

Spreads; (2) transaction costs; (3) payment for order flow; and (4) quote message traffic.

The Commission believes that the thirteen options classes to be included in the penny pilot program represent a diverse group of options classes with varied trading characteristics. This diversity should facilitate analyses by the Commission, the options exchanges and others. The Commission also believes that the Penny Pilot Program is sufficiently limited that it is unlikely to increase quote message traffic beyond the capacity of market participants' systems and disrupt the timely receipt of quote information.

Nevertheless, because the Commission expects that the Penny Pilot Program will increase quote message traffic, the Commission is also approving the Exchange's proposals to reduce the number of quotations it disseminates.

SIFMA commented on the CBOE's quote mitigation proposal.<sup>11</sup> SIFMA recommends that all six of the option exchanges adopt a comprehensive and uniform quote mitigation strategy. In particular, SIFMA strongly supports the adoption of the "holdback timer" mitigation proposal as the most efficient means of reducing quotation traffic. SIFMA, however, expressed concern that the lack of uniformity among the quote mitigation proposals adopted by the exchanges will impose a burden on member firms and cause confusion for market participants, especially retail investors.

Although SIFMA urges the adoption of a uniform and comprehensive approach to quote mitigation, it does not oppose CBOE's quote mitigation proposals. In fact, SIFMA acknowledges that certain of CBOE's proposals, such as notifying members whose quote activity suggests systems malfunctions or wrong settings and delisting inactive series can contribute to quote mitigation. SIFMA, however, expressed its belief that these proposals do not go far enough to resolve the industry's concerns regarding systems capacity.

Although the Commission supports efforts to implement a uniform, industry-wide quote mitigation plan, it does not believe such efforts preclude individual exchanges from initiating their own quote mitigation strategies. The Commission agrees with CBOE that its proposed quote mitigation strategies will not lead to confusion among market participants.<sup>12</sup>

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>13</sup> that the proposed rule change (SR-CBOE-2006-92), as modified by Amendment No. 1, be, and hereby is, approved on a six month pilot basis, which will commence on January 26, 2007.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

[FR Doc. E7-1586 Filed 1-31-07; 8:45 am]

**BILLING CODE 8011-01-P**

#### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-55172; File No. SR-CBOE-2006-110]

#### Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change and Amendment No. 1 Thereto Relating to the Establishment of CBOE Stock Exchange, LLC

January 25, 2007.

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 December 26, 2006, the Chicago Board Options Exchange, Incorporated (the "CBOE" or "Exchange") filed with the Securities and Exchange Commission (the "SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by the Exchange. CBOE filed Amendment No. 1 to the proposed rule change on January 10, 2007. 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

CBOE proposes to establish CBOE Stock Exchange ("CBSX") as a facility, as that term is defined in Section 3(a)(2) of the Act,<sup>3</sup> of CBOE. CBSX will administer a fully automated marketplace for the trading of securities other than options by CBOE members. CBSX will be operated by CBOE Stock Exchange, LLC ("CBSX LLC"), a Delaware limited liability company. In

this filing, CBOE submitted to the Commission the First Amended and Restated Operating Agreement ("Operating Agreement") of CBSX LLC. The Certificate of Formation and the Operating Agreement are the source of CBSX LLC's governance and operating authority, and therefore, function in a similar manner as articles of incorporation and bylaws for a corporation. Additionally, CBOE proposes to adopt Rule 3.32 pertaining to ownership concentration and affiliation limitations.

The text of the proposed rule change is available on the Exchange's Web site (<http://www.cboe.com>), at the Office of the Secretary, CBOE, and at the Commission's Public Reference Room. The text of the proposed rule change is also available on the Commission's Web site (<http://www.sec.gov/rules/sro.shtml>).

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

In its filing with the Commission, CBOE 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. CBOE 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

CBOE is a registered national securities exchange under Section 6 of the Act and a self-regulatory organization ("SRO"). CBOE indicates that CBSX will be a facility of CBOE, subject to self-regulation by CBOE and oversight by the SEC. CBOE will act as the SRO for CBSX pursuant to a Services Agreement to be entered into between CBOE and CBSX LLC. CBOE will have the primary regulatory responsibility for the activities of CBSX. CBOE represents that it has adequate funds to discharge all regulatory functions related to the facility that it has undertaken to perform under the Services Agreement.<sup>4</sup>

<sup>13</sup> 15 U.S.C. 78s(b)(2).

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> 15 U.S.C. 78c(a)(2).

<sup>4</sup> CBOE represents that CBSX LLC will not be entitled to any revenue generated in connection with penalties, fines, and regulatory fees that may be assessed by CBOE against CBOE members in connection with trading on CBSX. Rather, all

<sup>11</sup> See SIFMA Letter, *supra* note 4.

<sup>12</sup> See CBOE Letter, *supra* note 6.

