

method to approach penny pricing in the options markets, rather than a mechanism that bypasses auction market principles.<sup>27</sup> As discussed above, with respect to the commenter's substantive arguments, the Commission believes the AAO functionality is consistent with the Act. Further, the Commission notes that the proposal, as amended, is intended to make it easier for Public Customers to participate in the PIP (or other future Improvement Auctions), which already allows trading in penny increments. In addition, pursuant to the amended proposal, AAOs may only be entered in series that are limited to quoting in standard increments greater than one cent. The Commission believes it is consistent with the Act to allow BSE to implement another initiative designed to allow limited *trading* in penny increments at the same time it participates in the Penny Pilot Program.

#### D. Accelerated Approval

The Commission finds good cause to approve the proposal prior to the thirtieth day after the proposal was published for comment in the **Federal Register**. The proposed rule change, as modified by Amendment No. 1, was published for full notice and comment.<sup>28</sup> Amendment No. 2, which limits the AAO functionality to Public Customer accounts, and in a series for which the standard trading increment is greater than one cent, modifies the proposal in response to issues raised by a commenter. For these reasons, the Commission finds good cause, consistent with section 19(b)(2) of the Act, to grant accelerated approval to the proposed rule change.

#### V. Conclusion

*It is therefore ordered*, pursuant to section 19(b)(2) of the Act,<sup>29</sup> that the proposed rule change (SR-BSE-2006-56), as modified by Amendments No. 1 and 2, be, and it hereby is, approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>30</sup>

**Florence E. Harmon,**  
Deputy Secretary.

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<sup>27</sup> See ISE Letter, *supra* note 4, at 3.

<sup>28</sup> See Notice, *supra* note 3.

<sup>29</sup> 15 U.S.C. 78s(b)(2).

<sup>30</sup> 17 CFR 200.30-3(a)(12).

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-56185; File No. SR-BSE-2007-39]

### Self-Regulatory Organizations; Boston Stock Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Clarify How the BOX Trading Host Systematically Filters All Orders Against the National Best Bid and Offer

August 2, 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 July 30, 2007, the Boston Stock Exchange, Inc. ("Exchange" or "BSE") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been substantially prepared by the Exchange. The Exchange has designated the proposed rule change as a non-controversial rule change pursuant to section 19(b)(3)(A)(iii) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposed rule change effective upon filing with the Commission. 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 amend the rules of the Boston Options Exchange ("BOX") to clarify how the BOX Trading Host systematically filters all orders against the National Best Bid and Offer ("NBBO") to ensure that a trade-through to the detriment of the inbound order does not occur, and that the customer's interests are protected by making sure that any execution of its order on BOX is at a price at least as good as the best price available on any of the other options exchanges. The proposed rule filing also seeks to clarify how BOX currently processes such orders when the NBBO is either locked or crossed. The text of the proposed rule change is set forth below; new text is in *italics* and deleted text is in brackets.

<sup>1</sup> 17 CFR 200.30-3(a)(12).

<sup>2</sup> 15 U.S.C. 78s(b)(1).

<sup>3</sup> 17 CFR 240.19b-4.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

## RULES OF THE BOSTON OPTIONS EXCHANGE FACILITY

### Chapter V

#### Sec. 16 Execution and Price/Time Priority

(a)—No change.

(b) Filtering of BOX In-Bound Orders [to Prevent Trade-Throughs].

i. *With the exception of Improvement Orders and Primary Improvement Orders submitted during a PIP (which are processed in accordance with section 18 of this Chapter V) and Directed Orders (which are processed in accordance with section 5, subsections b and c, of Chapter VI) [A]ll inbound orders to BOX (whether on behalf of Customers, non-BOX Participant broker-dealer proprietary accounts or market makers at other exchanges) as well as inbound Principal ("P") and Principal as Agent ("P/A") (see Chapter XII, "Intermarket Linkage Rules", herein) orders received via InterMarket Linkage will be filtered by the Trading Host prior to entry on the BOX Book to ensure that these orders will not [execute at price outside the current NBBO ("trade-throughs")].:*

*1) in the case of a sell order, execute at a price below the NBBO bid price*  
*-or-*

*2) in the case of a buy order, execute at a price above the NBBO offer price.*

*All of the filtering rules described in this section are independent of whether the NBBO is locked or crossed or not, except where the BOX best price on the same side of the market as the inbound order has crossed, or is crossed by, the opposite side NBBO, the order will be routed, if eligible, or rejected immediately.*

ii.-iv.—No change.

