its quote before receiving a previously marketable order should not be required to provide an execution against its prior quote. Because, in the case of the proposed rule change, an incoming order will not attempt to execute until after the end of the five millisecond period, and no market participants will receive notice of the existence of the order during that time, the Exchange believes that it would be contrary to the purpose of this exception if a broker-dealer were required to honor its prior quote merely because the Exchange was temporarily holding an order of which the broker-dealer had no awareness.

Under Regulation NMS, a trading center that displays an “automated quotation” must “immediately and automatically” execute an incoming order that is “marked as immediate-or-cancel,” up to the full size of the displayed quotation.<sup>8</sup> Moreover, the Commission stated that “immediately” means that “a trading center’s systems should provide the fastest response possible without any programmed delay.”<sup>9</sup> Thus, although PSX’s response time will remain extremely rapid, the Exchange will mark PSX’s quotations for Tape A Securities as “manual quotations” within the meaning of

---

<sup>7</sup> See [www.oxforddictionaries.com](http://www.oxforddictionaries.com).

<sup>8</sup> 17 CFR 242.600(b)(3).

<sup>9</sup> Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37519 (June 29, 2005) (File No. S7-10-04).



Regulation NMS. The Exchange notes, however, that in adopting Regulation NMS, the Commission “emphasize[d] that adoption of Rule 611<sup>10</sup> in no way lessens a broker-dealer’s duty of best execution.... The duty of best execution requires broker-dealers to execute customers’ trades at the most favorable terms reasonably available under the circumstances, i.e., at the best reasonably available price.” Accordingly, it is the Exchange’s belief that market participants will be required to consider the price, size, accessibility, and cost of PSX’s quotations in determining whether they have satisfied their best execution obligations.

The Exchange proposes adopting the change on a one-year pilot basis with respect to Tape A Securities only. This approach will allow the Exchange to compare trading patterns and market performance with respect to stocks subject to the pilot and those that are not. Based on this information, the Exchange will determine whether to expand the pilot, seek permanent approval for it, or allow it to lapse. The Exchange reserves the right to submit a proposed rule change prior to the end of the pilot period in order to make such changes as it believes warranted.

b. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>11</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>12</sup> in particular, in that it is designed to promote just and equitable principles of trade, to remove

---

<sup>10</sup> 17 CFR 242.611. Rule 611 provides that trading centers must establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks.

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The Exchange believes that the rule change will promote these goals by providing broker-dealers and investors that post liquidity with a better opportunity to adjust the prices of their orders to reflect changed market circumstances, thereby enhancing their ability to avoid so-called toxic order flow. The Exchange believes that firms willing to provide liquidity in large numbers of stocks provide benefits to investors and listed companies by supporting active markets in those stocks and dampening volatility. Specifically, the Exchange believes that widespread quoting activity benefits retail and institutional investors that have longer investment horizons and do not calibrate their purchases or sales to intraday variations in prices. As discussed above, however, as a firm becomes active in providing liquidity in a larger number of stocks, it faces greater challenges in ensuring that its quoted prices are up-to-date. If firms that wish to actively quote are unable to mitigate the asymmetric risks created by opportunistic traders, they are likely to decrease their quoting activity, rather than incur losses. Accordingly, the Exchange believes that it is appropriate to adopt the proposed rule change as a means to assist liquidity providers in mitigating these risks, and thereby encourage greater levels of liquidity provision in a wider range of stocks.

The Exchange does not believe that the proposal is unfairly discriminatory. Although the change may be seen as diminishing the ability of opportunistic traders to access quotes before they are updated to reflect changed market information, the Exchange believes that the anticipated benefits of the proposal in supporting liquidity

provision and the interests of investors with longer trading horizons outweigh the potentially diminished profit opportunities for traders with shorter trading horizons. Moreover, because the Exchange's market share is small, the change will have little effect on the ability of traders to continue trading actively with a short-term focus on numerous other venues.

4. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. Although the change will delay the execution time for incoming marketable orders, the Exchange believes that the extremely fast overall processing time of 5.075 milliseconds should not be considered a burden on the ability of market participants to compete for order executions. Moreover, the Exchange believes that the change is appropriate in furtherance of the purposes of the Act because it will help liquidity providers to mitigate the asymmetric risks associated with opportunistic traders. The Exchange further believes that any burden on the ability of opportunistic traders to realize short-term trading opportunities on the Exchange will be minimal, because such opportunities will continue to exist on other trading venues. Moreover, the Exchange believes that any such burden will be outweighed by the benefits that it seeks to provide to support liquidity provision and the interests of investors with longer-term trading horizons.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

No written comments were either solicited or received.