In this filing, CBOE submitted to the SEC the Certificate of Formation and the Operating Agreement of CBSX LLC, which specifically relate to the control and governance of CBSX LLC that would ensure that CBOE has the authority within CBSX LLC to maintain CBOE's responsibility for all regulatory functions related to CBSX. The Operating Agreement provides that CBOE and the SEC would have regulatory authority over the CBSX LLC owners and the members of CBSX LLC's Board of Directors. CBOE will submit separate rule filings to establish rules relating to listing, membership and trading on CBSX.<sup>5</sup> Because the primary purpose of this rule filing is to focus on those provisions that are directly related to CBSX LLC's governance and ownership, and CBOE's authority for all regulatory functions of the CBSX, the Exchange's discussion in this filing will be limited to those relevant provisions of the Operating Agreement.

#### *CBSX LLC*

As a limited liability company, ownership of CBSX LLC is represented by limited liability membership interests in CBSX LLC. The holders of such interests are referred to as "Owners" in this rule filing.<sup>6</sup> Initially, there are five Owners of CBSX LLC. CBOE is one of the Owners of CBSX LLC, and owns all "Series A" Voting Shares<sup>7</sup> of CBSX LLC, representing

regulatory fines, penalties and fees assessed against and paid by CBOE members to CBOE in connection with trading on CBSX shall remain with CBOE.

<sup>5</sup> The Commission notes that on December 18, 2006, the Exchange filed a proposed rule change relating to a permit program for CBSX. See Securities Exchange Act Release No. 54987, 71 FR 78481 (December 29, 2006). The Commission also notes that on December 29, 2006, the Exchange filed a proposed rule change to establish the equity trading rules for CBSX. See Securities Exchange Act Release No. 55034, 72 FR 1350 (January 11, 2007).

<sup>6</sup> "Owner" means a limited liability company "member" as that term is defined in § 18-101(11) of the Delaware Limited Liability Company Act ("DLLCA"), and shall include each Voting Owner and each Management Owner, but only so long as such person is shown on CBSX's books and records as the owner of at least one (1) Share (or fraction of one (1) Share). "Owner" shall include a "Substituted Owner" as defined in Section 6.5(a) of the Operating Agreement, but only upon compliance with all of the requirements of Sections 6.4 and 6.5 of the Operating Agreement. For purposes of clarity, no person shall become an "Owner" as to any Shares, if the acquisition of those Shares will require a change of ownership notice to the SEC, or will constitute a proposed rule change subject to the requirements of the rule filing process of Section 19 of the Act, until all of the requirements of such notice or rule filing process have been accomplished and, if necessary, approved by the SEC. See Section 2.1(16) of the Operating Agreement.

<sup>7</sup> "Voting Shares" means those Shares entitled to vote on matters submitted to the Owners, which Voting Shares are held by the Voting Owners. See Section 2.1(27) of the Operating Agreement.

(50%) of CBSX LLC.<sup>8</sup> The other four Owners and their respective ownership interests are: VDM Chicago, LLC (20%); LaBranche & Co., Inc. (10%); IB Exchange Corp. (10%); and Susquehanna International Group, LLP. (10%). Each of these four Owners owns "Series B" Voting Shares of CBSX LLC.

Under Section 3.2 of the Operating Agreement, the CBSX LLC Board of Directors may authorize the issuance of "Series C" Non-Voting Restricted Shares<sup>9</sup> from time to time to employees, consultants, or officers of CBSX LLC, or any other person, each of whom will become a Management Owner<sup>10</sup> of CBSX LLC.

As provided in Section 8.9 of the Operating Agreement, the outstanding Series A Voting Shares shall, in the aggregate (and without being deemed to be a voting trust), be entitled to a number of votes equal to 50% of the total number of Voting Shares outstanding, on each matter submitted to a vote of the Owners. Each outstanding Series B Voting Share shall be entitled to one vote on each matter submitted to a vote of the Owners. The Series C Non-Voting Restricted Shares shall not be entitled to vote on any matter submitted to a vote of the Owners.

#### *Governance of CBSX LLC*

Pursuant to Section 9.1 of the Operating Agreement, CBSX LLC will be managed by or under the direction of its own Board of Directors. Section 9.2 of the Operating Agreement provides that the Board of Directors will consist of 9 Directors and also provides how the composition of the Board of Directors shall be determined. Each Owner

<sup>8</sup> As noted in Section 3.2 of the Operating Agreement, it is the intention of the Owners that no other members of CBSX LLC (other than Affiliates of CBOE) be owners of Series A Voting Shares, and that no additional Series A Voting Shares be authorized, created or issued for such purpose; provided however, that this provision is not intended to limit or restrict any rights of CBOE to transfer any of its Series A Voting Shares with the prior approval of the SEC as provided for in Article VI, including Section 6.14 of the Operating Agreement, or any other provision thereof, or any rights to be acquired by a transferee of those Shares as provided therein.

<sup>9</sup> "Non-Voting Restricted Share" means a Share held by a Management Owner containing the voting limitations and other restrictions described in the Operating Agreement. See Section 2.1(15) of the Operating Agreement.

