

*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-NYSE-2006-11 on the subject line.

*Paper Comments*

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

All submissions should refer to File Number SR-NYSE-2006-11. 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 inspection and copying in the Commission's Public Reference Room. 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-NYSE-2006-11 and should be submitted on or before April 21, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Nancy M. Morris,**  
Secretary.

[FR Doc. E6-4674 Filed 3-30-06; 8:45 am]

**BILLING CODE 8010-01-P**

**SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-53548; File No. SR-Phlx-2005-42]

**Self-Regulatory Organizations;  
Philadelphia Stock Exchange, Inc.;  
Notice of Filing of Proposed Rule  
Change and Amendment Nos. 1, 2 and  
3 Thereto Relating to Establishment of  
a Neutral "Referee"**

March 24, 2006.

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 June 10, 2005, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. On June 20, 2005, the Phlx filed Amendment No. 1 to the proposed rule change.<sup>3</sup> On February 16, 2006, the Phlx filed Amendment No. 2 to the proposed rule change.<sup>4</sup> On March 10, 2006, the Phlx filed Amendment No. 3 to the proposed rule change.<sup>5</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Phlx proposes to amend: (1) Exchange By-Law Article X, Section 10-9, Audit Committee; (2) Exchange Rule 124, Disputes; Exchange Rule 1092, Obvious Errors; (3) Option Floor Procedure Advice ("OFPA") F-27, Floor Official Rulings—Options; OFPA G-2, Trading Rotations, Halts or Reopenings; and (4) Equity Floor Procedure Advice ("EFPA") F-27, Floor Official Rulings—Equity. The proposal would establish a neutral "Referee," an Exchange employee or independent contractor who would have authority to review and rule on appeals from Floor Official rulings concerning the nullification and adjustment of trades, and authorize the Referee to make other initial rulings currently made only by Floor Officials.

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

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

<sup>3</sup> In Amendment No. 1, the Phlx indicated that the Exchange's Board of Governors approved the proposed amendment to Exchange By-Law Article X, Section 10-9 for filing with the Commission on June 15, 2005.

<sup>4</sup> Amendment No. 2 superseded and replaced in their entirety the original filing and Amendment No. 1 thereto.

<sup>5</sup> In Amendment No. 3, the Phlx made minor changes to the purpose section and rule text of the proposed rule change.

The text of the proposed rule change is set forth below. [Brackets] indicate deletions; *italics* indicate new text.

**PHILADELPHIA STOCK EXCHANGE,  
INC. BY-LAWS**

\* \* \* \* \*

**Article X**

**Standing Committees**

Sec. 10-1.-10-8. No change.

**Audit Committee**

Sec. 10-9. (a)-(c) No change.

*(d) The Audit Committee shall recommend for appointment by the Board of Governors a qualified Exchange employee or independent contractor, the Referee, to review Floor Official rulings concerning the nullification and/or adjustment of transactions, and to act in the capacity of a Floor Official respecting initial rulings concerning requests for relief from the requirements of certain Exchange rules, Equity Floor Procedure Advices and Option Floor Procedure Advices. The Audit Committee shall determine that the Referee has sufficient expertise in the area of securities trading to act in the capacity of a Floor Official respecting initial rulings concerning requests for relief and to conduct reviews of Floor Official rulings, and possesses sufficient knowledge of Exchange rules and the relevant sections of the Securities Exchange Act of 1934, as amended, and the rules thereunder.*

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**PHILADELPHIA STOCK EXCHANGE,  
INC. RULES OF THE BOARD OF  
GOVERNORS**

\* \* \* \* \*

**Disputes**

Rule 124. (a) Disputes occurring on and relating to the trading floor, if not settled by agreement between the members interested, shall be settled, if practicable, by vote of the members knowing of the transaction in question; if not so settled, they shall be settled by a Floor Official [summoned to the trading crowd] *designated by Market Surveillance to rule on the dispute.*

In issuing decisions for the resolution of trading disputes, Floor Officials [may] *shall* institute the course of action deemed to be most fair to all parties under the circumstances at the time. A Floor Official may direct the execution of an order on the floor, or adjust the transaction terms or participants to an executed order on the floor. However, two Option Floor Officials may nullify a transaction if they determine the transaction to have been in violation of

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

Rules 1014 (Obligations and Restrictions Applicable to Specialist and ROTs), 1015 (Quotation Guarantees), 1017 (Priority and Parity at Openings in Options), 1033 (Bids and Offers) or 1080 (AUTOM). Two Equity Floor Officials may nullify a transaction if they determine the transaction to have been in violation of Rules 110 (Bids and Offers—Precedence), 111 (Bids and Offers—Binding), 118 (Bids and Offers Outside Best Bid and Offer), 119 (Precedence of Highest Bid), 120 (Precedence of Offers at Same Price), 126 (Crossing), 203 (Agreement of Specialists), 218 (Customer Order Receives Priority), 229 (PACE System), 232 (Handling Orders When the Primary Market is Not Open for Free Trading), or 455 (Short Sales). This Rule 124(a) shall not apply to options transactions that are the result of an Obvious Error (as defined in Rule 1092). Options transactions that are the result of an Obvious Error shall be subject to the provisions and procedures set forth in Rule 1092.

(b) All rulings rendered by Floor Officials or the Referee (as defined in Commentary .02 to this Rule) are effective immediately and must be complied with promptly. Failure to promptly comply with an initial Floor Official ruling or a Referee [ruling] decision upon review of a Floor Official ruling concerning a trading dispute may result in referral to the Business Conduct Committee. Failure to promptly comply with other Floor Official rulings issued pursuant to Order and Decorum Regulations (Rule 60) or Floor Procedure Advices (Rule 970) and not concerning a trading dispute may result in an additional violation.

