

*Required fields are shown with yellow backgrounds and asterisks.*

Filing by NASDAQ 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 type="checkbox"/>	<input checked="" 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>	<input type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="text"/>	<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(6)	

<b>Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010</b>	<b>Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934</b>
<b>Section 806(e)(1) *</b>	<b>Section 806(e)(2) *</b>
<input type="checkbox"/>	<input type="checkbox"/>
	<b>Section 3C(b)(2) *</b>
	<input type="checkbox"/>

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

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

**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 action.

First Name \* Jeffrey Last Name \* Davis

Title \* Vice President and Deputy General Counsel

E-mail \* Jeffrey.Davis@nasdaq.com

Telephone \* (301) 978-8484 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.

(Title \*)

Date 12/09/2016

By Edward S. Knight

Executive Vice President and General Counsel

edward.knight@nasdaq.com

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 \***

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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 \***

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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 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

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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, security-based swap submission, or advance notice 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**

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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**

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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**

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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**

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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**

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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.

**SR-Phlx-2016-82 Amendment 1**

NASDAQ PHLX LLC (“Phlx” or “Exchange”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) and Rule 19b-4 thereunder, hereby submits this Amendment 1 to SR-PHLX-2016-82 (the “Original Proposal”) for the following three reasons:

1. To reflect changes to the Floor Broker Management System (“FBMS”) that occurred after the Exchange filed the Original Proposal on August 3, 2016. Specifically, on November 3, 2016, the Exchange officially retired FBMS 2, which was operational when the Exchange filed the Original Proposal. The Exchange simultaneously launched FBMS 3, which employs a new technological platform and offers enhanced functionality.
2. To modify the language of proposed Rule 1000(f)(iii)(D) to more completely reflect how rounding occurs in the processing of split price orders. Specifically, in the Original Proposal, the Exchange proposed to round prices where necessary to execute at the Minimum Price Variation and only to benefit a customer order. In Amendment 1, the Exchange proposes to add that rounding will also occur when multiple customer orders are involved, and in that case rounding will occur to benefit the customer order earliest in time. The Exchange also proposes to use rounding where no customer orders are involved, and in that case rounding will occur to benefit the non-customer order earliest in time.
3. Lastly, the Exchange is explaining further the circumstances in which a split price order will be processed under proposed Rule 100(f)(iii)(D). Specially, the Exchange has added three numbered examples of split price trades being

submitted by Floor Brokers. In each case, the Exchange sets forth below a detailed explanation of how the Floor Broker must comply with Exchange rules and how the Exchanges surveillance staff monitors such transactions and enforces applicable rules.

The Exchange respectfully submits this Amendment 1 with the intent to supersede and replace the Original Proposal in its entirety.

**EXHIBIT 1**

SECURITIES AND EXCHANGE COMMISSION  
(Release No. \_\_\_\_\_ ; File No. SR-Phlx-2016-82)

December \_\_, 2016

Self-Regulatory Organizations; NASDAQ PHLX LLC; Notice of Filing of Proposed Rule Change to Adopt a New Exception in Exchange Rule 1000(f)

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, 2016, NASDAQ PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the original proposed rule change and on December 9, 2016, the Exchange filed Amendment 1 to 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 Substance of the Proposed Rule Change

The Exchange proposes to adopt a new exception in Rule 1000(f) permitting Floor Brokers to execute certain split price orders in the trading crowd rather than electronically through the Options Floor Broker Management System, as described in detail below.

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

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

The text of the proposed rule change is set forth below. Proposed new language is underlined.

\* \* \* \* \*

### **NASDAQ PHLX Rules**

\* \* \* \* \*

### **Options Rules**

\* \* \* \* \*

### **Rule 1000. Applicability, Definitions and References**

(a) – (e) No change.

(f) All Exchange options transactions shall be executed in one of the following ways[, once the Exchange's new Options Floor Broker Management System functionality has been operating for a certain period to be established by the Exchange]:

(i) automatically by the Exchange Trading System pursuant to Rule 1080 and other applicable options rules;

(ii) by and among members in the Exchange's options trading crowd none of whom is a Floor Broker; or

(iii) through the Options Floor Broker Management System for trades involving at least one Floor Broker. Although Floor Brokers may represent orders in the trading crowd, Floor Brokers are not permitted to execute orders in the Exchange's options trading crowd, except as follows:

(A) The Exchange may determine to permit executions otherwise than in accordance with subparagraphs (i) - (iii) above respecting an option or all options in the event of a problem with Exchange systems.