<sup>10</sup> "Management Owner" means a natural person who is identified on Exhibit A of the Operating Agreement (Exhibit 5C to the proposed rule change) as a Management Owner, who subsequently becomes a Management Owner pursuant to the provisions of Section 3.2(c) of the Operating Agreement, or who is a transferee or assignee of Non-Voting Restricted Shares (other than a Voting Owner). See Section 2.1(13) of the Operating Agreement.

owning Series B Voting Shares representing at least five percent (5%) of the aggregate "Percentage Interests"<sup>11</sup> of CBSX LLC shall be entitled to designate one Director. The Owners of Series A Voting Shares (currently, CBOE) shall collectively be entitled to designate a number of Directors equal to the aggregate number of Directors designated by the Owners owning Series B Voting Shares representing at least five percent (5%) of the aggregate Percentage Interests of CBSX LLC. The Directors then shall designate one additional Director from the executive management of CBSX LLC.

Thus, initially, VDM Chicago, LLC, LaBranche & Co., Inc., IB Exchange Corp., and Susquehanna International Group, LLP will each be entitled to designate one Director. CBOE, as the Owner of the Series A shares, will be entitled to designate four Directors. The eight Directors will then designate one additional Director from among the executive management of CBSX LLC.

Section 9.2 of the Operating Agreement also provides that as long as CBSX remains a facility of CBOE, CBOE shall have the right to retain/designate one Director in the event CBOE is no longer otherwise entitled to designate any Directors pursuant to Section 9.2 of the Operating Agreement, whether or not CBOE maintains any Percentage Interest or is admitted to CBSX as an Owner.

Under Section 9.3 of the Operating Agreement, a Director appointed pursuant to Section 9.2 of the Operating Agreement shall serve until his or her earlier death, resignation, or removal in a manner permitted by applicable law or the Operating Agreement, or, with respect to Directors designated by Owners of Series B Voting Shares, until such time as the Owner designating such Director ceases to own a Percentage Interest representing at least five percent (5%) of the aggregate Percentage Interests of CBSX LLC. In such latter event, upon the termination of service of such a Series B-designated Director, the service of a single Director designated by the Owner(s) of the Series A Voting Shares (identified by the Series A Owner(s) in their sole discretion) shall simultaneously terminate.

Section 1.8 of the Operating Agreement provides that notwithstanding anything contained in

<sup>11</sup> "Percentage Interest" means with respect to an Owner, a fraction (expressed as a percentage) determined from time to time, the numerator of which is the number of all Shares held by such Owner and the denominator of which is the sum of all Shares held by all Owners. See Section 2.1(17) of the Operating Agreement.

the Operating Agreement to the contrary, so long as CBSX is a facility of CBOE, in the event that CBOE, in its sole discretion, determines that any action, transaction or aspect of an action or transaction, is necessary or appropriate for, or interferes with, the performance or fulfillment of CBOE's regulatory functions, its responsibilities under the Act or as specifically required by the SEC (collectively, "Regulatory Requirements"), (i) CBOE's affirmative vote will be required to be included in order to constitute a "Super Majority Vote of the Owners,"<sup>12</sup> (ii) without CBOE's affirmative vote no such action, transaction or aspect of an action or transaction shall be authorized, undertaken or effective, and (iii) CBOE shall have the sole and exclusive right to direct that any such required, necessary or appropriate act, as it may determine in its sole discretion, to be taken or transaction be undertaken by or on behalf of CBSX LLC without regard to the vote, act or failure to vote or act by any other party in any capacity.

Section 5.6 of the Operating Agreement states that except as otherwise specifically provided by the Operating Agreement or required by the DLLCA or by the SEC pursuant to the Act, no Owner shall have the power to act for or on behalf of, or to bind, CBSX LLC.

Section 5.7 of the Operating Agreement provides that CBSX LLC, and to the extent that it relates to CBSX LLC, each Owner, agrees to comply with the federal securities laws and the rules and regulations thereunder; to cooperate with the SEC and CBOE pursuant to their regulatory authority and the provisions of the Operating Agreement; and to engage in conduct that fosters and does not interfere with CBSX LLC's ability to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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.

<sup>12</sup> "Super Majority Vote of the Owners" means, subject to the provisions of Section 1.8 of the Operating Agreement as to Regulatory Requirements, the affirmative vote of both (i) all of the Owners of the Series A Voting Shares at the time, and (ii) any two (2) of the Initial Owners of Series B Voting Shares who then retain ownership of Series B Voting Shares. See Section 2.1(25) of the Operating Agreement.

Additionally, Section 5.7 of the Operating Agreement states that, after appropriate notice and opportunity for hearing, the Board, with the approving vote of both CBOE, in exercise of its authority under Section 1.8 of the Operating Agreement, and a majority vote of the Owners, excluding the vote of the Owner subject to sanction, may suspend or terminate an Owner's voting privileges or membership in CBSX LLC under the Operating Agreement: (i) In the event such Owner is subject to a "statutory disqualification," as defined in Section 3(a)(39) of the Act; or (ii) in the event such Owner has violated any provision of the Operating Agreement implicating any federal or state securities law; or (iii) if the Board determines that such action is necessary or appropriate in the public interest or for the protection of investors.

