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SECURITIES AND EXCHANGE COMMISSION
[Release No. 34-71417; File No. SR-Phlx-2014-04]

Self-Regulatory Organizations; NASDAQ OMX PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Outbound Routing

January 28, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1], and Rule 19b-4 thereunder,[2] notice is hereby given that on January 15, 2014, NASDAQ OMX PHLX LLC ("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 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 use Nasdaq Execution Services, LLC ("NES") as opposed to Nasdaq Options Services LLC ("NOS") for outbound order routing, as explained further below. The Exchange also proposes to use NES as opposed to NOS to handle the stock component of a Complex Order, including Complex Orders submitted into the Price Improvement XL ("PIXL") System. In addition, the Exchange proposes to route equities and options orders through NES either directly or through a third party routing broker-dealer, as explained further below.

1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

The text of the proposed rule change is available on the Exchange's Website at http://nasdaqomxphlx.cchwallstreet.com/, at the principal office of the Exchange, and at the Commission's Public Reference Room.

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 update the Exchange's rules to reflect the ability to route orders to other exchanges using either the Exchange's affiliated broker-dealer or a third party unaffiliated broker-dealer, which the Exchange may choose to use for efficiency and potential cost savings.

Today, the relevant Exchange rules provide that the Exchange shall route orders in options via Nasdaq Options Services LLC ("NOS") and in equities[3] via Nasdaq Execution Services LLC ("NES"). Both NOS and NES are affiliates and member organizations of Phlx. As a result, certain conditions have been imposed on the existing routing arrangements.[4]

Replacing NOS with NES

The Exchange proposes to amend its rules to provide that it shall use NES for routing orders in options rather than NOS. The Exchange has determined to use NES for outbound

3 The Exchange operates an equities market known as PSX.

4 See, e.g., Securities Exchange Act Release No. 59995 (May 28, 2009), 74 FR 26751 (June 3, 2009) (SR-Phlx-2009-32) at 26756.

routing in options, in addition to equities. The Exchange originally set up its affiliated broker-dealers as two separate entities. Now, the Exchange believes that this is unnecessary and costly. Accordingly, pursuant to Rule 1080(m)(iii), NES will now be the outbound routing broker for Phlx options. As the new Routing Facility for options, NES will operate the same way as NOS currently does, in terms of routing options orders to destination options exchanges pursuant to Rule 1080(m). This is substantially similar to NYSEArca's use of its affiliate Archipelago Securities LLC for order routing in both equities and options.

In addition to outbound order routing, NOS also, with Commission approval,[5] currently executes and reports the underlying security component of a Complex Order, pursuant to Rule 1080.08(h). A Complex Order is an order involving the simultaneous purchase and/or sale of two or more different options series in the same underlying security, priced as a net debit or credit based on the relative prices of the individual components, for the same account, for the purpose of executing a particular investment strategy.[6] A Complex Order can also be a stock-option order, which is an order to buy or sell a stated number of units of an underlying security (stock or Exchange Traded Fund Share ("ETF")) coupled with the purchase or sale of options contract(s).[7] Members of FINRA or the NASDAQ Stock Market ("NASDAQ") are required to have a Uniform Service Bureau/Executing Broker Agreement ("AGU") with NOS in order to trade Complex Orders containing a stock/ETF component; firms that are not members of FINRA or NASDAQ are required to have a Qualified Special Representative ("QSR") arrangement with NOS in order to trade Complex Orders containing a stock/ETF component. Under this proposal,

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5 Securities Exchange Act Release No. 63777 (January 26, 2011), 76 FR 5630 (February 1, 2011)(SR-Phlx-2010-157).

6 See Rule 1080.08(a)(i).

7 Id.

members will now be required to have an AGU or QSR with NES. In terms of NOS' role in the execution of such Complex Orders, the Exchange electronically communicates the underlying security component of a Complex Order to NOS, its designated broker-dealer, for immediate execution. The execution cannot occur on PHLX along with the option component, because the PHLX options market does not trade equities like stocks or ETFs. Such execution and reporting occurs otherwise than on the Exchange and is handled by NOS pursuant to applicable rules regarding equity trading. NES will now perform this function and this paragraph will be amended accordingly.