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

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

**1. Purpose**

The purpose of the proposed rule change is to amend the BOX Rules to describe how the BOX Trading Host systematically filters all orders against the NBBO to ensure that a trade-through to the detriment of the inbound order does not occur. The proposal also describes how customers' interests are protected by making sure that any execution of his order on BOX is at a price at least as good as the best price available on any of the other options exchanges.

BOX's responsibility to the inbound customer or broker-dealer order is to ensure that its execution is at the best price available across all markets at that moment. Presently, BOX processes trades irrespective of whether the NBBO is locked, crossed, or "normal." As a result of this practice, there is the potential to cause a trade-through. The purpose of this rule filing is to amend the BOX rules to recognize that only the price on the side of the NBBO opposite to the inbound order needs to be taken into account when filtering inbound orders, regardless of whether the NBBO is locked, crossed, or "normal," and regardless of whether BOX is presently part of the NBBO on the opposite side from the order. The Exchange has obtained exemptive relief for any trade-throughs that occur as a result of this practice.<sup>5</sup>

The following examples illustrate BOX's proposed processing of NBBO filtering:

*Example 1:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.00 .....	2.10
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order executed at 2.00 on BOX.		

*Example 2:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.00 .....	2.10

current rule requirement for separate firms. Such policies and procedures must, at a minimum, include information barriers that prevent the flow of non-public information between a member organization's ETF specialist on the one hand and the member organization's specialist in an associated

	Bid	Offer
BOX Trading Host receives an order to sell 20 "at market."		
Inbound sell order executed for 10 at 2.00 on BOX. The remaining ten are exposed <sup>6</sup> internally at 2.00 and, if not executed, will be routed to the exchange disseminating the best price or rejected to sender.		

*Example 3:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.05 .....	2.10
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order exposed internally at 2.05 on BOX; and if not executed, will be routed to the exchange disseminating the best price or rejected to sender.		

*Example 4:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.00 .....	2.00
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order executed at 2.00 on BOX since this is best price available nationally for a seller.		

*Example 5:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.05 .....	2.05
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order exposed internally at 2.05 on BOX; and if not executed, will be routed to the exchange disseminating the best price or rejected to sender.		

*Example 6:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.00 .....	1.95
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order executed at 2.00 on BOX since this is best price available nationally for a seller.		

*Example 7:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.00 .....	1.95

	Bid	Offer
BOX Trading Host receives an order to sell 20 "at market."		
Inbound sell order executed for 10 at 2.00 on BOX since this is best price available nationally for a seller. The remaining 10 are exposed internally at 2.00, and if not executed, will be routed to the exchange disseminating the best price or rejected to sender.		

*Example 8:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.05 .....	1.95
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order exposed internally at 2.05 on BOX; if not executed, will be routed to the exchange disseminating the best price or rejected to sender.		

In the following example (Example 9), the BOX best price on the same side of the market as the inbound order is crossed by the opposite side NBBO. In this particular case, it is impractical to expose the inbound executable order at the opposite NBBO as in the previous examples since BOX is already showing a better offer (of 2.10 versus the NBBO exposure price of 2.15) with which nobody has traded.

In this unique circumstance (where the same side BBO on BOX is crossed by the opposite side NBBO), BOX will immediately route the order to the exchange disseminating the best price, if possible, or reject the order back to the sender.

*Example 9:*

	Bid	Offer
BOX .....	10 @ 2.00 .....	20 @ 2.10
NBBO .....	2.15 .....	2.05
BOX Trading Host receives an order to sell 10 "at market."		
Inbound sell order routed immediately to the exchange disseminating the best price at 2.15 or rejected back to sender.		

As illustrated by the above examples, the BOX NBBO filtering process ensures that a sell order is never executed on BOX at a price inferior to the best bid available at the other options exchanges; similarly, any order to buy an option would not be executed on BOX at price worse than the best offer available elsewhere at that moment. BOX believes that in the case of a crossed NBBO, it is in the inbound customer order's interest to execute at the best price on the opposite side of the NBBO on BOX, where possible, as this is much quicker than routing to an away exchange.