(c) Review—Floor Official [R] rulings issued pursuant to Order and Decorum Regulations are reviewable pursuant to Rule 60. Floor Official rulings issued pursuant to Floor Procedure Advices are reviewable pursuant to Rule 970. All other Floor Official rulings are reviewable pursuant to paragraph (d) of this Rule.

(d) Review of Floor Official Rulings (Trading Disputes)—[Options] All Floor Official rulings are reviewable by [a] the Referee [minimum of three members of the Sub-Committee on Rules and Rulings, a sub-committee of the standing committee, which shall be empowered to review such rulings, or the Chairperson of the standing committee (or his designee) if three Sub-Committee members cannot be promptly convened. Equity Floor Official Rulings are reviewable by a minimum of three members of the Floor Procedure Committee, or the Chairperson of the Floor Procedure

Committee (or his designee) if three members cannot be promptly convened. This constitutes a Review Panel for Floor Official rulings. Any person who appeals an Options Floor Official ruling concerning a trading dispute and loses will be subject to a \$250.00 fee upon a finding by the Review Panel, that such appeal is frivolous].

(i) *Market Surveillance staff must be advised within 15 minutes of a Floor Official's ruling that a party to such ruling has determined to appeal from such ruling to the Referee.* The Exchange may establish the procedures for the submission of a request for a review of a Floor Official ruling. Floor Official rulings concerning the nullification or adjustment of transactions may be sustained, overturned or modified by the Referee [a majority vote of the Review Panel members present]. In making a determination, the [Review Panel] Referee may consider facts and circumstances not available to the ruling Floor Official as well as action taken by the parties in reliance on the Floor Official's ruling (e.g., cover, hedge and related trading activity). [Decisions of the Review Panel will be considered final decisions of a standing floor committee and may be appealed to the Exchange's Board of Governors pursuant to Exchange By-Law Article XI.]

(ii) *All decisions made by the Referee in connection with initial rulings on requests for relief and with the review of a Floor Official ruling pursuant to this paragraph (d) shall be documented in writing and maintained by the Exchange in accordance with the record keeping requirements set forth in the Securities Exchange Act of 1934, as amended, and the rules thereunder.*

(iii) *A member or member organization seeking the Referee's review of a Floor Official ruling shall be assessed a fee of \$250.00 for each Floor Official ruling to be reviewed that is sustained and not overturned or modified by the Referee.*

(iv) *Decisions of the Referee concerning (A) the review of Floor Official rulings relating to the nullification or adjustment of transactions, and (B) initial requests for relief shall be final and may not be appealed to the Exchange's Board of Governors.*

(v) *As appropriate, the Chairman of the Options Committee, Foreign Currency Options Committee, or of the Floor Procedure Committee, or their respective designees, shall refer a Referee that fails to make any ruling in accordance with Exchange rules to the Audit Committee for possible disciplinary action, including removal.*

*A Floor Official that fails to make any ruling in accordance with Exchange rules may be subject to possible disciplinary action by the Exchange.*

(vi) *Failure to promptly comply with a Floor Official or Referee decision under this Rule may result in referral to the Business Conduct Committee.*

Commentary:

.01. No change.

.02. The Referee.

(a) An Exchange employee or independent contractor, the Referee, shall be appointed by the Board of Governors on the recommendation of the Audit Committee to review Floor Official rulings concerning the nullification and adjustment of transactions in accordance with Rule 124(d), and to act in the capacity of a Floor Official respecting initial rulings concerning requests for relief from the requirements of Exchange Rules relating to:

(i) bid/ask differentials pursuant to Rule 1014(c) and Options Floor Procedure Advice ("OFPA") F-6;

(ii) disengagement of Exchange automatic execution systems pursuant to Rule 1080(e) and OFPA A-13;

(iii) the determination pursuant to Rule 1080(c)(i) that quotes in options on the Exchange or another market or markets are subject to relief from the firm quote requirement set forth in the SEC Quote Rule, as defined in Exchange Rule 1082(a)(iii) (the "Quote Rule"), and that quotes in options on the Exchange or another market or markets previously subject to such relief are no longer subject to such relief; and

(iv) trading halts, openings and re-openings pursuant to Rules 1017, 1047 and 1047A and OFPAs A-12, A-14 and G-2.

(b) The Audit Committee shall recommend for appointment by the Board of Governors any other Exchange employee(s) or independent contractor(s) to function as the Referee in the event that the Referee is unavailable ("Backup Referees") as set forth in Commentary .02(f) below. The Exchange's rules and procedures applicable to the Referee shall also apply to Backup Referees, and any reference to the Referee in these rules shall be deemed to include Backup Referees.

