

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-54437; File No. SR-CHX-2005-06)

September 13, 2006

Self-Regulatory Organizations; Chicago Stock Exchange, Inc.; Order Approving a Proposed Rule Change and Amendment No. 1 and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 2 to a Proposed Rule Change Relating to Disciplinary and Delisting Procedures

I. Introduction

On March 7, 2005, the Chicago Stock Exchange, Inc. (“CHX” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposal to revise the Exchange’s disciplinary and delisting procedures. The Exchange filed Amendment No. 1 to the proposed rule change on June 2, 2006. The proposed rule change, as amended by Amendment No. 1, was published for comment in the Federal Register on June 27, 2006.<sup>3</sup> The Commission received no comments regarding the proposal, as amended by Amendment No. 1. On August 10, 2006, the Exchange filed Amendment No. 2 to the proposed rule change.<sup>4</sup> This order approves the proposal, as amended. In addition, the Commission is publishing notice to solicit comments on, and is simultaneously approving, on an accelerated basis, Amendment No. 2.

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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> See Securities Exchange Act Release No. 54021 (June 20, 2006), 71 FR 36571 (“Notice”).

<sup>4</sup> Amendment No. 2 revises the proposal to: (1) clarify that the Exchange will use its emergency suspension authority under CHX Art. VII, Rule 2(a)(1)(i) only with respect to CHX Participants, and not with respect to associated persons of CHX Participants; (2) confirm that the Exchange will not use its emergency suspension authority under CHX Art. VII, Rule 2(a)(1)(i) unless the Exchange believes that the rule violation suggests that a Participant is in such financial or operational difficulty that the Participant cannot be permitted to continue to do business as a Participant with safety to investors, creditors,

## II. Description of the Proposal

The proposal revises a number of rules governing the CHX's disciplinary and delisting procedures. According to the CHX, the Exchange reviewed its rules, in part, to respond to the requirements of the Commission's 2003 order instituting public administrative proceedings against the Exchange,<sup>5</sup> and in light of the Commission's guidance that a self-regulatory organization ("SRO") should ensure that its "regulatory function is strong, vigorous, and sufficiently independent and insulated from improper influence from management or any regulated entity."<sup>6</sup>

### A. Authorization of Formal Disciplinary Actions and Other Proceedings

Several CHX rules currently require the CHX's Chief Executive Officer ("CEO") to authorize the institution of disciplinary and related proceedings.<sup>7</sup> The proposal revises these rules to authorize the CHX's Chief Regulatory Officer ("CRO"), rather than its CEO, to institute these proceedings. The Exchange believes that requiring the CRO, rather than the CEO, to

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other Participants, or the Exchange; and (3) clarify that only a Participant, but not an associated person of a Participant, may hold a trading permit.

<sup>5</sup> See Securities Exchange Act Release No. 48566 (September 30, 2003), Administrative Proceeding File No. 3-11282 ("Order"). The Exchange noted that certain aspects of the proposed rule change are based on the recommendations of the Independent Counsel appointed by the terms of the Order.

<sup>6</sup> See Securities Exchange Act Release No. 48946 (December 17, 2003), 68 FR 74678 (December 24, 2003) (order approving File No. SR-NYSE-2003-34).

<sup>7</sup> See, e.g., CHX Art. VII, Rule 2, "Emergency Suspensions" (authorizing the CEO to suspend a Participant or associated person under certain circumstances); CHX Art. XII, Rule 2(a), "Minor Infraction," (authorizing the CEO to censure a respondent or impose a fine for a minor infraction); and CHX Article XII, Rule 2(d) (renumbered by the proposal as 2(b), "Collateral Proceedings") (authorizing the CEO to suspend or expel a Participant or associated person sanctioned by another SRO). See also CHX Art. XII, Rule 1(b) (requiring the CEO to direct the CHX's staff to prefer written charges if it appears to the CEO that there has been a violation of the CHX's rules).

authorize proceedings under these rules will eliminate any appearance of a conflict of interest and bolster the apparent and actual independence of the Exchange's regulatory processes.<sup>8</sup>

The proposal will allow either the CRO or the CEO to institute proceedings under CHX Art. XI, Rule 8, "Operational Capability," based upon a Participant's failure to maintain operational capability, and to impose restrictions on Participant Firm operations under CHX Art. XI, Rule 3(d), "Restrictions on Operations," relating to net capital and aggregate indebtedness requirements. The Exchange believes that allowing either the CEO or the CRO to authorize proceedings under these rules is appropriate because they may involve a mixture of business and regulatory concerns.