Section 9.13 of the Operating Agreement also provides that a Director may be removed for cause by the act of a "Majority in Interest of the Owners"<sup>13</sup> at a meeting of the Owners called expressly for the purpose of removing the Director. For these purposes, "for cause" shall mean: (1) The Director has (A) committed a willful serious act of dishonesty, such as fraud, embezzlement or theft, (B) committed or attempted any act against CBSX LLC intending to enrich himself or herself at the expense of CBSX LLC, or (C) made an unauthorized use or disclosure of "Confidential Information;"<sup>14</sup> (2) the Director has been charged with an act constituting a felony; (3) the Director has engaged in conduct that has caused serious injury, monetary or otherwise, to

<sup>13</sup> "Majority in Interest of the Owners" means the affirmative vote of more than 50% of the Voting Shares held solely by the Voting Owners. See Section 2.1(12) of the Operating Agreement.

<sup>14</sup> "Confidential Information" means (A) information relating to the terms of any contract, agreement or other relationship between CBSX LLC and a third party, an Owner, an Affiliate of CBSX LLC or an Owner, or any other person, (B) information relating to the terms of the Operating Agreement or any other agreement between or among CBSX LLC, and an Owner, an Affiliate of CBSX LLC or an Owner, or any other person (C) financial information about CBSX LLC, an Owner, an Affiliate of CBSX LLC or an Owner, (D) any process, system or procedure with which or whereby CBSX LLC or any Owner or Affiliate of an Owner does business, (E) any trade secrets, confidential know-how or designs, formulae, plans, devices, business information, software, systems, technology, financial data or material (whether or not patented or patentable) of CBSX LLC, or an Owner or Affiliate of CBSX LLC or an Owner, and (F) any confidential member or user or customer lists of CBSX LLC, or an Owner or Affiliate of CBSX LLC or an Owner, in each case to which a party hereto becomes privy or learns of by reason of the Operating Agreement, discussions or negotiations relating to the Operating Agreement or the relationship of the parties contemplated hereby. See Section 2.1(6), and Section 15.2 of the Operating Agreement.

CBSX LLC; or (4) the Director, in carrying out his or her duties, has been guilty of negligence or willful misconduct.

Under Section 9.14 of the Operating Agreement, the Board of Directors may designate one or more committees, which shall be comprised of individuals chosen by the Board, and may at the Board's discretion include non-Board members. Any such committee, to the extent provided in the resolution, shall have the authority and power to exercise such functions as may be delegated by the Board, which delegation may be revoked by the Board at any time in its discretion and any action taken pursuant to such delegation may be modified, suspended, overruled or revoked by the Board at any time in its discretion.

Section 9.15(a) of the Operating Agreement contains limitations on the authority of the Board of Directors. Specifically, Section 9.15(a) of the Operating Agreement provides that notwithstanding any contrary provision of this Agreement, and subject always to CBOE's rights to act under Section 1.8 of the Operating Agreement and the final provision of Section 9.15(a) of the Operating Agreement, it shall require the affirmative action of the Board, acting on behalf of CBSX LLC, the additional prior approving vote of CBOE, in exercise of its authority under Section 1.8 of the Operating Agreement, and a Super Majority of the Owners, to cause CBSX LLC to:

- Enter into a material new line of business or exit or change a material line of business outside the scope of the business contemplated in Section 1.6 of the Operating Agreement;
- Enter into any transaction with an Owner or Affiliate<sup>15</sup> of an Owner outside the ordinary course of business or requiring payments in excess of \$1 million;
- Make any material amendment to the organizational documents of CBSX LLC;
- Engage in any liquidation, dissolution, reorganization or recapitalization;
- Enter into licensing or other contractual arrangements, including without limitation, those providing for the encumbrance of assets or properties,

<sup>15</sup> "Affiliate" means with respect to any person, any other person that directly, or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such person. As used in this definition, the term "control" means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract or otherwise with respect to such person. See Section 2.1(1) of the Operating Agreement.

outside the ordinary course of business, or requiring payments in excess of \$1 million;

- Grant Board seats to new Owners or alter Board seat allocations for or among existing Owners (which action will require compliance with the rule filing process of Section 19 of the Act as well);

- Issue additional equity securities of CBSX LLC or securities convertible into equity securities of CBSX LLC, other than as provided for in Section 3.2(c) and (d) of the Operating Agreement;

- Declare or pay dividends or distributions, or repurchase any securities of CBSX LLC (other than Series C Non-Voting Restricted Shares), other than those that apply proportionately to all Owners;

- Enter into any merger, consolidation or acquisition or sale of material assets or ownership interests;

- Undertake an initial public offering;
- Change senior level management, including entering into, terminating or amending employment agreements with management and key employees;

- Materially change CBSX LLC's business model;

- Change auditors or accounting policies, practices or procedures;

- Change the status or registration of CBSX LLC as a facility of CBOE (which action will require compliance with the rule filing process of Section 19 of the Act as well);

- Create or designate any new or additional class or series of Shares or increase the authorized number of Shares of any class or series;

- Approve or authorize the acquisition by any person or group of a greater than 20% Percentage Interest in CBSX LLC (which action will require compliance with Section 6.14 of the Operating Agreement as well); or

- Amend, or be bound by or recognize an amendment of, the provisions of Section 9.15(a) of the Operating Agreement in any way.