(c) The Referee shall be an employee of the Exchange or an independent contractor designated by the Audit Committee. The Referee shall not be a member of the Exchange nor affiliated with any Exchange member or member organization and shall not be an immediate family member of any Exchange member. The Referee shall not be a debtor or creditor of any

*Exchange member or member organization.*

*(d) The Audit Committee shall have supervision over the Referee, and, based on the advice of the Exchange's General Counsel and Human Resources management, may recommend the level of compensation of the Referee to the Board of Governors, and may establish other conditions of employment of the Referee. The Audit Committee or its designee shall conduct annual performance evaluations, and shall consider any written complaints from members and member organizations concerning the Referee. The Audit Committee shall not have the authority to overrule or modify any ruling made by the Referee. The Audit Committee may terminate the employment of the Referee for good cause shown, and may otherwise discipline the Referee as appropriate for good cause shown.*

*(e) The Exchange's General Counsel or his or her designee may assign additional duties and responsibilities to the Referee not related to Referee rulings. Notwithstanding the foregoing, the Referee shall not:*

*(i) participate in any Exchange enforcement action, investigation, market surveillance activity, hearing (other than as a witness) or other activity related to disciplinary matters;*

*(ii) issue citations for violations of Exchange rules;*

*(iii) rule on any matter concerning order and decorum pursuant to Exchange Rule 60 and the regulations thereunder; and*

*(iv) prepare, research, draft, review, or file a proposed rule change with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934 and the rules thereunder concerning the Exchange's disciplinary rules.*

*(f) If the Referee is unavailable or unable to make a ruling for any reason (including, without limitation, absence from the Exchange trading floor, vacation, illness, or in the process of making another Referee ruling), Market Surveillance staff will immediately notify the Exchange's General Counsel, or his/her designee, who would designate a Backup Referee to make such a ruling.*

*(g) The Referee shall make fair and impartial rulings in accordance with Exchange rules and By-Laws.*

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#### **PHILADELPHIA STOCK EXCHANGE, INC. OPTIONS RULES**

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#### **Obvious Errors**

Rule 1092. The Exchange shall either nullify a transaction or adjust the execution price of a transaction that results in an Obvious Error as provided in this Rule.

(a)–(e) No change.

(f) Request for Review. If a party affected by a determination made under this Rule so requests within the time permitted, [a Review Panel of Floor Officials] the Referee will review decisions made under this Rule in accordance with Exchange Rule 124(d). A request for review under this paragraph must be made within thirty minutes after a party receives verbal notification of a final determination by the Floor Official(s) under this Rule, except that if such notification is made after 3:30 p.m. Eastern Time, either party has until 9:30 a.m. Eastern Time on the next trading day to request a review. Such a request for review must be in writing or otherwise documented. The [Review Panel] Referee shall review the facts and render a decision on the day of the transaction, or the next trade day in the case where a request is properly made after 3:30 p.m. on the day of the transaction or where the request is properly made the next trade day.

\* \* \* \* \*

#### **PHILADELPHIA STOCK EXCHANGE, INC. OPTIONS FLOOR PROCEDURE ADVICES AND ORDER AND DECORUM REGULATIONS**

\* \* \* \* \*

#### **F-27 Floor Official Rulings-Options**

Floor Officials are empowered to render rulings on the trading floor to resolve trading disputes occurring on and respecting activities on the trading floor. All rulings rendered by Floor Officials are effective immediately and must be complied with promptly. Failure to promptly comply with a ruling concerning a trading dispute may result in referral to the Business Conduct Committee. Failure to promptly comply with other rulings issued pursuant to Order and Decorum Regulations or Floor Procedure Advices and not concerning a trading dispute may result in an additional violation. Floor Officials need not render decisions in any instance where the request for a ruling was not made within a reasonable period of time. A Floor Official should not render a decision or authorize a citation where such Floor Official was involved in or affected by the dispute, as well as in any situation where the Floor Official is not able to objectively and fairly render a decision.

Floor Officials shall endeavor to be prompt in rendering decisions. However, in any instance where a Floor Official has determined that the benefits of further discovery as to the facts and circumstances of any matter under review outweigh the monetary risks of a delayed rulings, the Floor Official may determine to delay rendering the ruling until such time as that further discovery is completed. In issuing decisions for the resolution of trading disputes, Floor Officials shall institute the course of action deemed by the ruling [f]Floor Official to be more fair to all parties under the circumstances at the time. A Floor Official may direct the execution of an order on the floor, o[f]r adjust the transaction terms or participants to an executed order on the floor. However, two Floor Officials may nullify a transaction if they determine the transaction to have been in violation of Rules 1014 (Obligations and Restrictions Applicable to specialist and ROTs), 1015 (Quotation Guarantees), 1017 (Priority and Parity at Openings in Options), 1033 (Bids and Offers) or 1080 (AUTOM).

[A minimum of three members of the Sub-Committee on Rules and Rulings, a sub-committee of the standing committee, or the Chairperson of the standing committee (or his designee) if three Sub-Committee members cannot be promptly convened, shall be empowered by the standing committee to review Floor Official rulings ("Review Panel"). Requests for a review must be submitted to the Director of the Market Surveillance Department of the Exchange (or his designee) within 15 minutes from the time the contested ruling was rendered. Any person who appeals a Floor Official ruling concerning a trading dispute and loses will be subject to a \$250.00 fee upon a finding by the Review Panel that such appeal is frivolous. The Review Panel shall endeavor to meet on the matter as soon as practicable after notice of a request for a review of a Floor Official ruling. Floor Official rulings may be sustained, overturned or modified by a majority vote of the Review Panel members present. In making a determination, the Review Panel may consider facts and circumstances not available to the ruling Floor Official as well as action taken by the parties in reliance on the Floor Official's ruling (e.g., cover, hedge, and related trading activity). Decisions of the Review Panel will be considered final decisions of the standing committee and may be appealed to the Exchange's Board of Governors pursuant to Exchange By-Law Article XI. Neither Floor Official

rulings nor Review Panel decisions reviewing Floor Official rulings preclude a person from also availing upon the Exchange's Arbitration facilities.]