6. Extension of Time Period for Commission Action

The Exchange does not consent to an extension of the time period for Commission action.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

The proposed rule change is not based on the rules of another self-regulatory organization or of the Commission.

9. Exhibits

1. Notice of proposed rule for publication in the Federal Register.
5. Proposed Rule Text

**EXHIBIT 1**

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. SR-Phlx-2012-103)

August \_\_, 2012

Self-Regulatory Organizations; NASDAQ OMX PHLX LLC; Notice of Filing of Proposed Rule Change to Modify Exchange Rule 3307 to Institute a Five Millisecond Delay in the Execution Time of Marketable Orders on NASDAQ OMX PSX (“PSX”).

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> notice is hereby given that on August 3, 2012, NASDAQ OMX PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange proposes to modify Exchange Rule 3307 to institute a five millisecond delay in the execution time of marketable orders on NASDAQ OMX PSX (“PSX”). The text of the proposed rule change is below. Proposed new language is underlined; proposed deletions are in brackets.

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

In its filing with the Commission, the Exchange 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

---

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

<sup>2</sup> 17 CFR 240.19b-4.

the places specified in Item IV below. The Exchange 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

The purpose of the proposed rule change is to modify Exchange Rule 3307 to institute a five millisecond delay in the execution time of marketable orders. The proposal will be implemented initially on a one-year pilot basis with respect to the trading of Tape A Securities. The Exchange introduced PSX, which features a unique price/size/pro-rata execution algorithm, in order to encourage market participants to display more liquidity in a transparent market environment. As among equally priced orders on the PSX book, PSX allocates execution opportunities in proportion to the size of the posted order, rather than its time of entry. Thus, the Exchange's market model is intended to deemphasize the importance of speed in realizing trading opportunities.

Although PSX has enjoyed a measure of success, the Exchange is concerned that slower liquidity providers that post on PSX are sometimes subject to suboptimal executions due to disparities in the speed with which market participants are able to react to market information. Thus, in a circumstance where a broker posts a large order on PSX and changes in market conditions render the price of the order stale, a market participant with superior capabilities to process information may be able to route an order before the broker can change its price, thereby obtaining a fill at a price that is out of line with the price that will prevail in the market generally once the changes in the market conditions are fully digested. While the potential for a posted order to interact with orders entered by market participants with faster reaction capabilities responding to short-

term information – sometimes referred to as “toxic order flow” – exists on all markets, the larger posted sizes and pro rata allocation model on PSX may make the impact more pronounced, since fills are allocated among all market participants posting orders at a particular price.

It should also be noted that liquidity providers face asymmetric risks as compared with firms that seek to access liquidity opportunistically. To illustrate this point, consider the following example. Firm A is providing liquidity in 1,000 securities while Firm B is seeking opportunistically to access liquidity if it perceives a quote is mispriced. Both firms receive information (e.g., index market data from a futures market) simultaneously that causes both to re-evaluate the fair value of all 1,000 securities quoted by Firm A. Firm A immediately seeks to update its quotes to reflect the change in fair value, while Firm B seeks to access those quotes before they are updated. If Firm B’s orders are able to access a quote before it is updated, Firm A faces the risk of executing at stale prices in up to 1,000 securities. If, on the other hand, Firm A’s updates are processed before Firm B’s orders, Firm B faces the opportunity cost of failing to execute at the opportunistic price, but otherwise has no exposure as a result of its relative latency. As this illustrates, the risk of being technologically inferior is substantially higher for liquidity providers (Firm A is exposed to up to 1,000 mispriced executions) than for liquidity removers (Firm B has no executions).

In an effort to address these issues, the Exchange is proposing to institute a five millisecond delay in the time between when a marketable order is received by the PSX

system and when it is presented for execution against the PSX book.<sup>3</sup> No information about the receipt of an incoming marketable order will be provided to any market participant before the order is presented for execution.<sup>4</sup> However, any updates or cancellations of resting orders that are received during the five millisecond period will be processed before the incoming order is presented for execution. After an order has been presented for execution, any unexecuted shares will be cancelled back to the member, routed, or posted to the book as applicable. As is the case with all orders on PSX, any price improvement will be allocated to the party that entered the incoming order. If the incoming order becomes non-marketable while it is being held, it will nevertheless continue to be held until the end of the five-millisecond period. In addition, the market participant entering the order may not cancel or modify it until the order has been presented at the end of the period.