**B. Initial Decision by Hearing Officers**

To eliminate any appearance of a conflict of interest, the proposal eliminates the provisions in current CHX Art. XII, Rule 5(b), "Decision," that authorize the CEO to review a Hearing Officer's proposed decision and modify its conclusions, remand the matter for additional findings or supplemental proceedings, or conduct further proceedings himself.<sup>9</sup> The revised rule provides that the Hearing Officer's decision will be final, although it may be appealed to a Judiciary Committee or to the Board, as applicable, in accordance with CHX Art. XII, Rule 6.

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<sup>8</sup> Although the CRO reports to the CEO, and therefore could potentially be influenced by the CEO's views on a proposed disciplinary matter, the Exchange noted that the CRO is required to appear before, and report on the Exchange's regulatory programs to, the Exchange's Regulatory Oversight Committee not less than quarterly. The Regulatory Oversight Committee, a committee of the CHX's Board of Directors ("Board") composed predominately of independent directors, is charged with oversight of the Exchange's regulatory function. The Exchange believes that this review by the Regulatory Oversight Committee serves as a reasonable mechanism to prevent any conflict of interest from interfering with the Exchange's regulatory role.

<sup>9</sup> The proposal renumbers this provision as CHX Art. XII, Rule 5(f).

C. Criteria for the Selection of Hearing Officers in Disciplinary and Delisting Proceedings

The proposal revises CHX Article XII, Rule 5, "Hearing Procedure," to delineate the criteria that the CEO must consider in selecting a Hearing Officer for a disciplinary proceeding<sup>10</sup> and to create a process through which a respondent may object to a particular Hearing Officer on the grounds of bias or conflict of interest.<sup>11</sup> The proposal adopts identical criteria and objection procedures with respect to Hearing Officers for delisting hearings.<sup>12</sup>

D. Elimination of Redundant Procedures

The proposal eliminates the summary hearing process in current CHX Art. XII, Rule 2(b), "Summary Hearing and Penalty," which the Exchange believes is redundant of other CHX disciplinary processes and, therefore, unnecessary. Similarly, the proposal deletes the suspension and termination rules applicable to specialists, odd-lot dealers, and market makers in CHX Articles XXX, XXXI, and XXXIV, respectively, because the Exchange believes that these provisions are obsolete and redundant of the Emergency Suspension provisions provided under CHX Art. VII, Rule 2.

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<sup>10</sup> See CHX Art. XII, Rule 5(e), "Appointment of Hearing Officer." Specifically, the rule states that the CEO should give reasonable consideration to a prospective Hearing Officer's professional competence and reputation, experience in the securities industry, familiarity with the subject matter involved, the absence of bias and any conflict of interest, and any other relevant factors.

<sup>11</sup> See CHX Art. XII, Rule 5(h), "Impartiality of Hearing Officer." The rule permits a respondent to file a motion seeking the disqualification of a Hearing Officer for bias or conflict of interest within 15 days of the Hearing Officer's appointment.

<sup>12</sup> See CHX Art. XXVIII, Rule 4(d).

E. Appeal of Disciplinary Proceedings

The proposal revises CHX Art. XII, Rule 6 to allow the Exchange, as well as a respondent, to appeal decisions to a Judiciary Committee.<sup>13</sup> Similarly, the proposal revises CHX Art. XXVIII, Rule 4(e) to allow the Exchange, as well as an issuer, to appeal the decision of a Hearing Officer in a delisting proceeding.

In addition, the proposal streamlines the current appellate review process for disciplinary actions. Currently, appeals are heard first by a Judiciary Committee, then by the Executive Committee and finally, on a discretionary basis, by the Board.<sup>14</sup> The proposal eliminates appellate review by the Executive Committee and provides that appeals will be heard by a Judiciary Committee and, on a discretionary basis, by the full Board.<sup>15</sup> The Exchange believes that the revised procedures should reduce the time required to reach a final judgment, thus contributing to the fair and effective enforcement of the Exchange's rules.