(B) In addition, Floor Brokers can execute orders in the options trading crowd pursuant to Rule 1059, Accommodation Transactions (cabinet trades), and Rule 1079, FLEX Equity, Index and Currency Options.

(C) Multi-leg orders with more than 15 legs can be executed in the trading crowd.

(D) The following split price orders that, due to FBMS system limitations, require manual calculation:

(I) simple orders not expressed in the applicable minimum increment (“sub-MPV”) and that cannot be evenly split into two whole numbers to create a price at the midpoint of the minimum increment; and

(II) complex and multi-leg orders with at least one option leg with an odd-numbered volume that must trade at a sub-MPV price or one leg that qualifies under (I) above.

Surveillance staff must approve all executions submitted under this Rule 1000(f)(iii) to validate that each abides by applicable priority and trade through rules. Under subsection (f)(iii)(D), the rounding of prices may be used only where necessary to execute the trade at the MPV, and only to the benefit of a customer order or, where multiple customers’ orders are involved, for the customer order that is earliest in time. If no customer order is involved, rounding of prices is available to the non-customer order that is earliest in time.

(g) No change.

\* \* \* \* \*

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 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 proposal is to provide an exception to the mandatory use of the Floor Broker Management System ("FBMS") pursuant to Rule 1000(f) to permit Floor Brokers to execute certain split price orders in the trading crowd rather than electronically and to facilitate these transactions. Through the use of a surveillance process to verify that the conditions of the exception are met, the Exchange will ensure that the proposed exception is used only rarely.

Development of FBMS System

Until April 1, 2016, the Exchange operated two Options Floor Broker Management Systems concurrently on the options trading floor: the original Floor Broker Management System operating since 2005 ("FBMS 1");<sup>3</sup> and the enhanced Floor Broker

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<sup>3</sup> Under FBMS 1, orders were executed in the trading crowd by the Floor Broker and that execution was recorded in FBMS 1, which enabled the Exchange to electronically process the order in terms of trade reporting and clearing. If a trade that occurred in the trading crowd fails to give priority to an order on the book, for example, such violation is addressed by the Exchange's surveillance and enforcement programs after the fact.



Management System (“FBMS 2”). After March 31, 2016, FBMS 1 was retired and Floor Brokers were required to use FBMS 2.

FBMS 2 was launched in March 2014 in order to prevent certain types of violations and enhance order handling protections. With FBMS 2, all options transactions on the Exchange involving at least one Floor Broker were required to be executed by FBMS 2 as opposed to being executed by the Floor Broker in the trading crowd.<sup>4</sup> With FBMS 2, all orders were to be represented in the trading crowd, but the negotiation and agreement that occurred in the trading crowd did not result in a final trade, but rather a “meeting of the minds” that was then submitted through FBMS 2 for execution in the matching engine.<sup>5</sup>

The Exchange received approval to implement FBMS 2 as of June 1, 2013,<sup>6</sup> and delayed its implementation until July 2013,<sup>7</sup> until September 2013,<sup>8</sup> until December 2013,<sup>9</sup> and until March 2014.<sup>10</sup> Implementation began on March 7, 2014, with FBMS 2

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<sup>4</sup> Securities Exchange Act Release No. 69471 (April 29, 2013), 78 FR 26096 (May 3, 2013) (SR-Phlx-2013-09).

<sup>5</sup> A trade is consummated when the “meeting of the minds” occurs, but it is not final until FBMS or, as explained below, an Exchange Official, verifies that the trade complies with trade through and priority rules.

<sup>6</sup> Id.

<sup>7</sup> Securities Exchange Act Release No. 69811 (June 20, 2013), 78 FR 38422 (June 26, 2013) (SR-Phlx-2013-67).

<sup>8</sup> Securities Exchange Act Release No. 70141 (August 8, 2013), 78 FR 49565 (August 14, 2013) (SR-Phlx-2013-83).