Exchange staff may determine that a Floor Official is ineligible to participate in a particular ruling where it appears that such Floor Official has a conflict of interest. For purposes of this Rule, and without limitation, a conflict of interest exists where a Floor Official: (a) Is directly or indirectly affiliated with a party seeking a Floor Official ruling; (b) is a participant or is directly or indirectly affiliated with a participant in a transaction that is the subject of a Floor Official ruling; (c) is a debtor or creditor of a party seeking a Floor Official ruling; or (d) is an immediate family member of a party seeking a Floor Official ruling. Exchange staff may consider other circumstances, on a case-by-case basis, in determining the eligibility or ineligibility of a particular Floor Official to participate in a particular ruling due to a conflict of interest.

*All Floor Official rulings concerning the adjustment and nullification of transactions are reviewable by the Referee (as defined in Rule 124).*

*(i) Market Surveillance staff must be advised within 15 minutes of a Floor Official's ruling that a party to such ruling has determined to appeal from such ruling to the Referee. The Exchange may establish the procedures for the submission of a request for a review of a Floor Official ruling. Floor Official rulings concerning the nullification or adjustment of transactions may be sustained, overturned or modified by the Referee. In making a determination, the Referee may consider facts and circumstances not available to the ruling Floor Official as well as action taken by the parties in reliance on the Floor Official's ruling (e.g., cover, hedge and related trading activity).*

*(ii) All decisions made by the Referee in connection with initial rulings on requests for relief and with the review of a Floor Official ruling pursuant to Rule 124(d) shall be documented in writing and maintained by the Exchange in accordance with the record keeping requirements set forth in the Securities Exchange Act of 1934, as amended, and the rules thereunder.*

*(iii) A member or member organization seeking the Referee's review of a Floor Official ruling shall be assessed a fee of \$250.00 for each Floor Official ruling to be reviewed that is sustained and not overturned or modified by the Referee.*

*(iv) Decisions of the Referee concerning (A) the review of Floor Official rulings relating to the nullification or adjustment of transactions, and (B) initial requests for relief shall be final and may not be appealed to the Exchange's Board of Governors.*

*(v) As appropriate, the Chairman of the Options Committee, Foreign Currency Options Committee, or of the Floor Procedure Committee, or their respective designees, shall refer a Referee that fails to make any ruling in accordance with Exchange rules to the Audit Committee for possible disciplinary action, including removal. A Floor Official that fails to make any ruling in accordance with Exchange rules may be subject to possible disciplinary action by the Exchange.*

*(vi) Failure to promptly comply with a Floor Official or Referee decision under this Rule may result in referral to the Business Conduct Committee.*

#### FINE SCHEDULE

\$250.00

\* \* \* \* \*

#### G-2 Trading Rotations, Halts or Reopenings

(a)-(b) No change.

(c) Halts: Trading on the Exchange in any option may be halted with the approval of [one] two Floor Officials, with the concurrence of a Market Surveillance officer, whenever trading on the primary market in underlying securities representing more than 10% of the current index value is halted or suspended. Trading shall be halted whenever [the Exchange] two Floor Officials, with the concurrence of a Market Surveillance officer, deem[s] such action appropriate in the interests of a fair and orderly market and to protect investors. Among the factors that may be considered are the following:

(i)-(iii) No change.

(d)-(f) No change.

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#### PHILADELPHIA STOCK EXCHANGE, INC. EQUITY FLOOR PROCEDURE ADVICES AND ORDER & DECORUM REGULATIONS

\* \* \* \* \*

#### F-27 Floor Official Rulings—Equity

Floor Officials are empowered to render rulings on the trading floor to resolve disputes occurring on and respecting activities on the trading floor. All rulings rendered by Floor Officials are effective immediately and must be compiled with promptly. Failure to promptly comply with a ruling concerning a trading dispute may result in referral to the Business Conduct

Committee. Failure to promptly comply with other rulings issued pursuant to Order and Decorum Regulations of Floor Procedures Advices and no[r]t concerning a trading dispute may result in an additional violation. Floor Officials need not render decisions in any instance where the request for a ruling was not made within a reasonable period of time. A Floor Official should not render a decision or authorize a citation where such Floor Official was involved in or affected by the dispute, as well as in any situation where the Floor Official is not able to objectively and fairly render a decision.

Floor Officials shall endeavor to be prompt in rendering decisions. However, in any instance where a Floor Official has determined that the benefits of further discovery as to the facts and circumstances of any matter under review outweigh the monetary risks of a delayed ruling, the Floor Official may determine to delay rendering the ruling until such time as that further discovery is completed. In issuing decisions for the resolution of trading disputes, Floor Officials shall institute the course of action deemed by the ruling Floor Official to be most fair to all parties under the circumstances at the time. A Floor Official may direct the execution of an order on the floor, or adjust the transaction terms or participants to an executed order on the floor. However, two Floor Officials may nullify a transaction if they determine the transaction to have been in violation of Rules 110 (Bids and Offers—Precedence), 111 (Precedence of Highest Bid), 120 (Precedence of Offers at Same Price), 126 (Crossing), 203 (Agreement of Specialists), 218 (Customer's Order Receives Priority), 229 (PACE System), 232 (Handling Orders When the Primary Market is Not Open for Free Trading), or 455 (Short Sales).