Section 9.15(a) of the Operating Agreement further provides that without the affirmative vote of CBOE if exercised under Section 1.8 of the Operating Agreement, no such action, transaction or aspect of an action or transaction shall be authorized, undertaken or effective. Additionally, with respect to any matter, including those listed above, that implicates Regulatory Requirements, CBOE shall always have the sole discretion and authority to cause any action to be taken by and on behalf of CBSX LLC, as provided for in Section 1.8 of the Operating Agreement, without regard to the foregoing requirements of Section 9.15(a) of the Operating Agreement.

CBOE believes that the foregoing limitations on the authority of the CBSX LLC Board enable CBOE to have authority over the actions of CBSX LLC especially as they relate to regulatory responsibilities.

Under Section 9.15(c) of the Operating Agreement, each Director shall agree to comply with the federal securities laws and the rules and regulations thereunder, and to cooperate with the SEC and CBOE pursuant to their regulatory authority and the provisions of the Operating Agreement. In addition, each Director will take into consideration whether any actions taken or proposed to be taken as a Director for or on behalf of CBSX LLC, or any failure or refusal to act (including a failure to be present to constitute a quorum, or to reasonably provide an affirmative vote or consent) would constitute interference with CBOE's regulatory functions and responsibilities in violation of the Operating Agreement or the Act. Interference shall be determined reasonably and in good faith by the Board designees of CBOE, which determination will be final and binding.

Section 9.16 of the Operating Agreement also provides that in serving as a Director, each Director agrees to comply with the federal securities laws and the rules and regulations thereunder; to cooperate with the SEC and CBOE pursuant to their regulatory authority and the provisions of the Operating Agreement; and to engage in conduct that fosters and does not interfere with CBSX LLC's ability to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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.

Moreover, after appropriate notice and opportunity for hearing, the Board, with the approving vote of both CBOE in exercise of its authority under Section 1.8 of the Operating Agreement, and a majority vote of the Owners, excluding the vote of the Owner whose Director designee is subject to sanction, may suspend or terminate a Director's service as such to CBSX LLC under the Operating Agreement: (i) In the event such Director is subject to a "statutory disqualification," as defined in Section 3(a)(39) of the Act; or (ii) in the event such Director has violated any provision of the Operating Agreement implicating any federal or state securities law; or

(iii) if the Board determines that such action is necessary or appropriate in the public interest or for the protection of investors.

CBOE believes that these provisions, including Sections 5.7, 9.15(c) and 9.16 of the Operating Agreement, would require each CBSX LLC Director to adhere to regulatory responsibilities in that they must comply with federal securities laws and the rules and regulations promulgated thereunder, and cooperate with the SEC and CBOE pursuant to their regulatory authority.

#### *Changes in Ownership of CBSX LLC*

Pursuant to Section 6.1 of the Operating Agreement, an Owner shall have the right to assign Shares only by a written assignment, the terms of which do not contravene any provision of this Operating Agreement, and which has been duly executed by the assignor and assignee, received by the Board, and recorded on the books of CBSX LLC. For all purposes of the Operating Agreement, the terms "transfer" and "assign," and all derivatives or variants of those terms, include any transfer, disposition, sale, gift, bequest, pledge, encumbrance, hypothecation, exchange or other act whether voluntary or involuntary, by operation of law or otherwise, whereby an Owner's ownership, interest, or rights in any Shares are disposed of, impaired, or in any way affected.

Section 6.2 of the Operating Agreement states that, subject to the requirements of Article VI of the Operating Agreement, an Owner can assign any portion of its shares to a "Permitted Transferee." A "Permitted Transferee" means (i) as to any Owner, an Affiliate of such Owner, and not the Affiliate of any other Owner, (ii) as to VDM Chicago, LLC during the period specified in the Operating Agreement, Mill Bridge IV, LLC or CBONP, LLC,<sup>16</sup> or (iii) as to any Owner that is an individual (A) such Owner's estate, heirs or beneficiaries, (B) any guardian or conservator appointed for such Owner's estate, or (C) any trust for the benefit of such Owner or such Owner's immediate family members, or to any limited partnership or limited liability company in which the non-controlling partners or members, as the case may be, are members of such Owner's immediate family, and so long as the Owner is the sole trustee, general partner or manager of such trust, limited

<sup>16</sup> Prior to SEC approval of this rule filing, VDM Chicago Holdings, LLC, Mill Bridge IV, LLC, and CBONP, LLC will execute an Indirect Controlling Party Amendment to the Operating Agreement, pursuant to Section 15.16 of the Operating Agreement.

partnership or limited liability company, as the case may be. A Permitted Transferee shall become a Substituted Owner only if and as provided in Sections 6.4 and 6.5 of the Operating Agreement.