<sup>9</sup> Securities Exchange Act Release No. 70629 (October 8, 2013), 78 FR 62852 (October 22, 2013) (SR-Phlx-2013-100).

<sup>10</sup> Securities Exchange Act Release No. 71212 (December 31, 2013), 79 FR 888 (January 7, 2014) (SR-Phlx-2013-129).

operating concurrently with FBMS 1. FBMS 2 was made available to all Floor Brokers in all options and, on March 31, 2016, FBMS 1 was retired.<sup>11</sup> As a result, FBMS 2 was the only system in use as of April 1, 2016.

The Exchange also contracted with a third-party to build an alternative system (“FBMS 3”) to replace FBMS 2. The Exchange had intended to implement FBMS 3 by November 2015, and then by March 2016, but, ultimately launched it on November 3, 2016. The Exchange simultaneously retired FBMS 2, leaving FBMS 3 as the sole operating system.

### Proposal

The Exchange proposes to adopt a new exception to the mandatory use of FBMS to execute trades for the processing of split-price orders. Currently, Rule 1000(f) provides that all Exchange options transactions shall be executed in one of the following ways:

- (i) automatically by the Exchange Trading System pursuant to Rule 1080 and other applicable options rules;
- (ii) by and among members in the Exchange’s options trading crowd none of whom is a Floor Broker; or

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<sup>11</sup> See Securities Exchange Act Release Nos. 72135 (May 9, 2014), 79 FR 27966 (May 15, 2014) (SR-Phlx-2014-33). Accordingly, the Exchange proposes to delete language from the first sentence of Rule 1000(f) that refers to the continued operation of FBMS 1. Nevertheless, the Exchange delayed the retirement of FBMS 1 until September 1, 2014, November 3, 2014, November 3, 2015, and, most recently, until April 1, 2016. See also Securities Exchange Act Release Nos. 72135 (May 9, 2014), 79 FR 27966 (May 15, 2014) (SR-Phlx-2014-33); 73246 (September 29, 2014), 79 FR 59874 (October 3, 2014) (SR-Phlx-2014-59); 73586 (November 13, 2014), 79 FR 68931 (November 19, 2014) (SR-Phlx-2014-71); and 67187 (October 19, 2015), 80 FR 64462 (October 23, 2015) (SR-Phlx-2015-80).

(iii) through the Options Floor Broker Management System for trades involving at least one Floor Broker. Although Floor Brokers may represent orders in the trading crowd, Floor Brokers are not permitted to execute orders in the Exchange's options trading crowd.

There are currently three exceptions to Rule 1000(f)(iii) that permit executions otherwise than in accordance with subparagraphs (i) - (iii) above. The first, under subparagraph (A), applies to executions respecting an option or all options in the event of a problem with Exchange systems. In addition, under subparagraph (B), Floor Brokers can execute orders in the options trading crowd pursuant to Rule 1059, Accommodation Transactions (cabinet trades), and Rule 1079, FLEX Equity, Index and Currency Options. Finally, under subparagraph (C), Multi-leg orders with more than 15 legs can be executed in the trading crowd. These three exceptions in (A) – (C) have been narrowly crafted to address specific situations, such as the complexity of a trade involving more than 15 legs. Each time a Floor Broker invokes an exception to Rule 1000(f), the Floor Broker is required by Rule 1063(e)(ii) to record the information required by Rule 1063(e)(i) on paper trade tickets, and may not represent an order for execution that has not been time stamped with the time of entry on the trading floor; such trade tickets must be time stamped upon the execution of such an order.

***Creation of Split-Price Orders.*** The Exchange first recognized the complexity of the split-price order in 2005 when it filed to create an exception from existing priority rules for split-price orders under Rule 1014(g)(i)(B).<sup>12</sup> The purpose behind the split-price

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<sup>12</sup> Securities Exchange Act Release No. 51820 (June 10, 2005), 70 FR 35759 (June 21, 2005) (SR-Phlx-2005-28) (pilot approval). See also Securities Exchange Act

priority exception was “to bring about the execution of large orders, which by virtue of their size and the need to execute them at multiple prices may be difficult to execute without a limited exception to the priority rules.” The proposed exception allows a member effecting a trade that betters the market to have priority on the balance of that trade at the next pricing increment, even if there are orders in the book at the same price. Floor Brokers that avail themselves of the split-price priority rule are obligated to ensure compliance with Section 11(a) of the Act.<sup>13</sup>