In connection with proposed rule change, the Exchange has respectfully

requested an exemption, pursuant to Rule 608(e) of Regulation NMS, from the requirement of Rule 608(c) of Regulation NMS that the Exchange comply with and enforce compliance by its members with the requirements of Section 8(c) of the Plan for the Purpose of Creating and Operating an Intermarket Options Linkage ("the Plan") in the limited circumstance where a trade-through occurs due to an execution when the NBBO is crossed by the disseminated market of another options exchange, or BOX's disseminated market crosses the NBBO, and BOX's price<sup>7</sup> on the opposite side of the market for the incoming order establishes, or is equal to, the NBBO. To the same extent and subject to the same limitations, the Exchange has requested exemptive relief from the requirement in Rule 608(c) of Regulation NMS that the Exchange comply with section 4(b) of the Plan by enforcing compliance by its members with the provisions of section 8(c) of the Plan. The Commission has granted the requested exemption.<sup>8</sup>

## 2. Statutory Basis

The Exchange believes that the proposal is consistent with the requirements of Section 6(b) of the Act<sup>9</sup> in general, and Section 6(b)(5) of the Act<sup>10</sup> in particular, in that it is designed to promote just and equitable principles of trade, to perfect the mechanism of a free and open market and the national market system, and to protect investors and the public interest by clarifying how the BOX Trading Host systematically filters all orders against the NBBO to ensure that a trade-through to the detriment of the inbound order does not occur.

### *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*

The Exchange has neither solicited nor received comments on the proposed rule change.

<sup>7</sup> BOX's price could be either BOX's disseminated price or it could be a Participant response to the exposure of the incoming order pursuant to Chapter V, Section 16(b) of BOX Rules. Therefore, an incoming order during a crossed market must execute at a price equal to the NBBO on the opposite side of the incoming order.

<sup>8</sup> See *supra* note 5.

<sup>9</sup> 15 U.S.C. 78f(b).

<sup>10</sup> 15 U.S.C. 78f(b)(5).

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

The Exchange has designated the proposed rule change as one that: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date of filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest. Therefore, the foregoing rule change has become effective pursuant to section 19(b)(3)(A) of the Act<sup>11</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>12</sup> The Exchange has asked the Commission to waive the operative delay to permit the proposed rule change to become operative prior to the 30th day after filing so that the Exchange can clarify the conditions under which BOX provides automatic executions during times of crossed markets, thus allowing the maximum potential number of orders to be handled electronically on the Exchange.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest.<sup>13</sup> Waiving the delay will allow the Exchange's clarifications of the operation of the BOX Trading Host's filtering of orders against the NBBO to become operative immediately. Waiving the delay will also allow the proposal to become operative simultaneously with the trade-through exemption granted to the Exchange as of July 30, 2007,<sup>14</sup> the date the proposed rule change was filed. Therefore, the Commission designates the proposal operative upon filing.

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate the rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

## **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*. Please include File No. SR-BSE-2007-39 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-BSE-2007-39. 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, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such 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-BSE-2007-39 and should be submitted on or before August 29, 2007.

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>12</sup> 17 CFR 240.19b-4(f)(6). As required under Rule 19b-4(f)(6)(iii), the Exchange provided the Commission with written notice of its intent to file the proposed rule change at least five business days before doing so.

<sup>13</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>14</sup> See *supra* note 5.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

**Florence E. Harmon,**  
*Deputy Secretary.*

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**BILLING CODE 8010-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-56182; File No. SR-FICC-2006-19]

### Self-Regulatory Organizations; Fixed Income Clearing Corporation; Order Granting Approval of Proposed Rule Change Relating to Membership, Definitions, and the Electronic Pool Notification Service

August 1, 2007.

#### I. Introduction

On December 13, 2006, the Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) a proposed rule change 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> to restructure FICC’s Government Securities Division’s (“GSD”) membership standards and membership requirements, update various definitions, and make technical changes to GSD’s rules and to FICC’s Mortgage-Backed Securities Division’s (“MBSD”) Electronic Pool Notification (“EPN”) rules. The proposed rule change was published for comment in the **Federal Register** on March 29, 2007.<sup>3</sup> No comment letters were received on the proposal. This order approves the proposal.