With the change, the overall processing time for incoming marketable orders will still be extremely rapid – in most cases, about 5.075 milliseconds – and will be faster than the processing time for several existing exchange markets. However, the Exchange believes that the additional time will be sufficient to allow liquidity providers to make adjustments if they believe them to be warranted. Accordingly, the change will “level the playing field” between liquidity providers and opportunistic traders, consistent with the Exchange’s goal of making PSX a market that rewards investors for the size of their trading interest rather than the speed of their trading algorithms.

---

<sup>3</sup> Post-only orders and non-marketable orders with a time-in-force other than “Immediate-or-Cancel” will not be subject to the five millisecond delay.

<sup>4</sup> Because the incoming order will not be presented for execution against the resting quote until after the end of the five millisecond period, and no market participants will receive notice of the existence of the order during that time, the delay will not cause any compliance issues under SEC Rule 602(b), 17 CFR 242.602(b).



Although the proposal will allow liquidity providers to adjust their quotes during the delay period after an order is received by PSX, the Exchange does not believe that the proposal presents any issues under the provisions of SEC Rule 602(b),<sup>5</sup> generally known as the “firm quote rule.” Subject to certain exceptions, paragraph (b)(2) of the rule provides:

[E]ach responsible broker or dealer shall be obligated to execute any order to buy or sell a subject security, other than an odd-lot order, presented to it by another broker or dealer, or any other person belonging to a category of persons with whom such responsible broker or dealer customarily deals, at a price at least as favorable to such buyer or seller as the responsible broker's or dealer's published bid or published offer (exclusive of any commission, commission equivalent or differential customarily charged by such responsible broker or dealer in connection with execution of any such order) in any amount up to its published quotation size.

However, paragraph (b)(3) provides that “[n]o responsible broker or dealer shall be obligated to execute a transaction for any subject security as provided in paragraph (b)(2) of this section if ... [b]efore the order sought to be executed is presented, such responsible broker or dealer has communicated to its exchange or association pursuant to paragraph (b)(1) of this section, a revised bid or offer.” The application of these provisions to the proposed rule change hinges on the word “presented”: if an order executable against a quote is presented to a broker-dealer, it must be executed unless a revised quote has been communicated to the exchange before the order is presented. The rule does not define the term “presented,” nor do the relevant proposing and adopting releases shed extensive light on its interpretation.<sup>6</sup> The relevant dictionary definition of

---

<sup>5</sup> 17 CFR 242.602(b).

<sup>6</sup> Securities Exchange Act Release No. 12670 (July 29, 1976), 41 FR 32856 (August 5, 1976); Securities Exchange Act Release No. 13626 (June 14, 1977), 42

“present” – to “show or offer (something) for others to scrutinize or consider”<sup>7</sup> – suggests the need for awareness of a recipient of the thing that is presented. As a matter of logic, moreover, a broker-dealer should not be held responsible for executing an order of which it is not aware. Indeed, this would appear to be the purpose of the exception provided by paragraph (b)(3): a broker-dealer that has updated its quote before receiving a previously marketable order should not be required to provide an execution against its prior quote. Because, in the case of the proposed rule change, an incoming order will not attempt to execute until after the end of the five millisecond period, and no market participants will receive notice of the existence of the order during that time, the Exchange believes that it would be contrary to the purpose of this exception if a broker-dealer were required to honor its prior quote merely because the Exchange was temporarily holding an order of which the broker-dealer had no awareness.

Under Regulation NMS, a trading center that displays an “automated quotation” must “immediately and automatically” execute an incoming order that is “marked as immediate-or-cancel,” up to the full size of the displayed quotation.<sup>8</sup> Moreover, the Commission stated that “immediately” means that “a trading center’s systems should provide the fastest response possible without any programmed delay.”<sup>9</sup> Thus, although PSX’s response time will remain extremely rapid, the Exchange will mark PSX’s

---

FR 32418 (June 24, 1977); Securities Exchange Act Release No. 14415 (January 26, 1978), 43 FR 4342 (February 1, 1978).

<sup>7</sup> See [www.oxforddictionaries.com](http://www.oxforddictionaries.com).

<sup>8</sup> 17 CFR 242.600(b)(3).

<sup>9</sup> Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37519 (June 29, 2005) (File No. S7-10-04).

quotations for Tape A Securities as “manual quotations” within the meaning of Regulation NMS. The Exchange notes, however, that in adopting Regulation NMS, the Commission “emphasize[d] that adoption of Rule 611<sup>10</sup> in no way lessens a broker-dealer’s duty of best execution.... The duty of best execution requires broker-dealers to execute customers’ trades at the most favorable terms reasonably available under the circumstances, i.e., at the best reasonably available price.” Accordingly, it is the Exchange’s belief that market participants will be required to consider the price, size, accessibility, and cost of PSX’s quotations in determining whether they have satisfied their best execution obligations.