F. Failure to Promptly Pay Fines

Under CHX Art. XIV, Rule 10, "Failure to Pay Debts," a Participant who fails to pay a fine owed to the Exchange within 60 days may be suspended, after due notice, until payment is made. The proposal revises this rule to authorize the Exchange to initiate a disciplinary proceeding under Art. XII against a Participant or associated person for the failure to pay a debt owed to the Exchange. The Exchange believes that the revised rule will provide the Exchange with the flexibility to assess additional fines or other sanctions, either in lieu of or in addition to a

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<sup>13</sup> Specifically, the revised rule allows the Exchange to appeal an order issued under CHX Art. XII, Rules 2(b), 4(b), and 5.

<sup>14</sup> See CHX Art. XII, Rule 6.

<sup>15</sup> See CHX Art. XII, Rule 6.

suspension, as an added inducement to avoid late payment of a fine owed to the Exchange.

G. Procedural Changes

The proposal revises several CHX rules to provide greater clarity to the Exchange's disciplinary and delisting procedures. In this regard, the proposal sets forth clear timeframes for responding to charges, scheduling hearings, filing motions, and issuing orders.<sup>16</sup> The proposal also: (i) specifies the information that must be included in certain notices;<sup>17</sup> (ii) creates limited rights to prehearing discovery for all parties to a proceeding;<sup>18</sup> (iii) sets timeframes for motions

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<sup>16</sup> For example, the proposal revises CHX Art. XII, Rule 5, to require that: (i) a respondent file a written answer to charges within 30 days from the date of service of the charges; (ii) the Hearing Officer schedule a hearing within 30 days after the filing of an answer; and (iii) the Hearing Officer ordinarily issue an order within 90 days after the conclusion of a hearing. Similarly, the proposal revises CHX Art. XXVIII, Rule 4(d), "Hearing," to require that a Hearing Officer in a delisting hearing to schedule a hearing within 30 days after receipt of an issuer's demand for a hearing, and that the Hearing Officer issue an order within 90 days after the conclusion of a hearing.

<sup>17</sup> Specifically, the proposal revises Article XII, Rule 1(b), "Written Charges," to state that a respondent must be served with written charges identifying with specificity each Exchange rule or provision of the federal securities laws alleged to have been violated. The proposal revises CHX Art. XII, Rule 2(a), "Minor Infraction," to state explicitly that the person against whom a fine is imposed shall be served with a written statement (the "Notice of Fines"), signed by the CRO or his designee, setting forth: (i) the rule(s) or policy(ies) alleged to have been violated; (ii) the act or omission constituting each such violation; (iii) the fine imposed for each such violation; (iv) the date on which such action is taken; and (v) the date on which such determination becomes final and such fine becomes due and payable to the Exchange, or on which such action must be contested. The Exchange represents that it currently provides this notice to persons against whom a fine is imposed, and that the language added to the rule confirms that this practice should continue.

<sup>18</sup> The parties must exchange a list of witnesses that they plan to call to testify at least 30 days before the hearing. See CHX Art. XII, Rule 5(c)(1). In addition, any party may request production of some or all of the documents that an opposing party intends to introduce as evidence. This request must be made at least 45 days prior to the hearing, and the documents must be produced at least 30 days before the hearing. See CHX Art. XII, Rule 5(c)(2). A party that does not identify witnesses or produce requested documents will be barred from presenting those witnesses or documents at the hearing,

and appeals;<sup>19</sup> (iv) confirms that the Board or the Executive Committee could direct the CRO to initiate a disciplinary proceeding;<sup>20</sup> (v) confirms that a Hearing Officer must make specific findings as to each proffered charge and impose an appropriate sanction for violations that are found to have occurred;<sup>21</sup> (vi) clarifies that fines assessed under the summary procedure of CHX Art. XII, Rule 2 are not publicly reported, except as may be required by Rule 19d-1 under the Act;<sup>22</sup> and (vii) confirms that the three-person Board panel that hears an appeal from an emergency suspension decision will consist of at least two public directors on the Board.<sup>23</sup> The proposal also adopts provisions that set forth the required content of settlement agreements in disciplinary proceedings.<sup>24</sup>

#### H. Removal of Securities

The proposal revises CHX Art. XXVIII, Rule 4, "Removal of Securities," to provide that

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unless the party seeking to introduce the evidence can show good cause for the failure to earlier identify the witnesses or documents and can establish that the failure to allow the presentation of the evidence would result in undue hardship to that party. See CHX Art. XII, Rules 5(c)(1) and 5(c)(2).