Rule 1080(n)(ii)(J) will be amended in a similar fashion. This subparagraph covers Complex Orders with a stock/ETF component entered into PIXL, which is a process whereby members electronically submit orders they represent as agent against principal interest or other interest that they represent as agent. The submitted orders are stopped at a price and are subsequently entered into an auction seeking price improvement. In 2013, the Exchange began accepting Complex Orders into PIXL, including those with a stock/ETF component.[8] NOS' role is the same as for Complex Orders not entered into PIXL, in that NOS executes the stock/ETF component. NES will now perform this function and this paragraph will be amended accordingly. Additionally, the Exchange represents that its prior representations in connection with the performance of executing the stock/ETF component of both PIXL and non-PIXL Complex Orders by NOS will apply to NES, including the representations relating to compliance with Regulation SHO.[9]

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8 Securities Exchange Act Release No. 69845 (June 25, 2013), 78 FR 39429 (July 1, 2013) (SR-Phlx-2013-46).

9 Id. See also Securities Exchange Act Release Nos. 63777 (January 26, 2011), 76 FR 5630 (February 1, 2011)(SR-Phlx-2010-157); and 63967 (February 25, 2011), 76 FR

Third-Party Routing Broker

The Exchange also proposes to codify in its rules the ability to use a third-party routing broker to route to away exchanges, rather than routing directly through NES, for both equities and options. To date, the Exchange has used a third-party routing broker in equities and is amending Rule 3315 to clarify this and incorporate the use of a third-party routing broker expressly into that rule. Specifically, today, the Exchange routes equities orders to away markets through NES, which, in turn, sometimes routes directly to away markets; in addition, sometimes when the Exchange routes equities orders through NES today, NES routes those orders through a third-party routing broker.

In options, the Exchange currently routes options orders to NOS, which routes directly to away markets. The Exchange proposes to use NES, rather than NOS, as explained above, and to have NES route either directly to other options exchanges or to a third-party routing broker (which will, in turn, route to other options exchanges). The Exchange proposes to amend Rule 1080(m) accordingly.

Regardless of whether a third-party routing broker is used in either equities or options, all routing will go through NES, but the Exchange could determine to direct NES to route orders to certain exchanges through a routing broker rather than routing an order directly.

The Exchange previously stated that from time to time, it may use non-affiliate third-party broker-dealers to provide outbound routing services (*i.e.*, third-party Routing Brokers).[10] In those cases, orders are submitted to the third-party Routing Broker through the affiliated

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12206 (March 4, 2011) (SR-Phlx-2011-27).

10 See Securities Exchange Act Release Nos. 68393 (December 10, 2012), 77 FR 74520 (December 14, 2012)(SR-Phlx-2012-134) at note 4; and 67654 (August 14, 2012), 77 FR 50187 (August 20, 2012)(SR-Phlx-2012-81) at note 6.

routing broker, and the third-party Routing Broker routes the orders to the routing destination in its name.

Under this proposal, the relevant rules would now expressly provide that the Exchange could use one or more third-party unaffiliated routing broker-dealers ("routing brokers"). Specifically, the Exchange proposes to amend Rule 1080(m)(iii)(A), which applies to options, to refer to such routing brokers. The Exchange proposes to similarly amend Rule 3315(b)(1) respecting equities. The Exchange proposes to further amend its rules with respect to certain policies and procedures. Specifically, Rules 1080(m)(iii)(C) and 3315(b)(8) currently provide that the Exchange shall establish and maintain procedures and internal controls reasonably designed to adequately restrict the flow of confidential and proprietary information between the Exchange and the Routing Facility, and any other entity, including any affiliate of the Routing Facility. The Exchange proposes to amend those rules to provide that, where there is a routing broker, the Exchange shall establish and maintain procedures and internal controls reasonably designed to adequately restrict the flow of confidential and proprietary information between the Exchange, the Routing Facility and any routing broker, and any other entity, including any affiliate of the routing broker (and if the routing broker or any of its affiliates engages in any other business activities other than providing routing services to the Exchange, between the segment of the routing broker or affiliate that provides the other business activities and the segment of the routing broker that provides the routing services).[11] This way, this provision extends to the routing broker, if one is used.