Today, split-price orders are processed primarily via FBMS or, much less frequently, via paper ticket. If the split-price order is evenly split and requires simple calculations to determine the number of contracts at two price points, the order is handled through FBMS. If the split-price order computation is more complicated, involving non-even integers and sub MPV price points, the surveillance staff declare an FBMS system malfunction – in accordance with PHLX Rules 1000(f)(iii)(A) and 1063(e)(ii) – and allow the floor broker to utilize a paper ticket and oral execution of the split-price order in the trading crowd. The Exchange believes that the treatment of split-price orders under Rule 1000(f) should be made clearer.

Therefore, the Exchange proposes to add an additional exception to Rule 1000(f)(iii), also narrowly crafted to reflect the complexities of executing split-price orders. Specifically, pursuant to proposed Rule 1000(f)(iii)(D), the following split price orders that require, due to a system design limitation, a manual calculation to determine specific volumes at different prices can be executed in the trading crowd: (I) simple

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Release No. 55993 (June 29, 2007), 72 FR 37301 (July 9, 2007) (SR-Phlx-2007-44) (permanent approval).

<sup>13</sup> See PHLX Rule 1014, Commentary .19.

orders with a price not expressed in the applicable minimum increment (“sub-MPV”)<sup>14</sup> and that cannot be evenly split into two whole numbers to create a price at the midpoint of the minimum increment; and (II) complex and multi-leg orders with at least one option leg with an odd-numbered volume that must trade at a sub-MPV price or one leg that qualifies under (I) above, thereby requiring the Floor Broker to determine the specific volumes to trade at each price. Surveillance staff must approve any such executions in open outcry to validate that such execution abides by applicable priority and trade through rules.

The proposed exception is similar to the existing exceptions in that it permits additional time when there is a system problem or when needed for the entry and completion of complicated trades. Here, the relief from the requirement to effect the trade in FBMS provided by the proposed exception is needed when a split-price trade calculation is complicated or requires contracts be rounded due to the fact that the determination of how many contracts are executed at two different prices requires manual intervention. The use of this exemption is anticipated to be implemented infrequently and in the following ways;

- 1) The floor broker knows that the order is not able to be handled by FBMS 3, due to the limitations of the system. In this scenario, the floor broker would comply with the information entry requirements of Rule 1063(e), enter the crowd, expose the order to the crowd, and request from the Options Exchange Official the application of the exemption.<sup>15</sup> The Options Exchange Official

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<sup>14</sup> See PHLX Rule 1034 (Minimum Increments).

<sup>15</sup> While the Exchange has rules which describe the manner in which Floor Brokers may submit orders for execution on the trading floor, such as PHLX Rule 1064,

would confirm understanding of the order and the availability of the exemption, and if the floor brokers request is deemed valid based on the specifics of the split price calculation, the Options Exchange Official would announce the application of the exemption to the floor broker and the trading crowd. The floor broker would then complete the negotiation of the trade in open outcry and consummate the transaction in an open outcry fashion in the trading crowd, using a paper ticket. In accordance with Rule 1063(e), the floor broker would record the timestamp for the consummation of the transaction which, when subsequently finalized, will become the time of execution.<sup>16</sup> Typically the Options Exchange Official would also capture a timestamp reflecting the time the Options Exchange Official observed the consummated transaction and may, in its discretion, substitute this timestamp for the timestamp recorded by the floor broker at the time of consummation.<sup>17</sup> The Options Exchange Official will review the pending transaction to confirm the specifics of the pending transaction compared to the Exchange order book

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the Exchange's Regulatory Group monitors executions for compliance with just and equitable principles of trade among other regulatory standards provided for in Exchange Rules. Regulatory staff ensures the audit trail reflects accurate order details.

<sup>16</sup> The consummated transaction is finalized when surveillance staff verifies that at the time the trade was consummated in the trading crowd the trade complied with applicable priority and trade through rules.