[Equity Floor Official Rulings are reviewable by a minimum of three members of the Floor Procedure Committee, or the Chairperson of the Floor Procedure Committee (or his designee) if three members cannot be promptly convened ("Review Panel"). Requests for a review must be submitted to the Director of the Market Surveillance Department of the Exchange (or his designee) within 15 minutes from the time the contested ruling was rendered. The Review Panel shall endeavor to meet on the matter as soon as practicable after notice of a request for a review of a Floor Official ruling. Floor Official rulings may be sustained, overturned or modified by a majority vote of the Review Panel members present. In making a determination, the Review Panel may

consider facts and circumstances not available to the ruling Floor Official as well as action taken by the parties in reliance on the Floor Official's ruling (e.g., cover, hedge, and related trading activity). Decisions of the Review Panel will be considered final decisions of a standing floor committee and may be appealed to the Exchange's Board of Governors pursuant to Exchange By-Law Article XI. Neither Floor Official rulings nor Review Panel decisions reviewing Floor Official rulings preclude a person from also availing upon the Exchange's Arbitration facilities.]

*All Floor Official rulings concerning the adjustment and nullification of transactions are reviewable by the Referee (as defined in Rule 124).*

*(i) Market Surveillance staff must be advised within 15 minutes of a Floor Official's ruling that a party to such ruling has determined to appeal from such ruling to the Referee. The Exchange may establish the procedures for the submission of a request for a review of a Floor Official ruling. Floor Official rulings concerning the nullification or adjustment of transactions may be sustained, overturned or modified by the Referee. In making a determination, the Referee may consider facts and circumstances not available to the ruling Floor Official as well as action taken by the parties in reliance on the Floor Official's ruling (e.g., cover, hedge and related trading activity).*

*(ii) All decisions made by the Referee in connection with initial rulings on requests for relief and with the review of a Floor Official ruling pursuant to Rule 124(d) shall be documented in writing and maintained by the Exchange in accordance with the record keeping requirements set forth in the Securities Exchange Act of 1934, as amended, and the rules thereunder.*

*(iii) A member or member organization seeking the Referee's review of a Floor Official ruling shall be assessed a fee of \$250.00 for each Floor Official ruling to be reviewed that is sustained and not overturned or modified by the Referee.*

*(iv) Decisions of the Referee concerning (A) the review of Floor Official rulings relating to the nullification or adjustment of transactions, and (B) initial requests for relief shall be final and may not be appealed to the Exchange's Board of Governors.*

*(v) As appropriate, the Chairman of the Options Committee, Foreign Currency Options Committee, or of the Floor Procedure Committee, or their respective designees, shall refer a*

*Referee that fails to make any ruling in accordance with Exchange rules to the Audit Committee for possible disciplinary action, including removal. A Floor Official that fails to make any ruling in accordance with Exchange rules may be subject to possible disciplinary action by the Exchange.*

*(vi) Failure to promptly comply with a Floor Official or Referee decision under this Rule may result in referral to the Business Conduct Committee.*

NO FINE SCHEDULE APPLICABLE.

\* \* \* \* \*

## **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 Phlx 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 Phlx 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 improve the process of resolving trading disputes and Floor Official rulings by creating a new regulatory position on the Exchange, who would be either an Exchange employee or an independent contractor known as a neutral "Referee." The Referee would have the authority to: (1) Review and rule on appeals from Floor Official rulings concerning the nullification or adjustment of trades; and (2) act in the capacity of a Floor Official respecting initial rulings concerning requests for relief from the requirements of certain Exchange rules, Equity Floor Procedure Advices,<sup>6</sup> and Option Floor Procedure Advices.<sup>7</sup>

*Current Floor Official Program.*  
Pursuant to Exchange By-Law Article

<sup>6</sup> The Exchange clarified that a Referee may also have the authority to act in the capacity of a Floor Official respecting initial rulings concerning requests for relief from the requirements of Equity Floor Procedure Advices. Telephone conversation between Richard Rudolph, Vice President and Counsel, Phlx, and Jennifer Dodd, Special Counsel, Division of Market Regulation, Commission, on March 10, 2006 ("Telephone Conversation").

<sup>7</sup> Floor Officials would retain their authority to make such initial rulings. The Referee would simply have the same authority as a Floor Official concerning such initial rulings.

VIII, Floor Officials, as designees<sup>8</sup> of the Chairmen of the Options Committee,<sup>9</sup> Floor Procedure Committee,<sup>10</sup> and Foreign Currency Options Committee,<sup>11</sup> respectively, are authorized to administer the provisions of Exchange By-Laws and Rules of the Exchange pertaining to the respective trading floors and the immediately adjacent premises of the Exchange. They may impose penalties as applicable, for breaches of the Exchange's rules or regulations relating to order, decorum, health, safety and welfare on the respective trading floors. Additionally, they may rule to nullify, or adjust the terms of, executed trades under specific and limited conditions contained in Exchange rules, and may grant relief from certain requirements of on-floor members and member organizations if authorized to do so by rule.

Currently, Floor Official rulings and appeals for review from such rulings are governed by Exchange Rule 124, Disputes. Rule 124(d) provides that Options Floor Official rulings may be appealed to a Review Panel consisting of three members of the Options Subcommittee on Rules and Rulings (the "Subcommittee"),<sup>12</sup> or the Chairperson of the standing committee (or his designee) if three Subcommittee members cannot be promptly convened, and Equity Floor Official rulings may be appealed to a Review Panel consisting of three members of the Floor Procedure Committee, or the Chairperson of the Floor Procedure Committee (or his designee) if three members cannot be promptly convened.<sup>13</sup> Decisions of the Review Panel are considered final decisions of the standing committee and may be appealed to an Advisory

<sup>8</sup> The designees of the respective floor Committee chairmen are generally members of the respective committees and subcommittees thereof.

<sup>9</sup> The Options Committee has general supervision of the dealings of members on the options trading floor. See Exchange By-Law Article X, Section 10-20.