<sup>19</sup> See, e.g., CHX Art. XII, Rule 5(h) (regarding motions to disqualify the hearing examiner) and CHX Art. XII, Rule 6(a) (regarding appeals to the Judiciary Committee).

<sup>20</sup> See CHX Art. XII, Rule 1(b)(2).

<sup>21</sup> See CHX Art. XII, Rule 5(f).

<sup>22</sup> See CHX Art. XII, Rule 2(a).

<sup>23</sup> See CHX Art. VII, Rule 2(b).

<sup>24</sup> See CHX Art. XII, Rule 1(d). The proposal deletes the current provisions in CHX Art. XII, Rule 2(c) governing settlement agreements and adopts new Rule 1(d) of CHX Art. XII. This provision confirms that a respondent could settle a proceeding at any time by entering into a settlement agreement with the Exchange without admitting or denying the charges, except as to jurisdiction, which must be admitted. The settlement agreement must contain a waiver by the respondent of all rights to appeal and a proposed penalty to be imposed, which must be reasonable under the circumstances and consistent with the seriousness of the alleged violations. The CRO will have the sole right to approve a proposed settlement agreement.

the Listing Unit of the CHX's Market Regulation Department, rather than the Board, will make the initial determination to delist a security. The proposal also eliminates the CEO's review of a Hearing Officer's findings with respect to a delisting. In addition, the proposal confirms that a Hearing Officer's decision is final unless a review is specifically demanded,<sup>25</sup> and sets forth the process and standards that the Executive Committee must follow with respect to any appeal of a Hearing Officer's decision.<sup>26</sup>

I. Role of Exchange Counsel

The proposal clarifies the role of Exchange counsel in disciplinary and delisting proceedings by providing that, in both types of proceedings, the Exchange counsel acting as counsel to the Hearing Officer may not be an employee of the CHX's Market Regulation Department and may not have directly participated in any examination, investigation, or decision associated with the initiation or conduct of the proceeding.<sup>27</sup>

J. Additional Changes

The proposal also revises several terms used throughout CHX Art. XII. For example, the proposal revises CHX Art. XII to substitute the term "respondent" for "accused" and "hearing" for "trial."

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<sup>25</sup> Appeals from a Hearing Officer's decision would be heard by the Executive Committee. See CHX Art. XXVIII, Rule 4(e).

<sup>26</sup> See CHX Art. XXVIII, Rules 4(d) and (e). As noted above, the proposal also adopts provisions setting forth the criteria that a CEO must consider in selecting a Hearing Officer for a delisting proceeding and provides a process for objecting to a Hearing Officer on the grounds of bias or conflict of interest. See notes 10 – 12, supra, and accompanying text.

<sup>27</sup> See CHX Art. XII, Rule 5(g) and CHX Art. XXVIII, Rule 4(d).



K. Effective Date of the Rule Changes

The Exchange states that the rule changes contained in the proposal will apply to any formal disciplinary proceeding, suspension decision, or delisting proceeding that the Exchange initiates on or after a date that immediately follows the date of the Commission's approval. The Exchange will issue a notice to Participants announcing this date.

L. Amendment No. 2

CHX Art. VII, Rule 2(a)(1)(i), as amended, provides the Exchange with emergency suspension authority over a Participant that has failed to perform its contracts, is insolvent, or is in such financial or operational condition or otherwise conducting its business in such a manner that the Participant cannot be permitted to continue in business with safety to its customers, creditors, or the Exchange, including a reasonable belief that the Participant is violating and will continue to violate any provision of the CHX's rules, the federal securities laws or rules or regulations thereunder, or any condition or restriction imposed pursuant to the provisions of CHX Art. XI, Rule 3(d), or CHX Art. XI, Rule 8(a). Amendment No. 2 revises the proposal to: (1) clarify that the Exchange will use its emergency suspension authority under CHX Art. VII, Rule 2(a)(1)(i) only with respect to CHX Participants, and not with respect to associated persons of CHX Participants; (2) confirm that the Exchange will not use its emergency suspension authority under CHX Art. VII, Rule 2(a)(1)(i) unless the Exchange believes that the rule violation suggests that a Participant is in such financial or operational difficulty that the Participant cannot be permitted to continue to do business as a Participant with safety to investors, creditors, other Participants, or the Exchange; and (3) clarify that only a Participant, but not an associated person of a Participant, may hold a trading permit. The proposal also revises CHX Art. VII, Rule 2(a)(1)

to allow the Exchange to use its emergency suspension authority with respect to an associated person who has been barred or suspended from being associated with a member of any SRO.