In both the proposed equities and options rules, the Exchange proposes to provide that the Exchange may not use a routing broker for which the Exchange or any affiliate of the Exchange

11 This is substantially similar to NYSEArca Rule 6.96(a)(8).

is the designated examining authority. This is similar to the existing provisions that do not permit the Exchange to be the designated examining authority for its affiliated routing brokers.[12]

The Exchange also proposes to expressly state in Rule 1080(m)(iii)(G) and Rule 3315(b)(1) that the Exchange will determine the logic that provides when, how, and where orders are routed away to other exchanges. In addition, the routing broker(s) cannot change the terms of an order or the routing instructions, nor does the routing broker have any discretion about where to route an order. This is consistent with, but more specific than, the current language that states that routing is performed under the direction of the Exchange.[13]

The Exchange may determine to use a different routing broker by product or by destination exchange, depending upon the costs and technological efficiencies involved. The proposal is intended to allow the Exchange to structure its routing arrangements accordingly. At a minimum, the Exchange anticipates using a routing broker to access certain markets where the Exchange finds that the costs of maintaining a membership (for NES) and/or the costs of connectivity and execution do not make sense in light of the number or types of orders the Exchange typically routes to that particular market. These costs necessarily determine the ultimate costs to the Exchange of routing to a market, and, in turn, affect how the Exchange chooses to recoup those costs through its own transaction fees.[14] Sometimes, it will not make

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12 See Phlx Rule 1080(m)(iii)(A) (which currently provides that NOS is a broker-dealer that is a member of an unaffiliated self-regulatory organization which is the designated examining authority for the broker-dealer) and Rule 3315(b)(4) (which currently provides that the designated examining authority for NES shall be a self-regulatory organization unaffiliated with the exchange or any of its affiliates). This is also substantially similar to NYSEArca Rule 6.96(a)(7).

13 This is based on NYSEArca Rule 6.96(a)(1)(A).

14 For these reasons, today, transaction fees for orders vary depending on the market where an order is ultimately executed. See e.g., Section V of the NASDAQ OMX PHLX

economic sense for NES to access an exchange directly. Accordingly, the Exchange intends to use a routing broker where the Exchange determines that it is appropriate. In addition to costs, the Exchange will also consider ease of connectivity and execution as well as general reliability in selecting a routing broker.

For several weeks, the Exchange has been working with the Financial Regulatory Authority ("FINRA") and The Options Clearing Corporation ("OCC") to secure the necessary approvals for NES to perform these functions. The Exchange has now secured those approvals. The Exchange seeks to complete this process and implement this proposal in January or February.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act[15] in general, and furthers the objectives of Section 6(b)(5) of the Act[16] 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 providing an alternative routing arrangement. The proposal should remove impediments to and perfect the mechanism of a free and open market and a national market system by providing customer order protection and by facilitating trading at away exchanges so customer orders trade at the best market price. The proposal should also protect investors and the public interest by fostering compliance with the Options Order Protection and Locked/Crossed Market Plan. The Exchange also believes that the proposal to

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Pricing Schedule.

15 15 U.S.C. 78f(b).

16 15 U.S.C. 78f(b)(5).

use NES rather than NOS for options routing is designed to promote just and equitable principles of trade and to protect investors and the public interest, by eliminating the costs and inefficiencies associated with operating a separate broker-dealer for options routing. In addition, the Exchange believes that the proposal is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, because there are specific protections pertaining to the routing broker in light of the potential conflict of interest where the member routing broker could have access to information regarding other members' orders or the routing of those orders. These protections include the Exchange's control over all routing logic as well as the confidentiality of routing information.[17] The proposal to use NES rather than NOS for Complex Order-related functions is consistent with promoting just and equitable principles of trade and protecting investors and the public interest, because it merely substitutes one affiliated broker-dealer for another. For the same reason, compliance with Regulation SHO will not be affected.

(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 proposal is pro-competitive because it enables broker-dealers other than NOS and NES to provide routing services to the Exchange, which has the potential to reduce the Exchange's costs of routing orders and, potentially, the fees the Exchange charges for routed orders. The proposal does not raise issues of intra-market competition, because the Exchange's decision to route through a particular routing broker would impact all participants equally.

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[17] See proposed Rules 1080(m)(iii)(G) and 3315(b)(1).

(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

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act[18] and subparagraph (f)(6) of Rule 19b-4 thereunder.[19]

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is: (i) Necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or 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:

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18 15 U.S.C. 78s(b)(3)(a)(ii).

19 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

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. Please include File Number SR-Phlx-2014-04 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-Phlx-2014-04. 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-2014-04 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.[20]

Kevin M. O'Neill,
Deputy Secretary.

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[20] 17 CFR 200.30-3(a)(12).