Section 6.3 of the Operating Agreement further provides that no Owner may sell, assign, give, pledge, or otherwise voluntarily transfer, or involuntarily transfer by bankruptcy, death or disability, shares to a person other than a Permitted Transferee, and no shares shall be transferred on the books of CBSX LLC other than a transfer to a Permitted Transferee, unless prior to that transfer, an Owner, or, in the case of an involuntary transfer, the legal representative or successor in interest of an Owner (the "Transferring Owner"), first notifies CBSX LLC and all voting Owners (but not Management Owners) in writing of the number of shares that the Transferring Owner proposes to transfer pursuant to a bona fide offer received by the Transferring Owner, and otherwise complies with restrictions and conditions in Article VI pertaining to sale and transfer of shares.

Under Section 6.4 of the Operating Agreement, a Permitted Transferee and a transferee having purchased Shares after the Transferring Owner has complied with the right of first refusal set forth in Section 6.3(a) and (b) of the Operating Agreement, shall become a Substituted Owner,<sup>17</sup> provided that (i) the Permitted Transferee or other transferee executes a written acceptance and adoption of all terms and provisions of the Operating Agreement, as the same may have been amended, and (ii) all of the applicable requirements of a change of ownership notice to the SEC as required by Section 6.13 of the Operating Agreement, or a proposed rule change subject to the requirements of the rule filing process of Section 19 of the Act as required by Section 6.14 of the Operating Agreement have been accomplished and, if necessary, approved by the SEC.

Section 6.7 of the Operating Agreement provides that no transfer or assignment of any shares may be made if, in the written opinion of counsel for CBSX LLC: (1) Such transfer or assignment, together with all other

transfers and assignments of shares within the preceding twelve months, would result in a termination of CBSX LLC for purposes of Internal Revenue Code § 708 or any comparable provision then in effect; (2) such transfer or assignment would violate the Securities Act of 1933, as amended, or applicable state securities or Blue Sky laws, or any other applicable provision of law in any respect; or (3) such transfer or assignment would cause CBSX LLC to be treated as an association taxable as a corporation rather than as a partnership for federal, state or local income tax purposes.

#### *Ownership/Voting Limitations*

Section 6.12 of the Operating Agreement contains ownership concentration limitations. Specifically, Section 6.12(a) of the Operating Agreement provides that no person (other than CBOE), either alone or together with its Affiliates, at any time, may be an Owner, directly or indirectly, of record or beneficially, of an aggregate amount of Shares that would result in a greater than twenty percent (20%) Percentage Interest in CBSX LLC (the "Concentration Limitation"). Section 6.12(b) of the Operating Agreement states that the Concentration Limitation shall apply to each person (other than CBOE) unless and until: (i) Such person shall have delivered to the Board a notice in writing, not less than 45 days (or such shorter period as the Board shall expressly consent to) prior to the acquisition of any Shares that would cause such person (either alone or together with its Affiliates) to exceed the Concentration Limitation, of such person's intention to acquire such ownership; (ii) the Board shall have, in its sole discretion, consented to expressly permit such ownership; and (iii) such waiver shall have been filed with, and approved by, the SEC under Section 19(b) of the Act and shall have become effective thereunder. Section 6.12(c) of the Operating Agreement states that in exercising its discretion under Section 6.12(b) of the Operating Agreement, the Board shall have determined that (i) such beneficial ownership of Shares by such person, either alone or together with its Affiliates, will not impair the ability of CBSX LLC and the Board to carry out their functions and responsibilities, including but not limited to, under the Act, and is otherwise in the best interests of CBSX LLC and its Owners; (ii) such beneficial ownership of Shares by such person, either alone or together with its Affiliates, will not impair the ability of the SEC to enforce the Act; (iii) neither such person nor its Affiliates are

subject to any applicable "statutory disqualification" (within the meaning of Section 3(a)(39) of the Act); and (iv) neither such person nor its Affiliates is a member of CBOE.

Section 6.13 of the Operating Agreement provides that beginning after SEC approval of this proposed rule change, CBSX LLC shall provide the SEC with written notice ten days prior to the closing date of any transaction that results in a person's Percentage Interest, alone or together with any Affiliate, meeting or crossing the threshold level of 5% or the successive 5% Percentage Interest levels of 10% and 15%.

Section 6.14 of the Operating Agreement provides that beginning after SEC approval of this proposed rule change, in addition to the notice requirement in Section 6.13 of the Operating Agreement, (i) any transfer that results in the acquisition and holding by any person, alone or together with any Affiliate, of an aggregate Percentage Interest level permitted by Section 6.12 of the Operating Agreement that meets or crosses the threshold level of 20% or any successive 5% Percentage Interest level (i.e., 25%, 30%, etc.); and (ii) any transfer of Series A Voting Shares to a Permitted Transferee of CBOE or any of its Affiliates, will constitute a proposed rule change that will be subject to the requirements of the rule filing process of Section 19 of the Act, subject to approval by the SEC, and CBSX LLC shall make all necessary filings with the SEC thereunder.

Under Section 8.10 of the Operating Agreement, in the event that, despite the Concentration Limitation prohibitions of Section 6.12 of the Operating Agreement, an Owner of Series B Voting Shares that is also a CBOE member owns more than 20% of the outstanding Voting Shares, alone or together with any Affiliate of such Owner (Shares owned in excess of 20% being referred to as "Excess Shares"), the Owner and its designated Directors shall have no voting rights whatsoever, nor right to give any proxy in relation to a vote of the Owner, with respect to the Excess Shares held by such Owner. However, irrespective of whether such Owner or its designated Directors otherwise participate in a meeting in person or by proxy, such Owner's Excess Shares shall be counted for quorum purposes, and shall be counted as being voted on each matter in the same proportions as the Voting Shares held by the other Owners are voted (including any abstentions from voting).