<sup>10</sup> The Floor Procedure Committee has general supervision of the dealings of members on the equity trading floor. See Exchange By-Law Article X, Section 10-16.

<sup>11</sup> The Foreign Currency Options Committee has general supervision of the dealings of members on the foreign currency options trading floor. See Exchange By-Law Article X, Section 10-17.

<sup>12</sup> Each Standing and Special Committee may appoint such subcommittees as it may deem necessary for the efficient discharge of its duties. See Exchange By-Law Article X, Section 10-3(b). The Options Committee has appointed the Subcommittee to review and recommend the adoption of new rules or the amendment of current rules to the full Options Committee, and to discuss rulings made on the floor of the Exchange by Floor Officials.

<sup>13</sup> The Exchange clarified the current process for Equity Floor Official rulings. Telephone Conversation.

Committee on Appeals of the Board of Governors.

Floor Officials are also authorized to rule on requests for relief from the requirements of certain rules, including, without limitation, quote spread parameters,<sup>14</sup> and disengagement of Exchange automatic execution systems under extraordinary circumstances.<sup>15</sup>

*The Referee.* The Referee would be either an Exchange employee or an independent contractor who is not an employee of the Exchange who has entered into an employment contract with the Exchange for a fixed period of time. The Referee would be appointed by the Exchange's Board of Governors pursuant to the recommendation of the Audit Committee. Candidates for the Referee position would be recruited in the same fashion as candidates for other Exchange positions through the Exchange's Human Resources Department. After conducting an interview process with the various candidates, the Audit Committee would recommend its selection to the Board of Governors, who would then vote on the Audit Committee's recommendation. Upon the Commission's approval of this proposal, the Referee would be appointed to the new position.

The proposal would provide that decisions of the Referee concerning both (i) the review of Floor Official rulings relating to the nullification or adjustment of transactions, and (ii) and initial requests for relief, would be final and may not be appealed to the Exchange's Board of Governors.<sup>16</sup> The Referee would be authorized to sustain, overturn, or modify rulings made by Floor Officials and to make initial rulings in certain instances (as described below).

Because the Referee would be authorized to review Floor Official decisions to nullify or adjust trades on both the Exchange's equity and options floors, the proposed rule change includes conforming amendments to OFPA F-27 and to EFPA F-27 concerning such reviews of Floor Official rulings, as discussed more fully below.

As stated above, Floor Officials are authorized to rule on requests for relief from the requirements of certain rules, including, without limitation, quote spread parameters and disengagement of Exchange automatic execution systems

under extraordinary circumstances. The proposed rule change would authorize the Referee to make such rulings in the same manner as Floor Officials.

In order to ensure the neutrality of the Referee, the Referee would report to the Exchange's Audit Committee,<sup>17</sup> which would have supervision over the Referee. The Exchange's General Counsel or his/her designee would be responsible for purely administrative matters such as, without limitation, personnel issues and vacation. Additionally, based on the advice of the Exchange's General Counsel and Human Resources management, the Audit Committee may recommend the level of compensation of the Referee to the Board of Governors, and may establish other conditions of employment of the Referee. The Audit Committee or its designee would conduct annual performance evaluations, and would consider any written complaints from members and member organizations concerning the Referee. The Audit Committee would not, however, have the authority to overrule or modify any ruling made by the Referee. The Audit Committee would have the authority to terminate the employment of the Referee for good cause shown, and to otherwise discipline the Referee as appropriate for good cause shown.

The Referee would have jurisdiction over all Exchange trading floors and systems, except with regard to issues of order and decorum pursuant to Exchange Rule 60. The Options Committee would continue to have jurisdiction over order and decorum issues on the options floor;<sup>18</sup> the Floor Procedure Committee would continue to have jurisdiction over order and decorum issues on the equity floor;<sup>19</sup> and the Foreign Currency Options Committee would continue to have jurisdiction over order and decorum issues on the foreign currency options floor.<sup>20</sup>

The proposed rule change would provide that the Audit Committee would recommend for appointment by the Board of Governors other Exchange employee(s) or independent contractor(s) to function as the Referee in the event that the Referee is unavailable ("Backup Referees"). The Exchange's rules and procedures, including qualifications, applicable to the Referee would also apply to Backup Referees, and any reference to the Referee in the proposed rules would be

deemed to include Backup Referees. This is to ensure that a Backup Referee would be available if the Referee is not available due to, for example, a ruling on another matter that is in progress, vacation, illness, etc.

The proposal also would provide that the Market Surveillance staff would assign available Floor Officials to rule on disputes. The Exchange believes that this provision should ensure the neutrality of Floor Officials by assigning the next available Floor Official to rule on a particular matter.

*Qualifications of the Referee.* Under the proposal, the Referee would be required to have sufficient expertise in the area of trading to act in the capacity of a Floor Official concerning requests for relief and to conduct reviews of Floor Official rulings concerning the nullification and adjustment of trades. The Referee must possess sufficient knowledge of Exchange rules and the relevant sections of the Act (and the rules thereunder) to administer the Referee's responsibilities and authority.

In order to ensure neutrality, the proposal would provide that the Referee may not be a member of the Exchange, may not be directly or indirectly affiliated with any Exchange member or member organization, and may not be an immediate family member of any Exchange member. The Referee may not be a debtor or creditor of any Exchange member or member organization.