<sup>17</sup> The Exchange believes that it is necessary and appropriate for the Surveillance Staff to exercise independent judgment with respect to the proper timestamp for the consummation of trades on the floor of the Exchange. The Surveillance Staff is trained to observe objectively the conduct of floor participants, to detect conduct that improperly advantages floor participants, and to enforce Exchange rules. The absence of engaged and empowered Surveillance Staff would undermine the integrity of floor trading on the Exchange.

and national market best bid (or offer) to determine that at the time of the consummation of the transaction in the trading crowd the split price trade would have been trade through and priority compliant in FBMS, other than for the limitation to calculate the split price. The Options Exchange Official would then give the floor broker permission to submit a manual trade, via paper ticket reflecting the timestamp captured by the floor broker or, as described above, the Options Exchange Official.

- 2) The floor broker does not realize that the order, involving a complicated split price calculation will not be handled by FBMS (*e.g.*, the trade is rejected because it is not priced in the minimum price increment). In this scenario the floor broker would comply with the information entry requirements of Rule 1063(e), enter the trading crowd, and announce the order upon submission of the consummated transaction to FBMS, the floor broker would learn (based on a message returned to the floor broker from FBMS) that FBMS cannot calculate a split price. While the floor broker and the trading crowd agreed to a trade submitted to FBMS, the floor broker captures a timestamp for the time that the floor broker submitted the proposed execution into FBMS. Typically the Options Exchange Official would also capture a timestamp reflecting the time the Options Exchange Official observed the floor brokers attempt to execute a transaction and may, in its discretion, substitute this timestamp for the timestamp recorded by the floor broker as the time of consummation. Upon notification from the floor broker that FBMS could not compute the split price, the Options Exchange Official would confirm the specifics of the

consummated transaction and compare it to the Exchange order book and national market best bid (or offer). The Options Exchange Official would determine whether, at the time of the consummated transaction, the split price trade would have been permissible in FBMS, other than for the limitation to calculate the split price. If so, the Options Exchange Official would give the floor broker permission to submit a manual trade, via paper ticket reflecting the timestamp captured by the floor broker or, as described above, the Options Exchange Official.

- 3) The floor broker proceeds to handle an order in the same fashion as noted in item 2) above, but a reliable timestamp is not captured by either the Options Exchange Official or the floor broker when the consummated transaction was submitted through FBMS. In this scenario the Options Exchange Official would require the floor broker to “re-trade” the order. The transaction would then be processed according to the steps described in Example 1 above.

In all three of the above scenarios, the floor broker may then still attempt to input the determined split prices into FBMS for electronic execution. In the event that the electronic execution is again rejected by the trading system, the Floor Broker will execute using paper tickets and the transaction would be reported to the tape when the order processing of the manual execution, as reflected on the paper ticket, is completed by the Exchange Operations personnel. As with all manual trading occurring on a trading floor the transactions would be reported with the appropriate modifiers reflecting that the transaction is either late or out of sequence.



Even if the Floor Broker is unable to use FBMS to complete the entry of the split-price trade, the Floor Broker must still enter the order information required by Rule 1063 into FBMS for audit trail purposes.

The Surveillance staff will oversee Floor Brokers' use of the proposed exception as it does today under the current exceptions. Currently, when a Floor Broker states that there is a problem with the FBMS system, the Floor Broker will continue to input the order into FBMS (to the extent order entry functionality is accessible) and continue to announce the order in the trading crowd. Surveillance staff, knowing that the Floor Broker stated that he is experiencing a system problem or limitation will attempt to confirm the system problem with Exchange Operations staff. As described in detail above, if Surveillance staff is able to confirm that FBMS has a system limitation specific to the subject order, Surveillance staff will approve the use of a paper trade ticket and oral consummation of a transaction in the trading crowd that is contingent on Surveillance staff's additional confirmation that the trade complies with the trade through and price priority rules of the Exchange – a “pending trade.”

When it is determined that a pending trade complies with the trade through and price priority rules of the Exchange, the trade is approved as discussed above. If any pending trade does not comply with the trade through and price priority rules of the Exchange, the Surveillance staff will inform the applicable trading crowd participants that the pending trade does not comply with Exchange rules and not permit the trade to occur. This manual process performed by the Surveillance staff parallels the electronic process performed within the Exchange matching engine when FBMS is able to process a trade. Any delay attributable to manual surveillance does not change the time of trade

execution, which is set at the time a trade is consummated in the trading crowd as reflected by a timestamp on a paper ticket.