### III. Discussion

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>28</sup> In particular, the Commission finds that the proposed rule change, as amended, is consistent with Section 6(b)(1) of the Act,<sup>29</sup> which requires, among other things, that a national securities exchange have the capacity to enforce compliance by its members and persons associated with its members with the provisions of the Act and the rules and regulations thereunder, and with the rules of the exchange; with Section 6(b)(5) of the Act,<sup>30</sup> which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to, and perfect the mechanism of, a free and open market and a national market system and, in general, to protect investors and the public interest; and with Section 6(b)(7) of the Act,<sup>31</sup> which requires that the rules of a national securities exchange provide a fair procedure for the disciplining of members and persons associated with members. In addition, the Commission finds that the proposal, as amended, is consistent with Section 6(d)(1) of the Act,<sup>32</sup> which requires, among other things, that a national securities

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<sup>28</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>29</sup> 15 U.S.C. 78f(b)(1).

<sup>30</sup> 15 U.S.C. 78f(b)(5).

<sup>31</sup> 15 U.S.C. 78f(b)(7).

<sup>32</sup> 15 U.S.C. 78f(d)(1).

exchange, in determining whether a member or associated person should be disciplined, bring specific charges, notify the member or associated person of, and give him an opportunity to defend against the charges, and keep a record. The Commission also finds that the proposal, as amended, is consistent with Section 6(d)(3) of the Act,<sup>33</sup> which, among other things, allows a national securities exchange to summarily suspend a member or person associated with a member who has been and is expelled or suspended from any SRO or barred or suspended from being associated with a member of any SRO, and to summarily suspend a member who is in such financial or operating difficulty that the exchange determines and so notifies the Commission that the member cannot be permitted to continue to do business as a member with safety to investors, creditors, other members, or the exchange.

The Commission finds that the rule changes<sup>34</sup> requiring the CRO, rather than the CEO, to authorize the institution of disciplinary and related proceedings could help to reduce the appearance of, or potential for, a conflict of interest in the institution of such proceedings, thereby helping the Exchange to provide a fair procedure for disciplining members, as required by Section 6(b)(7) of the Act,<sup>35</sup> and helping to separate the CHX's business and regulatory functions. Similarly, the Commission finds that the proposal to eliminate the provisions in current CHX Art. XII, Rule 5(b) that allow the CEO to review and modify a Hearing Officer's proposed decision should help to eliminate the appearance of a conflict of interest in the

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<sup>33</sup> 15 U.S.C. 78f(d)(3).

<sup>34</sup> See note 7, supra, and accompanying text.

<sup>35</sup> Although the CRO reports to the CEO, the CRO must report not less than quarterly to the Board's Regulatory Oversight Committee, which is composed predominately of independent directors and assists the Board in monitoring the design, implementation,

Exchange's disciplinary process. The Commission believes that the proposal to amend CHX Art. XI, Rules 3(d) and 8(a), to allow the CRO, as well as the CEO, to authorize proceedings under those rules is reasonable because those rules govern matters that raise both business and regulatory concerns.

The Commission finds that the adoption of criteria that the CEO should consider in selecting a Hearing Officer for disciplinary proceedings, and the procedures for objecting to a Hearing Officer in a disciplinary proceeding,<sup>36</sup> are consistent with Section 6(b)(7) of the Act because they should help the Exchange to provide a fair procedure for disciplining members. The Commission finds that the comparable provisions relating to the criteria for selection of Hearing Officers for delisting proceedings<sup>37</sup> are consistent with Section 6(b)(5) of the Act because they should help the Exchange to provide a fair procedure for delisting proceedings.

