

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54332; File No. SR-CBOE-2006-70)

August 18, 2006

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of Proposed Rule Change to Adopt Rules Relating to Regulation NMS

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on August 18, 2006, the Chicago Board Options Exchange, Incorporated ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange submits this rule change filing to modify its rules relating to the trading of non-option securities to conform with Regulation NMS. The text of the proposed rule change is available from the Exchange's Web site (<http://www.cboe.com>), the Exchange's principal office, the Commission's Web site (<http://www.sec.gov>), and the Commission's Public Reference Room.

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

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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

CBOE anticipates migrating the trading of non-option securities on CBOE to CBOEdirect, the Exchange's screen-based trading platform. This migration is proposed in SR-CBOE-2004-21.³ Upon completion of the proposed migration, CBOE's platform for non-option securities would offer fully automated quotations that are accessible via automatic execution without regard to order size and that will never be posted "manually." Thus, unless execution of an order would cause an impermissible trade-through of another trading center, all marketable orders would automatically execute on the system against the Exchange quotation (which incorporates resting limit orders and interest from CBOE market-makers).

The purpose of this filing to amend the rules proposed in SR-CBOE-2004-21 to conform to certain requirements of Regulation NMS and to qualify as an automated trading center with protected quotations.⁴ In its release extending the compliance dates for Rules 610 and 611 of

³ See Securities Exchange Act Release No. 53112 (January 12, 2006), 71 FR 3579 (January 23, 2006).

⁴ The Commission notes that, at the time of filing of this proposal, it had taken no final action on SR-CBOE-2004-21. Therefore, the rules proposed in SR-CBOE-2004-21 have not yet been adopted by the Exchange, and the entire STOC ruleset is presented in Exhibit 5 to this filing as proposed rule text. However, in Exhibit 3 to this filing, the Exchange has provided a document that shows only the differences between the STOC rules as originally proposed in SR-CBOE-2004-21 and how they would be revised by the instant proposal.

Regulation NMS,⁵ the Commission established a "Specifications Date" of October 16, 2006, by which certain milestones must be achieved by trading centers to ensure that quotations may be deemed protected from trade-throughs by other trading centers. A major component of the milestones relate to adopting certain rules that are consistent with Regulation NMS. More specifically, trading centers are required to: (1) establish a framework for identifying (marking) quotations as automated or manual to meet the requirements of Rule 600(b)(4); (2) adopt an immediate-or-cancel order ("IOC") functionality that meets the requirements of Rule 600(b)(3); and (3) adopt an intermarket sweep order ("ISO") functionality that allows other industry participants to meet the requirements of Rule 600(b)(30). The proposed rules would modify CBOE's screen-based rules to specifically address these requirements as well as other matters relating to Regulation NMS.

As previously mentioned, all quotes on the system would be firm and available for immediate and automated execution at all times unless the execution would cause an impermissible trade-through. There would be no "manual" mode or quotes. Accordingly, CBOE's quotations would always be "automated" for purposes of Rule 600(b)(4). This is made clear in proposed Rule 52.13(a). If CBOE were to experience a technical failure, it would cease disseminating quotations (as opposed to disseminating "manual" quotations).

The Exchange also proposes to modify the definition and handling of IOC orders to make clear that IOC orders routed to CBOE would either be immediately executed (in part or in full) or canceled. Such orders would not be "held up" for manual processing or for potential price

⁵ Securities Exchange Act Release No. 53829 (May 18, 2006), 71 FR 30038 (May 24, 2006).

improvement above CBOE's disseminated quote. The revised definition, which sets forth the manner in which these orders will be handled, is contained in proposed Rule 51.8(g)(4).

To allow other industry participants to comply with the requirements of Rule 600(b)(30) of Regulation NMS, which explains the manner in which ISOs must be routed, the Exchange is proposing to adopt ISO functionality so that ISO orders routed to CBOE would be automatically executed without regard for better prices displayed by other trading centers. Proposed Rule 51.8(n) spells out the Exchange's definition of ISOs. The Exchange would also provide technical specifications on its Web site to allow other market participants to access CBOE's protected quotations and to transmit ISOs to CBOE. Thus, upon activation of the system, CBOE would receive and process IOC and ISO orders consistent with Regulation NMS before the actual applicable compliance dates are reached.

The proposed rules also would incorporate additional language relating to Regulation NMS but that may not be a necessary component of the Specifications Date deadline. More specifically, the Exchange is proposing to add language providing that: (1) members should reasonably avoid displaying quotations that lock or cross protected quotations from other trading centers; (2) the Exchange may avail itself of the "self-help" exception contained in Rule 611(b)(8) of Regulation NMS; and (3) when sufficient functionality is available on CBOE, that the Exchange would route orders to trading centers displaying better-priced protected quotations on behalf of orders routed to CBOE using "private front-door" connectivity as opposed to via the ITS Plan or any successor to the ITS Plan.⁶ This "Routing Service" would be provided directly

⁶ Prior to that time, however, CBOE would access better priced quotes through the ITS Plan (or its successor). By way of example, if CBOE receives a market order to sell 1000

and automatically by CBOE pursuant to several contractual agreements referenced in proposed Rule 52.10.

The Exchange anticipates making additional enhancements to its non-option trading platform prior to the February 2007 compliance date for Regulation NMS that are not related to the requirements of the Specifications Date.

2. Statutory Basis

CBOE 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.⁷ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)⁸ requirements that the rules of an exchange be 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

shares while CBOE's bid is \$50 for 500 shares and Exchange A's bid is 50.02 for 200 shares and Exchange B's bid is 50.01 for 400 shares, and assuming CBOE Market-Makers do not match the 50.02 NBBO, then the order will route to the DPM for handling. The DPM's handling options include the following: (i) route 1000 shares to Exchange A; (ii) route 200 to Exchange A and 400 to Exchange B while concurrently executing 400 on CBOE at 50; or (iii) route 200 to Exchange A and price improve 800 on CBOE at 50.01. Note that, if a better price becomes available prior to the DPM routing away, such better price must be taken into account by the DPM.

⁷ 15 U.S.C. 78(f)(b).

⁸ 15 U.S.C. 78(f)(b)(5).

The Exchange believes the proposed rule change would impose no burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

No written comments were solicited or received by the Exchange on this proposal.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the Exchange consents, the Commission will:

- (A) by order approve the 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. Please include File Number SR-CBOE-2006-70 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-CBOE-2006-70. 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-2006-70 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.⁹

Nancy M. Morris
Secretary

⁹ 17 CFR 200.30-3(a)(12).