The Exchange proposes adopting the change on a one-year pilot basis with respect to Tape A Securities only. This approach will allow the Exchange to compare trading patterns and market performance with respect to stocks subject to the pilot and those that are not. Based on this information, the Exchange will determine whether to expand the pilot, seek permanent approval for it, or allow it to lapse. The Exchange reserves the right to submit a proposed rule change prior to the end of the pilot period in order to make such changes as it believes warranted.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>11</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>12</sup> in particular,

---

<sup>10</sup> 17 CFR 242.611. Rule 611 provides that trading centers must establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks.

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Exchange believes that the rule change will promote these goals by providing broker-dealers and investors that post liquidity with a better opportunity to adjust the prices of their orders to reflect changed market circumstances, thereby enhancing their ability to avoid so-called toxic order flow. The Exchange believes that firms willing to provide liquidity in large numbers of stocks provide benefits to investors and listed companies by supporting active markets in those stocks and dampening volatility.

Specifically, the Exchange believes that widespread quoting activity benefits retail and institutional investors that have longer investment horizons and do not calibrate their purchases or sales to intraday variations in prices. As discussed above, however, as a firm becomes active in providing liquidity in a larger number of stocks, it faces greater challenges in ensuring that its quoted prices are up-to-date. If firms that wish to actively quote are unable to mitigate the asymmetric risks created by opportunistic traders, they are likely to decrease their quoting activity, rather than incur losses. Accordingly, the Exchange believes that it is appropriate to adopt the proposed rule change as a means to assist liquidity providers in mitigating these risks, and thereby encourage greater levels of liquidity provision in a wider range of stocks.

The Exchange does not believe that the proposal is unfairly discriminatory. Although the change may be seen as diminishing the ability of opportunistic traders to access quotes before they are updated to reflect changed market information, the

Exchange believes that the anticipated benefits of the proposal in supporting liquidity provision and the interests of investors with longer trading horizons outweigh the potentially diminished profit opportunities for traders with shorter trading horizons. Moreover, because the Exchange's market share is small, the change will have little effect on the ability of traders to continue trading actively with a short-term focus on numerous other venues.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. Although the change will delay the execution time for incoming marketable orders, the Exchange believes that the extremely fast overall processing time of 5.075 milliseconds should not be considered a burden on the ability of market participants to compete for order executions. Moreover, the Exchange believes that the change is appropriate in furtherance of the purposes of the Act because it will help liquidity providers to mitigate the asymmetric risks associated with opportunistic traders. The Exchange further believes that any burden on the ability of opportunistic traders to realize short-term trading opportunities on the Exchange will be minimal, because such opportunities will continue to exist on other trading venues. Moreover, the Exchange believes that any such burden will be outweighed by the benefits that it seeks to provide to support liquidity provision and the interests of investors with longer-term trading horizons.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission shall: (a) by order approve or disapprove such proposed rule change, or (b) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-Phlx-2012-103 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-Phlx-2012-103. This file number should be included on the subject line if e-mail is used.

To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the

Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 website viewing and printing in the Commission's Public Reference Room on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal offices of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-Phlx-2012-103, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

Kevin M. O'Neill  
Deputy Secretary

---

<sup>13</sup> 17 CFR 200.30-3(a)(12).

**EXHIBIT 5**

*New text is underlined and deleted text is in brackets.*

\* \* \* \* \*

**RULES OF THE BOARD OF GOVERNORS**

\* \* \* \* \*

**NASDAQ OMX PSX**

\* \* \* \* \*

**Rule 3307 Book Processing**

(a) When presented for execution, [S]ystem orders shall be executed through the PSX Book Process set forth below:

(1) – (4) No change.

(b) Pilot Program for Tape A Securities. The following processing rule shall apply to orders for securities listed on the New York Stock Exchange (“Tape A Securities”) during a pilot period ending September 30, 2013: Prior to being presented to the System book for execution, an incoming marketable order will be held for five milliseconds. Any updates or cancellations of resting orders that are received during this five millisecond period will be processed before the incoming order is presented for execution. After an order has been presented for execution, any unexecuted shares will be cancelled back to the member, routed, or posted to the book as applicable. Post-only orders and non-marketable orders with a time-in-force other than “Immediate-or-Cancel” will not be subject to the five millisecond delay. No information about the receipt of an incoming marketable order will be provided to any market participant before the order is presented for execution.

\* \* \* \* \*