*Duties of the Referee.* The primary responsibility of the Referee would be to rule on appeals from Floor Official decisions concerning the nullification and adjustment of trades, and to have the same authority as Floor Officials concerning rulings on member requests for relief from the requirements of certain rules. The Referee would replace the current three-member Review Panel, which is currently comprised of Floor Officials, and would be authorized to review Floor Official rulings concerning the adjustment of the terms of a trade, or the nullification or "bust" of trades on appeal, and either uphold, overturn, or modify appealed Floor Official rulings pursuant to proposed amended Rule 124. If the Referee is unavailable or unable to make a ruling for any reason (including, without limitation, absence from the Exchange trading floor, vacation, illness, or in the process of making another Referee ruling), Market Surveillance staff will immediately notify the Exchange's General Counsel, or his designee, who would designate a Backup Referee to make such a ruling.

The proposed rule change would provide that the Exchange's General Counsel or his or her designee may assign additional duties and

<sup>14</sup> Relief from the established bid/ask differentials may be granted upon the receipt of an approval of two Floor Officials. See OFPA F-6.

<sup>15</sup> See Exchange Rule 1080(e).

<sup>16</sup> The Exchange clarified that a Referee may review Floor Official rulings relating to the nullification or adjustment of transactions. Telephone Conversation.

<sup>17</sup> See proposed Exchange By-Law Article X, Section 10-9.

<sup>18</sup> See Exchange By-Law Article X, Section 10-20.

<sup>19</sup> See Exchange By-Law Article X, Section 10-16.

<sup>20</sup> See Exchange By-Law Article X, Section 10-17.



responsibilities to the Referee not related to Referee rulings. In order to ensure the Referee's neutrality respecting any matter on which he or she is to rule, and to avoid the possibility that the Referee could be biased as a result of his or her knowledge of any pending investigation or disciplinary action concerning a person that is a party to a dispute or that requests relief from the requirements of an Exchange rule, the proposal would prohibit the Referee from: (i) Participating in any Exchange enforcement action, investigation, market surveillance activity, hearing (other than as a witness) or other activity related to disciplinary matters; (ii) issuing citations for violations of Exchange rules; (iii) ruling on any matter concerning order and decorum pursuant to Exchange Rule 60 and the regulations thereunder; and (iv) preparing, researching, drafting, reviewing, or filing of a proposed rule change with the Commission pursuant to the Act and the rules thereunder concerning the Exchange's disciplinary rules.

The proposed rules would require the Referee to make fair and impartial decisions in accordance with Exchange rules and By-Laws.

*Procedures for Review of Floor Official Rulings.* Proposed amended Rule 124(d), OFPA F-27, and EFPA F-27 would require that Market Surveillance staff be advised within 15 minutes of a Floor Official ruling concerning the nullification or adjustment of a trade that a party to such ruling has determined to seek the Referee's review of such ruling. The purpose of the notification requirement is to provide reasonably prompt notice to Market Surveillance and to participants in a trade subject to the rule that such ruling is subject to appeal and that the process set forth in the proposed rule has begun, and ultimately a decision to sustain, overturn, or modify the initial Floor Official decision concerning the trade will be made.<sup>21</sup>

As appropriate, the Chairman of the Options Committee, the Foreign Currency Options Committee or of the Floor Procedure Committee, or their respective designees,<sup>22</sup> would be

required to refer a Referee that fails to make any ruling in accordance with Exchange rules to the Audit Committee for possible disciplinary action, including removal. A Floor Official that fails to make any ruling in accordance with Exchange rules may be subject to possible disciplinary action by the Exchange.

In order to minimize the likelihood of frivolous appeals from Floor Official rulings, a member or member organization seeking the Referee's review of a Floor Official ruling concerning the nullification or adjustment of a trade would be assessed a fee of \$250.00 for each Floor Official ruling they seek to have reviewed if the Referee upholds the Floor Official decision. No fee would be assessed to the member or member organization seeking a review if the Floor Official decision is overturned or modified. This fee is currently imposed on options floor appeals that are found by the Review Panel to be frivolous.<sup>23</sup> The Exchange believes that the proposed rule concerning the \$250.00 fee provides an objective standard for imposition of the fee (*i.e.*, the fee would be imposed in situations where the Referee sustains a Floor Official ruling on the nullification or adjustment of a trade). Thus, the Referee would not have the discretion to impose the fee that Floor Officials currently have, and Exchange members and member organizations would have actual notice of the circumstances giving rise to the imposition of the fee.

*Rulings on Requests for Relief.* Proposed Rule 124, Commentary .02(a) would authorize the Referee to act in the capacity of a Floor Official respecting initial rulings concerning requests for relief from the requirements of Exchange Rules relating to: (i) Bid/ask differentials pursuant to Rule 1014(c) and OFPA F-6; (ii) disengagement of Exchange automatic execution systems pursuant to Rule 1080(e) and OFPA A-13; (iii) the determination that quotes in options on the Exchange or another market or markets are subject to relief from the firm quote requirement pursuant to Exchange Rule 1080(c)(i); and (iv) trading halts, openings and re-openings pursuant to Rules 1017, 1047 and 1047A and OFPAs A-12, A-14 and G-2.

Rule 1014(c) and OFPA F-6 set forth the maximum allowable bid/ask differentials, or quote widths, that may be disseminated by specialists and ROTs on the Exchange, depending on the price of the series to be quoted. The

Exchange believes that these requirements can have the unintended consequence of requiring those making markets to quote at prices that are unnecessarily narrow, thereby exposing them to great risk if markets move quickly.<sup>24</sup> Therefore, as stated in OFPA F-6, two Floor Officials may grant relief from these differentials during times of peak market activity where options markets and/or the market for securities underlying the option move quickly. Under the proposal, the Referee would have the same authority as a Floor Official to make such a ruling.