Similarly, the Commission believes that the rule changes prohibiting the person acting as Exchange counsel to the Hearing Officer in a disciplinary or delisting proceeding from being an employee of the CHX's Market Regulation Department or from having directly participated in any examination, investigation, or decision associated with the initiation or conduct of the proceeding<sup>38</sup> should help the Exchange to provide fair disciplinary and delisting proceedings by ensuring that such counsel did not participate in the initiation or conduct of the matter before the Hearing Officer.

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and effectiveness of the CHX's regulatory programs. See CHX Article IV, Rule 4, "Regulatory Oversight Committee."

<sup>36</sup> See notes 10 - 12, supra, and accompanying text.

<sup>37</sup> See CHX Art. XXVIII, Rule 4(d).

<sup>38</sup> See CHX Art. XII, Rule 5(g) and CHX Art. XXVIII, Rule 4(d).

The Exchange believes that the procedures in current CHX Art. XII, Rule 2(b), and in CHX Articles XXX, XXXI, and XXXIV are obsolete and redundant of the emergency suspension provisions of CHX Art. VII, Rule 2.<sup>39</sup> Accordingly, the Commission believes that the deletion of these provisions should simplify the CHX's rules.

The Commission finds that the rule changes<sup>40</sup> allowing the Exchange to appeal the decision of the Hearing Officer in disciplinary and delisting proceedings are consistent with Section 6(b)(1) of the Act because these provisions could enhance the Exchange's ability to enforce its rules and the federal securities laws and the rules and regulations thereunder. In addition, the Commission believes that the changes to CHX Art. XII, Rule 6 that eliminate Executive Committee review of Judiciary Committee decisions could allow disciplinary matters to be resolved more efficiently. The Commission notes that respondents will continue to have the ability to appeal a Hearing Officer's decision to the Judiciary Committee, and that the Board will continue to have the ability to review decisions of the Judiciary Committee on a discretionary basis.<sup>41</sup> Accordingly, although the proposal eliminates Executive Committee review of decisions by the Judiciary Committee, the Commission believes that the CHX's rules will continue to provide a fair procedure for disciplining members, consistent with Section 6(b)(7) of the Act.

The Commission believes that the amendments to CHX Art. XIV, Rule 10 authorizing the Exchange to initiate a disciplinary proceeding under CHX Art. XII for failure to pay a debt

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<sup>39</sup> See Section II.D., supra.

<sup>40</sup> See Section II.E., supra.

<sup>41</sup> See CHX Art. XII, Rule 6.

owed to the Exchange could facilitate the Exchange's collection of fines by providing the Exchange with an additional mechanism for sanctioning Participants, associated persons, and other persons or entities subject to the CHX's jurisdiction that fail to pay fines within the time prescribed in the CHX's rules.

As described more fully in Section II.G., supra, the proposal also revises the CHX's rules to, among other things, set timeframes for filing motions and appeals, scheduling hearings, and issuing orders; provide for pre-hearing discovery, with timeframes for exchanging witness lists and producing documents; and specify the required content of settlement agreements in disciplinary proceedings. The Commission finds that these changes should help the Exchange to provide a fair procedure for disciplining members, as required by Section 6(b)(7) of the Act, by adding clarity and specificity to the CHX's disciplinary rules and by establishing timeframes for respondents and Hearing Officers that could facilitate the timely resolution of disciplinary matters.

The Commission finds that proposal to revise CHX Art. XII, Rule 1(b) and CHX Art. XII, Rule 2(a)<sup>42</sup> to clarify in its rules that the Exchange must provide a respondent with written charges identifying the laws or rules allegedly violated is consistent with Section 6(d)(1) of the Act, which, among other things, requires that a national securities exchange, in a proceeding to determine whether to discipline a member or associated person, bring specific charges, notify the member or person of, and give him an opportunity to defend against, the charges, and keep a

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<sup>42</sup> See note 17, supra.

record.<sup>43</sup> Similarly, the Commission finds that the proposed changes to CHX Art. XII, Rule 5(f) requiring, among other things, that a Hearing Officer's order make specific findings as to each charge brought by the Exchange and, where a violation is found, impose an appropriate sanction,<sup>44</sup> is consistent with the requirements in Section 6(d)(1)(B) and (C) of the Act that a national securities exchange's determination to impose a disciplinary sanction be supported by a statement setting forth the specific law, rule, or regulation violated and the sanction imposed and the reasons therefor.