#### II. Description of the Proposal

##### A. Membership Rules

FICC is revising its rules concerning membership types, the membership application process, and the ongoing requirements of GSD members into a format that FICC believes will make such rules easier to locate and to understand by applicants and members. To accomplish this, FICC is amending current Rule 2 (retitled “Members”), is moving much of the content of current Rule 2 into a new Rule 2A (“Initial Membership Requirements”), and is revising Rule 3 (retitled “Ongoing Membership Requirements”). Other rules and provisions are being modified

to make technical corrections where necessary and to be in harmony with analogous rules of FICC’s affiliated clearing agency, the National Securities Clearing Corporation (“NSCC”).

##### 1. Membership Types

FICC’s current Rule 2 (“Comparison-Only and Netting Members”) sets forth the types of GSD memberships, eligibility requirements, application procedures, and member reporting requirements. FICC is revising Rule 2 to establish each GSD membership type: Comparison-Only Members, Netting Members, Sponsoring Members, Sponsored Members, and Funds-Only Settling Bank Members. Substantially all other provisions contained in the current Rule 2 are being moved to either new Rule 2A or revised Rule 3.

One exception to this is that FICC is deleting current Rule 2, Section 4 (“Financial Reports by Netting Applicants”). FICC states that the rationale for such deletion is that FICC already advises applicants during the application process of the required financial reports depending on the category of membership for which is being applied and on the applicant entity type. In addition, FICC is setting forth in revised Rule 3 the financial reports that must be submitted by members to FICC on an ongoing basis.

FICC is also deleting section 1(f) of Rule 2, which provides that applicants that have been approved for membership must execute and deliver to FICC a membership agreement. This provision is redundant with existing Rule 2, Section 3, which will now appear in new Rule 2A, Section 7.

##### 2. Consolidation of Membership Standards and Requirements

Prior to this rule change, the membership qualifications, financial standards, and operational requirements for each membership type were set forth in Rule 2 (“Comparison-Only and Netting Members”), Rule 3 (“Financial Responsibility, Operational Capability and Other Membership Standards of Comparison-Only and Netting Members”), and Rule 4 (“Clearing Fund, Watch List and Loss Allocation”). To consolidate this information, FICC is creating a new Rule 2A (“Initial Membership Requirements”) that will establish the initial membership eligibility requirements for all membership types and will set forth the process of membership application and evaluation. In addition, FICC is restructuring Rule 3 (“Ongoing Membership Requirements”) to contain all current GSD rule provisions

regarding the continuing requirements of members.

The restructuring will encompass three substantive changes:

(a) *Immediate Placement on the Watch List.* FICC is deleting current Rule 3, Section 1(d)(iii) that automatically disqualifies an applicant from becoming a member if the applicant is subject to any action or condition, the existence of which would require the applicant to be placed on FICC’s Watch List if it were already a member. FICC believes that eliminating such provision will not diminish FICC’s ability to deny membership to an unworthy applicant because FICC will still retain under other sections of its rules the discretion to deny membership based on the applicant’s underlying financial, operational, or character issues. Moreover, FICC’s credit risk matrix enables FICC to place such applicant directly on FICC’s watch list for closer monitoring.

##### (b) *Additional Reporting Requirements.*

FICC is adding new language to proposed Rule 3, Section 2 (“Reports by Netting Members”) that will require members to provide FICC with (i) reports from their independent auditors on internal controls [in revised Rule 3, Section 2(b)(ii)] and (ii) a copy of any letter granting an extension of time by a regulatory authority to a member with respect to the submission of a report [in revised Rule 3, Section 2(h), para. 2].

##### (c) *Annual Audited Financial Statements.*

FICC is removing the current requirement in Rule 2, Section 4(a) that audited annual financial statements submitted by netting members be “without qualification.” FICC believes that a qualification in an annual audited financial statement should not warrant automatic denial of membership because a qualification may not always be material. In addition, the event that triggered a qualification may have been corrected by the applicant or member by the time the applicant or member submits its financial statement for review by FICC. Going forward, FICC will analyze qualifications in GSD netting member financial statements on a case-by-case basis.

Other conforming and non-substantive changes are being made within the rules to accommodate this restructuring and to update cross-references where applicable.

<sup>15</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> Securities Exchange Act Release No. 55515 (Mar. 22, 2006), 72 FR 14839.