Rule 1080(e) and OFPA A-13 provide that, in the event extraordinary circumstances with respect to a particular class of options exist, two Floor Officials may determine to disengage AUTO-X with respect to that option, in accordance with Exchange procedures. The rule and OFPA go on to describe the procedures to be followed to bring about such disengagement. Under the proposal, the Referee would have the same authority as a Floor Official to make such a determination.

Rule 1080(c)(i) provides that the Chairman of the Exchange's Options Committee or his designee (or if neither is available, two Floor Officials) may determine that quotes in options on the Exchange or another market or markets are subject to relief from the firm quote requirement set forth in the SEC Quote Rule,<sup>25</sup> (thereby excluding such quotes from the Exchange's calculation of the National Best Bid/Offer ("NBBO")) and that quotes in options on the Exchange or another market or markets previously subject to such relief are no longer subject to such relief. The Referee would have the same authority as a Floor Official in making determinations concerning the above enumerated rules that require Floor Official rulings.

Rules 1017, 1047 and 1047A and OFPAs A-12, A-14<sup>26</sup> and G-2 govern trading halts, openings and re-openings on the Exchange.<sup>27</sup> Under the proposal, the Referee would have the same authority as a Floor Official to make rulings in the capacity of a Floor Official

<sup>24</sup> See, *e.g.*, Securities Exchange Act Release No. 50728 (November 23, 2004), 69 FR 69982 (December 1, 2004) (SR-Phlx-2004-74) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 by the Philadelphia Stock Exchange, Inc. Relating to \$5 Bid/Ask Differentials).

<sup>25</sup> 17 CFR 242.602.

<sup>26</sup> The Exchange clarified that the Referee would also have the same authority as a Floor Official to make rulings in the capacity of a Floor Official under OFPA A-14. Telephone Conversation.

<sup>27</sup> For consistency, the Exchange is proposing a conforming amendment to OFPA G-2, as described below.

<sup>21</sup> This is consistent with Exchange Rule 1092, Obvious Errors, which establishes a similar notice period. Under the proposal, Floor Official rulings made pursuant to Rule 1092 would be reviewed by the Referee, provided that the party seeking the review so requests within the time permitted. See proposed Rule 1092(f).

<sup>22</sup> The Exchange clarified that the Chairman of the Foreign Currency Options Committee, or his designee, would also be required to refer a Referee to the Audit Committee for disciplinary action, if appropriate. Telephone Conversation.

<sup>23</sup> This fee is not currently imposed on equity floor appeals. Telephone Conversation.

concerning rules that require Floor Official approval, as enumerated above.

*Referee's Decision Final.* As stated above, currently decisions of the Review Panel are considered final decisions of the standing committee and may be appealed to an Advisory Committee on Appeals of the Board of Governors. Initial rulings to grant or deny relief from the requirements of certain rules are not currently considered final decisions of a standing committee and are thus not currently appealable to the Exchange's Board of Governors.

The proposed rule change would provide that decisions of the Referee concerning (A) the review of Floor Official rulings relating to the nullification or adjustment of transactions, and (B) initial requests for relief, shall be final and may not be appealed to the Exchange's Board of Governors. The Exchange does not believe that these are the types of decisions that are appropriate for such appeals particularly because the need for speedy resolution and certainty are important, whereas other standing committee decisions are often prospectively applied.

This provision would not operate to preclude any aggrieved member or member organization from proceeding with any other legal remedy to which such member or member organization might be entitled (e.g., arbitration or appeal to the Commission if allowable by law).

*Obvious Errors.* The Exchange also proposes to amend Exchange Rule 1092, Obvious Errors. Currently, Rule 1092(f), Request for Review, provides that a Review Panel of Floor Officials will review decisions made under the Rule in accordance with Exchange Rule 124(d). For consistency, the Exchange proposes to amend Rule 1092(f) to provide that the Referee will review such decisions.

*Conforming Amendment to OFPA G-2.* As a housekeeping matter, the Exchange proposes to amend OFPA G-2(c), to reflect that trading on the Exchange in any option may be halted with the approval of two Floor Officials, with the concurrence of a Market Surveillance officer. Current Rule 1047A(c) includes this provision, and the Exchange proposes to amend OFPA G-2 for consistency.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>28</sup> in general, and furthers the

objectives of Section 6(b)(5) of the Act<sup>29</sup> in particular, 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, by establishing a neutral Referee to rule on appeals from Floor Official decisions and to rule initially on requests for relief from certain requirements under Exchange rules. The Exchange further believes that the proposal is consistent with 6(b)(1) of the Act,<sup>30</sup> in that the proposal is designed to enable the Exchange to continue to comply, and to enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulations thereunder, and the rules of the Exchange by improving the Exchange's Floor Official process and improving the review process of Floor Official rulings.

### *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 that is not necessary or appropriate in furtherance of the purposes of the Act.

### *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 35 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 Phlx consents, the Commission will:

(A) By order approve 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, as amended, 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-2005-42 on the subject line.

### *Paper Comments*

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

All submissions should refer to File Number SR-Phlx-2005-42. 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 inspection and copying in the Commission's Public Reference Room. Copies of the filing also will be available for inspection and copying at the principal office of the Phlx. 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-2005-42 and should be submitted on or before April 21, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>31</sup>

**Nancy M. Morris,**

*Secretary.*

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<sup>28</sup> 15 U.S.C. 78f(b).

<sup>29</sup> 15 U.S.C. 78f(b)(5).

<sup>30</sup> 15 U.S.C. 78f(b)(1).

<sup>31</sup> 17 CFR 200.30-3(a)(12).