

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-52929; File No. SR-BSE-2005-56)

December 8, 2005

Self-Regulatory Organizations; Boston Stock Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto Relating to the Initial Listing and Maintenance to List Options on Certain Securities

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 November 30, 2005, the Boston Stock Exchange, Inc. (“Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. On December 6, 2005, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The Exchange filed the proposed rule change as a “non-controversial” rule change under Rule 19b-4(f)(6) under the Act,<sup>4</sup> which rendered the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Exchange proposes to amend Section 3 (Criteria for Underlying Securities) and Section 4 (Withdrawal of Approval of Underlying Securities) of Chapter IV of the Rules of the Boston Options Exchange (“BOX”). Below is the text of the proposed rule change. Proposed additions are underlined and proposed deletions are in [brackets].

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

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

<sup>3</sup> In Amendment No. 1, the Exchange made non-substantive changes to the text of the proposed rule change.

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

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Rules of the Boston Options Exchange Facility

CHAPTER IV. SECURITIES TRADED ON THE BOSTON OPTIONS EXCHANGE FACILITY

Sec. 3 Criteria for Underlying Securities

- (a) Underlying securities with respect to which put or call options contracts are approved for listing and trading on BOX must meet the following criteria:
  - i. The security must be registered with the SEC and be an “NMS stock” as defined in Rule 600 of Regulation NMS under the Exchange Act
    - [1] listed on a national securities exchange; or
    - 2) traded through the facilities of a national securities association and reported as a “national market system” (“NMS”) security as set forth in Rule 11Aa3-1 under the Exchange Act]; and
  - ii. the security shall be characterized by a substantial number of outstanding shares that are widely held and actively traded.

Subsections (b) through (j) No Change.

Sec. 4 Withdrawal of Approval of Underlying Securities

Subsection (a) No Change.

- (b) An underlying security will not be deemed to meet BOXR’s requirements for continued approval whenever any of the following occur:
  - i. through iv. No Change.
  - v. {Reserved}[The issuer has failed to make timely reports as required by applicable requirements of the Exchange Act or Rules thereunder, and

such failure has not been corrected within thirty (30) days after the date the report was due to be filed.]

- vi. The underlying security ceases to be an “NMS stock” as defined in Rule 600 of Regulation NMS under the Exchange Act. [The issue, in the case of an underlying security that is principally traded on a national securities exchange, is delisted from trading on that exchange and neither meets NMS criteria nor is traded through the facilities of a national securities association, or the issue, in the case of an underlying security that is principally traded through the facilities of a national securities association, is no longer designated as an NMS security.]
- vii. No Change.

Subsection (c) through (j) No Change.

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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 Exchange proposes to amend a BOX rule pertaining to the continued approval of securities that underlie options traded on the Exchange. Specifically, the Exchange proposes to

eliminate Section 4(b)(v) of Chapter IV of the BOX rules. Section 4(b)(v) of Chapter IV of the BOX rules sets forth various situations under which an underlying security previously approved for options trading will in usual circumstances be deemed to no longer meet Exchange requirements for the continuance of such approval. In such circumstances, Section 4(b)(v) of Chapter IV of the BOX rules provides that the Exchange will not open for trading any additional series of options in that class and may also limit any new opening transactions in those options series that have already be opened.

Currently, Section 4(b)(v) of Chapter IV of the BOX rules provides that an underlying security will no longer be approved for options trading on the Exchange when:

“(v) The issuer has failed to make timely reports as required by applicable requirements of the Exchange Act or Rules thereunder, and such failure has not been corrected within thirty (30) days after the date the report was due to be filed.”<sup>5</sup>

The Exchange proposes to eliminate this provision because it limits investors’ ability to use options to hedge existing equity positions in such securities, and it is not necessary in the context of the rest of Section 4(b) of Chapter IV of the BOX rules.

First, Section 4(b)(v) of Chapter IV of the BOX rules can and does impact investors’ interests by preventing them from using new options series to hedge positions they may hold in the underlying security of companies that fail to make timely reports required by the Act. The Exchange states that such a restriction is inconsistent with rules and regulations in the markets for the underlying securities because no similar trading restriction is placed upon the trading of the underlying security itself. Thus, Section 4(b)(v) of Chapter IV of the BOX rules only serves

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<sup>5</sup> Phrase “or Rules thereunder” added pursuant to telephone conference between Bill Meehan, Assistant Vice President, Exchange, and David L. Orlic, Attorney, Division of Market Regulation, Commission, on December 7, 2005.

to limit the abilities of shareholders in such companies who may wish to hedge their positions with new options series, at a time when the ability to hedge may be particularly important.