With respect to simple orders, if a Floor Broker attempts to execute a customer order to sell 357 contracts in symbol XYZ (with a Minimum Price Variation increment of \$0.05) at a price of \$0.11 by way of split price execution, the floor broker must perform a manual calculation. As a result of FBMS being unable to calculate the number of contracts to split to determine a net price of at least \$0.11, the floor broker will manually enter 285 contracts @ \$0.10 and 72 contracts @ \$0.15 to arrive at an execution price as close as possible to an \$0.11 (\$0.110084 in this case) aggregate price for the 357 contracts ensuring that, when applicable, the customer side of the trade benefits from the difference between the \$0.11 limit and the actual average price. This example would qualify for the proposed exception because it is a sub-MPV price (not in \$0.05 increments) and cannot be evenly split to obtain the desired aggregate price.<sup>18</sup>

With respect to complex and multi-leg orders, consider the following example: A Floor Broker receives a two legged call spread in XYZ (with a Minimum Price Variation increment of \$0.05) to sell 456 contracts of leg A @ \$1.23 and buy 229 contracts of leg B @ \$0.50. Because a Floor Broker is restricted to trading in not less than the permitted MPV increments, and XYZ has a MPV of \$0.05 in trades under \$3.00, so the Floor Broker will need to determine the calculation that will amount to a price closest to \$1.23; namely 60% of 456 contracts equals 273.6 but that is a non-round number and the customer selling the volume at the higher price gets the contract volume rounded up

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<sup>18</sup> The exemption would not apply where an order for 500 contracts could be traded at a split price of .125 by splitting it into two lots of 250 contracts at .10 and 250 contracts at .15.

while the volume at the lower price is rounded down so as to offer an advantage to the customer. The result is 274 contracts of leg A @ \$1.25 and 182 contracts of leg A @ \$1.20. This equals a net price on leg A of \$1.23004. This is the closest achievable net price that is at least equal to the limit price of the Floor Broker's client without breaking the limit price. This would qualify because the Floor Broker will need to determine at which of the price points the additional contract will trade, given that the odd number of contracts cannot be split evenly across two price points.

Another example involving a simple order is if a Floor Broker has a customer order to buy 479 GOOG May 440 calls for \$3.67: GOOG has a Minimum Price Variation of \$0.10 in trades over \$3.00 so the Floor Broker will need to determine the calculation that will amount to a price closest to \$3.67; namely, 70% of 479 equals 335.3 but 335.3 is a non-round number and the customer buying the volume entered at the lower price gets the contract volume rounded up while the volume at the higher price is rounded down so as to offer an advantage to the customer.<sup>19</sup> The result is 335 at \$3.70 and 144 at \$3.60. Since the customer is buying, the volume at the lower price of 3.60 gets rounded up to offer the advantage of rounding to the customer. This transaction would qualify for the exception because the simple order is for a sub-MPV price and cannot be evenly split.

Under this proposal, Surveillance staff must validate that split-price executions abide by all applicable priority and trade through rules using the time of execution recorded by the Floor Broker (and separately confirmed by Surveillance staff) on the

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<sup>19</sup> Under Proposed Rule 1000(f)(iii)(D), Exchange surveillance staff would be required to validate the use of price rounding to ensure that it is necessary and properly processed. As set forth in the proposed rule, rounding must benefit a customer order or, where multiple customers' orders are involved, the customer order that is earliest in time. If no customer order is involved, rounding of prices is available to the non-customer order that is earliest in time.

paper order ticket. Referring back to a prior example involving a simple customer order to execute 357 contracts in symbol XYZ (with a Minimum Price Variation increment of \$0.05) at \$0.11 (285 contracts @ \$0.10 / 72 contracts @ \$0.15), if FBMS is unable to determine the correct number of contracts to split to derive the net price of \$0.11, the Floor Broker, upon confirmation and approval of the Surveillance staff, can verbally execute the order and Surveillance staff would capture the verbal execution time of the pending transaction and determine if the Floor Broker established priority over the customer bids and/or offers based on the documented verbal execution time. If the market was \$0.05 bid and \$0.15 offer (with a public customer order on the \$0.15 offer), Surveillance staff would approve this transaction because the Floor Broker established priority over the \$0.15 offers by trading more contracts at the better price of \$0.10. However, if the market was \$0.10 bid and \$0.20 offer (with public customer orders on the \$0.10 bid), On-Floor Surveillance staff would not approve this transaction because the Floor Broker did not establish priority over the \$0.10 bids by trading the greater number of contracts at the inferior price. Finally, if the market was \$0.10 bid and \$0.15 offer (when the bid and/or offer represent a quotation), On-Floor Surveillance staff would approve this transaction because the Floor Broker would have priority over the quotations (bids/offers) pursuant to Rule 1014(g)(i)(B).