CBOE believes that these provisions will prevent any person from exercising undue control over CBSX LLC and will

<sup>17</sup> "Substituted Owner" is a person admitted to all of the rights, and except as provided in the following sentence, who assumes all of the obligations, of an Owner who has made an assignment of shares in accordance with Section 6.4 of the Operating Agreement. Such obligations shall not include any obligation of the assignor to return to CBSX LLC or pay to a creditor, in accordance with Section 3.4 of the Operating Agreement, all or any part of a distribution that previously was made to the assignor. See Section 6.5 of the Operating Agreement.

protect the ability of CBOE, as well as other investors, to exercise its full ownership rights. By specifically imposing a voting limitation on any person other than CBOE that owns shares which represent in the aggregate more than 20% of the voting power then entitled to be cast, CBOE is ensuring that it is in all cases, able to maintain proper control over the exercise of its regulatory function in relation to CBSX LLC, and is not subject to influence that may be adverse to its regulatory responsibilities from any person who may own a substantial number of the outstanding shares. This provision and other related provisions relating to notice and rule filing requirements with respect to any person who acquires certain Percentage Interest levels in CBSX LLC will serve to protect the integrity of CBOE's self-regulatory responsibilities.

#### *Regulatory Jurisdiction Over CBSX LLC and Its Owners*

As noted earlier, CBOE will regulate CBSX as a facility of the Exchange. CBOE has responsibility under the Act for the CBSX facility. CBSX LLC, as owner and operator of the CBSX facility, will also be subject to the SEC's jurisdiction. In this regard, Section 6.15(a) of the Operating Agreement provides that the Owners acknowledge that to the extent they are directly related to CBSX LLC's activities, the books, records, premises, officers, directors, agents, and employees of the Owners shall be deemed to be the books, records, premises, officers, directors, agents, and employees of the Regulatory Services Provider<sup>18</sup> and its Affiliates for the purpose of and subject to oversight pursuant to the Act. Section 6.15(b) of the Operating Agreement additionally provides that the books, records, premises, officers, directors, agents, and employees of CBSX LLC shall be deemed to be the books, records, premises, officers, directors, agents, and employees of CBOE for the purpose of and subject to oversight pursuant to the Act.

Under Section 6.15(c) of the Operating Agreement, CBSX LLC, the Owners and the respective officers, directors, agents, and employees of each irrevocably submit to the jurisdiction of the U.S. federal courts, the SEC, and CBOE, for the purposes of any suit, action or proceeding pursuant to U.S. federal securities laws or the rules or regulations thereunder, directly arising

<sup>18</sup> "Regulatory Services Provider" means CBOE for the term of the regulatory services to be provided under the Services Agreement. See Section 2.1(22) of the Operating Agreement.

out of, or directly relating to, CBSX LLC's activities, and hereby waive, and agree not to assert by way of motion, as a defense or otherwise in any such suit, action or proceeding, any claims that they are not personally subject to the jurisdiction of the U.S. federal courts, SEC, or CBOE, that the suit, action or proceeding is an inconvenient forum or that the venue of the suit, action or proceeding is improper, or that the subject matter thereof may not be enforced in or by such courts or agency, and, to the fullest extent permitted by law, waive the defense or application of any foreign secrecy or blocking statutes or regulations with respect to the Owner, its officers, directors, agents and employees, that relate to CBSX LLC's activities or their participation therein or in connection therewith.

Section 6.15(d) of the Operating Agreement states that CBSX LLC and each Owner shall take such action as is necessary, unless otherwise provided for by law, written statement of policy, individual contract or otherwise, to ensure that the officers, directors, agents and employees of each consent in writing to the applicability of this provision with respect to CBSX LLC-related activities. Consent in writing to the provisions of this Section 6.15(d) of the Operating Agreement extends to the confidentiality provisions in Section 15.2 of the Operating Agreement.

Section 13.2 of the Operating Agreement provides, in part, that CBSX LLC's complete records and books of account shall be subject at all times to inspection and examination by CBOE and the SEC at no additional charge to CBOE and the SEC.

CBOE believes that these provisions will serve as notice to Owners that they will be subject to the jurisdiction of the U.S. federal courts, the SEC, and CBOE. It is important that regulatory cooperation is assured from all Owners, regardless of the Owner's business location, country of domicile or other circumstances which the SEC may deem to have the potential to be adverse to the regulatory responsibilities and interests of CBOE, the SEC or the U.S. federal courts.