The Exchange believes that Section 4(b)(v) of Chapter IV of the BOX rules has outlived any usefulness and now serves to unnecessarily burden and confuse the investing public. This provision was appropriate when it was first implemented in or around 1976, when the listing and trading of standardized options was still in its infancy and information pertaining to public companies was not readily available to the general investing public. The Exchange believes that today's listed options market, however, is a mature one with investors who have access to a significant amount of real-time market information to assist them in making informed investment decisions, including information as to whether companies have timely filed reports as required by the Act, and if not, why not. Therefore, the Exchange states that there is no reason to limit investors' ability to trade in options classes, including new series within those classes, simply because a company is not timely in filing its reports. The Exchange further advises that this restriction is further misplaced, considering that investors are not similarly restricted from buying or selling shares of the underlying security in the equity markets.

Moreover, the Exchange believes that Section 4(b)(v) of Chapter IV of the BOX rules limits an investors' ability to hedge his underlying stock positions at a time when he may be in most need to protect his investment. The failure of a public company to comply with its reporting requirements under the Act could cause a significant movement in the price of that company's stock. Restricting the Exchange from opening new options series may leave investors without means to hedge their positions with options contracts at strike prices that more accurately reflect the contemporaneous price trends of the underlying stock.

Clearly, new options series on a security should not be permitted to be opened if the underlying security ceases to be an NMS stock. Typically, the Exchange becomes aware of issues that may impact the continued listing of a security well before that security is delisted from its primary market. Exchange staff routinely monitors daily press releases and informational releases disseminated by various entities, such as the primary listing market of a security and private news services, in an effort to monitor the activities and news items pertaining to the issuers of securities that underlie options traded on the Exchange.<sup>6</sup> In many cases, an issuer is given a substantial amount of time to cure this deficiency before the primary market actually delists the issuer's security. Many times, the issuer is able to comply without its security ever being delisted. During this period, BOX staff continually monitors the status of the issuer's compliance with its reporting requirements to determine whether the security may be delisted. Finally, the primary listing market typically issues a press release well in advance of delisting an issuer's security to give investors and other market participants adequate notice.

Given the availability of data and information relating to public issuers of securities in today's markets, and in light of the extensive amount of additional continued listing standards under Section 4(b) of Chapter IV of the BOX rules, the Exchange believes that waiting until a security is actually delisted by its primary market is the appropriate point at which to restrict the issuance of new options series in an options class. Accordingly, the Exchange hereby proposes to eliminate Section 4(b)(v) of Chapter IV of the BOX rules.

Additionally, as a matter of "housekeeping," the Exchange also proposes to clarify Section 3(a)(i) and Section (4)(b)(vi) of Chapter IV of the BOX rules, which govern the criteria for the initial and continued listing of options on a particular security, respectively. Both of these

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<sup>6</sup> This is consistent with Section 4(d) of Chapter IV of the BOX rules.

provisions include as part of their criteria a requirement that the underlying security must be a national market system security (“NMS security”). As part of the recently adopted Regulation NMS, among other things, the Commission revised the definition of an NMS security.<sup>7</sup> Specifically, Rule 600(b) under Regulation NMS defines an NMS security as “any security or class of securities for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan, or an effective national market system plan for reporting transactions in listed options.” As such, each of these Rules will be amended to reflect these new terms.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>8</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>9</sup> in particular, in that the elimination of Section 4(b)(v) of Chapter IV of the BOX rules will serve to remove impediments to and perfect the mechanism of a free and open market and a national market system and is designed to promote just and equitable principles of trade and to protect investors and the public interest.

### 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 written comments on the proposed rule change.

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<sup>7</sup> See Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005).

<sup>8</sup> 15 U.S.C. 78f(b).

<sup>9</sup> 15 U.S.C. 78f(b)(5).

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

Because the proposed rule change: (i) does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) by its terms, does not become operative for 30 days after the date of filing, or such shorter time as the Commission may designate, if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>10</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>11</sup>

The Exchange has requested that the Commission waive the five-day pre-filing notice requirement and the 30-day operative delay period for “non-controversial” proposals and make the proposed rule change effective and operative upon filing. The Commission believes that waiver of the five-day pre-filing notice and the 30-day operative delay is consistent with the protection of investors and the public interest because this filing does not raise any novel issues. For this reason, the Commission designates the proposal to be effective and operative upon filing with the Commission.<sup>12</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such 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 the furtherance of the purposes of the Act.

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<sup>10</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>11</sup> 17 CFR 240.19b-4(f)(6).

<sup>12</sup> For the purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule’s impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BSE-2005-56 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-BSE-2005-56. 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 Section, 100 F Street, NE, Washington, DC 20549. 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-2005-56 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

Jonathan G. Katz  
Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).