In conclusion, the Exchange believes that certain split-price orders warrant an exception from the requirement that the order be executed by FBMS. First, the exception is needed because FBMS is not currently programmed to perform the calculations associated with split prices not at the minimum price variation. Accordingly, the Floor Broker must do so manually, which can be time consuming; by the time the calculation is

made, the market may have changed such that FBMS would return the order to the Floor Broker unexecuted. Second, heightened surveillance will be imposed. Under the proposal, the execution would occur on the trading floor in open outcry as a pending transaction. The transaction is completed only upon validation from Surveillance staff, based on the market prices at the time of execution. The proposal clarifies the need for a manual handling of the execution for these complicated split price trades, rather than leaving ambiguous the question of whether a split-price trade amounts to an FBMS system problem. This proposal does not change what is considered by the Exchange as a FBMS system problem, but rather clearly sets forth a defined system limitation for a split-price order with specific characteristics.

## 2. Statutory Basis

The Exchange believes that the proposed exception is consistent with Section 6(b) of the Act,<sup>20</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>21</sup> in particular, in that it is designed to promote just and equitable principles of trade and to protect investors and the public interest by permitting split-price trades, which are complicated, to be executed in the trading crowd, which should, in turn, result in a greater likelihood that such orders are properly executed. FBMS cannot calculate these particular prices, as described in the examples above.

The Exchange believes that the proposed exception is consistent with the Act because it is narrowly tailored to permit a small number of beneficial trades. As stated earlier, the Commission has recognized the importance of split-price trades because they

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<sup>20</sup> 15 U.S.C. 78f(b).

<sup>21</sup> 15 U.S.C. 78f(b)(5).

permit the execution of large blocks, even permitting a limited exception to priority rules. Although FBMS was designed to enhance compliance to the greatest extent possible, FBMS does not have the capability to calculate and process certain split-price trades. If an exception was denied, Floor Brokers' ability to execute these large, split-price trades that benefit the market would be substantially impaired.

Additionally, Exchange surveillance is well-designed to protect customer when the exception is used. As set forth above, every split-price trade that invokes the proposed exception will require approval by Exchange surveillance staff in order to validate compliance with applicable priority and trade through rules. Additionally, all relevant trade data will be recorded on both paper tickets and in the FBMS system in order to ensure a proper audit trail for T+1 surveillance.

Finally, to the extent the exception permits rounding of prices, rounding is required to occur in the customer's favor where a customer trades with a non-customer; in the earliest-entering customer's favor where multiple customers are involved; or in the earliest-entering non-customer's favor when multiple non-customers orders are involved. These results are consistent with prevailing practices in the industry. The proposed rounding is also consistent with the Act because it enables the Exchange to maintain a fair and orderly market, to better protect the interest of ordinary investors, and to reward the earliest entry of orders into the marketplace.

The proposal is not unfairly discriminatory because it applies to all Floor Brokers the same way. Nor is it unfairly discriminatory with respect to market participants other than Floor Brokers because only Floor Brokers use FBMS.

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. The Exchange believes that the proposal should allow it to compete with other floor-based exchanges and help the Exchange's Floor Brokers compete with floor brokers on other options exchanges by accommodating another type of complicated order.

Through the use of a surveillance process to verify that the conditions of the exception are met, the Exchange will ensure that the exception is used only rarely.

C. 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.

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-2016-82 on the subject line.

Paper comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-Phlx-2016-82. 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, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office 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-2016-82 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>22</sup>

Robert W. Errett  
Deputy Secretary

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<sup>22</sup> 17 CFR 200.30-3(a)(12).