Finally, Section 15.2 of the Operating Agreement generally provides that no Owner shall disclose any "Confidential Information" to any person or use any confidential information to the detriment of CBSX LLC or its Owners or for its own benefit or the benefit of others, except with the consent of the Board or as required by law or as requested by any governmental or regulatory authority (provided that such Owner shall notify the Board promptly of any request for information before

disclosing it, if practicable and permitted by applicable law), and other than with respect to CBOE's communications with the SEC with respect to the conduct of CBSX LLC's business. Section 15.2 of the Operating Agreement further provides that nothing in the Operating Agreement shall be interpreted to limit or impede the rights of the SEC or CBOE to access and examine any Confidential Information pursuant to the U.S. federal securities laws and the rules thereunder, or to limit or impede the ability of an Owner or an officer, director, agent or employee of an Owner to disclose any Confidential Information to the SEC or CBOE.

#### *Proposed New Rule 3.32*

CBOE proposes to adopt a new Rule 3.32—Ownership Concentration and Affiliation Limitation, as requested by the SEC staff.<sup>19</sup> Paragraph (a) of Rule 3.32 sets forth the "Concentration Limitation" applicable to CBSX LLC, and specifically states that for as long as CBSX LLC operates as a facility of the Exchange, no member of the Exchange, either alone or together with its Affiliates, at any time, may own, directly or indirectly, of record or beneficially, an aggregate amount of Shares that would result in a greater than twenty percent (20%) Percentage Interest in CBSX LLC.<sup>20</sup> In the event a member inadvertently violates the "Concentration Limitation," Paragraph (c) of Rule 3.32 provides that the member shall have 180 days to cure the inadvertent violation. In the event the violation is not cured during such time, the member shall have all trading rights and privileges suspended on CBSX, and shall also be subject to any appropriate disciplinary action, including action for the failure of such member to enter into the CBSX LLC Operating Agreement.

Paragraph (b) of Rule 3.32 provides that without prior SEC approval, the Exchange or any entity with which it is affiliated shall not directly acquire or maintain an ownership interest in an Exchange member. In addition, without prior SEC approval, no Exchange member shall be or become affiliated with (i) the Exchange or (ii) any affiliate of the Exchange. Paragraph (b) of Rule 3.32 also states that nothing therein shall prohibit a member from acquiring or holding an equity interest in CBSX

<sup>19</sup> CBOE notes that Rule 3.32 is similar to ISE Rule 312, and Article 9 Section 12 of the Boston Stock Exchange Constitution.

<sup>20</sup> For purposes of this paragraph (a), and unless the context otherwise requires, the terms "Affiliate," "Share," and "Percentage Interest" shall have the same meaning specified in the CBSX LLC Operating Agreement.

LLC that is permitted by the "Concentration Limitation" or from being affiliated with OneChicago, LLC, provided that the Exchange's proportionate share of OneChicago, LLC's gross revenues does not exceed 5% of the Exchange's gross revenues.<sup>21</sup>

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act. Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5) Act<sup>22</sup> requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and, in general, to protect investors and the public interest.

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

CBOE 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.

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

No written comments were solicited or received with respect to the proposed rule change.

## 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 CBOE 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 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-CBOE-2006-110 on the subject line.

### Paper Comments

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

All submissions should refer to File Number SR-CBOE-2006-110. 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-CBOE-2006-110 and should be submitted on or before February 22, 2007.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>23</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

[FR Doc. E7-1595 Filed 1-31-07; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-55164; File No. SR FICC-2006-20]

### Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Modify the EPN Rules of its Mortgage-Backed Securities Division to Implement New Messaging Capabilities and Establish a Fee Structure

January 24, 2007.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on December 28, 2006, the Fixed Income Clearing Corporation ("FICC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change described in Items I, II, and III below, which items have been prepared primarily by FICC. FICC filed the proposed rule change pursuant to Section 19(b)(3)(A)(ii) and (iii) of the Act<sup>2</sup> and Rules 19b-4(f)(2) and 19b-4(f)(4) thereunder<sup>3</sup> so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested parties.

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

The purpose of the proposed rule change is to modify the Electronic Pool Notification ("EPN") rules of FICC's Mortgage-Backed Securities Division ("MBSD") to implement new messaging capabilities for participants using the EPN service and to establish a fee structure for the new messaging capabilities.<sup>4</sup>

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

In its filing with the Commission, FICC 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. FICC has prepared summaries, set forth in sections (A), (B),

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

<sup>2</sup> 15 U.S.C. 78s(b)(3)(A)(ii) and (iii).

<sup>3</sup> 17 CFR 240.19b-4(f)(2) and 240.19b-4(f)(4).

<sup>4</sup> The text of the proposed rule change is available at the FICC, at [http://www.ficc.com/commondocs/rule\\_filings/rule\\_filing\\_06-20.pdf](http://www.ficc.com/commondocs/rule_filings/rule_filing_06-20.pdf), and at the Commission's Public Reference Room.

<sup>21</sup> See Amendment No. 1. OneChicago, LLC is a joint venture of Interactive Brokers Group, LLC, CBOE, the Chicago Mercantile Exchange, and the Chicago Board of Trade. It is an electronic security futures exchange that trades futures on individual stocks, narrow-based indexes and ETFs.

<sup>22</sup> 15 U.S.C. 78f(b)(5).

<sup>23</sup> 17 CFR 200.30-3(a)(12).