As described more fully above,<sup>45</sup> the proposal revises CHX Art. VII, Rule 2(a)(1) to clarify the manner in which the Exchange would use its emergency suspension authority and to allow the Exchange to use its emergency authority with respect to a Participant that it believes is violating any condition or restriction imposed pursuant to the provisions of CHX Art. XI, Rule 3(d), or CHX Art. XI, Rule 8(a).<sup>46</sup> The Commission finds that these changes are consistent with Section 6(d)(3)(B) of the Act, which allows a national securities exchange to summarily suspend a member who is in such financial or operating difficulty that the exchange determines and so notifies the Commission that the member cannot be permitted to continue to do business as a

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<sup>43</sup> The Exchange has represented that it currently provides respondents with written notice of the charges and that the proposed rule change is intended to confirm that this practice should continue.

<sup>44</sup> See Section II.G, supra.

<sup>45</sup> See Section II.L, supra.

<sup>46</sup> CHX Art. XI, Rule 3(d) allows the CEO or the CRO to impose restrictions or conditions on a Participant that fails to maintain necessary operational personnel or facilities or engages in an activity that casts doubt on the Participant's continued compliance with the CHX's net capital requirements. CHX Art. XI, Rule 8(a) allows the CEO or the CRO to impose conditions or restrictions on a Participant that fails to maintain adequate operational capability, including making and keeping current books and records in accordance with Rules 17a-3 and 17a-4 under the Act, 17 CFR 240.17a-3 and 17a-4.

member with safety to investors, creditors, other members, or the exchange. Similarly, the Commission finds that the revisions to CHX Art. VII, Rule 2(a)(1)(ii) that allow the Exchange to use its emergency authority with respect to an associated person barred or suspended from being associated with a member of any SRO is consistent with Section 6(d)(3)(A) of the Act, which allows a national securities exchange to summarily suspend a member or associated person who has been and is expelled or suspended from any SRO or barred or suspended from being associated with a member of any SRO.

In addition, the proposal confirms that the three-person Board panel that hears an appeal from an emergency suspension will include two public members of the Board.<sup>47</sup> The Commission believes that this change could help to ensure the impartiality of the panels that hear appeals from emergency suspensions, thereby helping the Exchange to provide a fair procedure for disciplining members and associated persons, as required by Section 6(b)(7) of the Act.

The Commission finds that the changes to CHX Art. XXVIII, Rule 4, relating to delisting procedures, are intended to clarify the CHX's delisting procedures and to ensure the fairness of the CHX's delisting proceedings and thus are consistent with the Act. In this regard, the proposal eliminates the CEO's review of a Hearing Officer's findings with respect to a delisting, thereby avoiding the appearance of, or potential for, a conflict of interest. Similarly, the proposal revises the CHX's rules to provide that the Listing Unit of the CHX's Market Regulation Department, rather than the Board, will make the initial determination to delist a security, thereby ensuring that the entity that initiates a delisting will not participate in an appellate review of the initial delisting determination. An issuer may request a hearing of a delisting before a Hearing

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<sup>47</sup> See CHX Art. VII, Rule 2(b).



Officer, and the Hearing Officer's decision will be final unless either the issuer or the Exchange requests review of the decision by the Executive Committee of the CHX Board.<sup>48</sup> The Executive Committee must uphold the Hearing Officer's decision if it finds that the Hearing Officer's factual conclusions are supported by substantial evidence and his or her decision is not arbitrary, capricious, or an abuse of discretion.<sup>49</sup> The Commission believes that adopting these processes and standards for review should help promote fairness with respect to the CHX's appellate process.

The Commission finds that the technical changes to revise certain terms used throughout the CHX's disciplinary rules are consistent with the Act.

The Commission finds good cause for approving Amendment No. 2 prior to the thirtieth day after the date of publication of notice of filing thereof in the Federal Register. As described more fully above, Amendment No. 2 clarifies the proposal by confirming that the Exchange will use its emergency suspension authority under CHX Art. VII, Rule 2(a)(1)(i) only with respect to Participants and only when the Exchange believes that a rule violation suggests that a Participant is in such financial or operational difficulty that the Participant cannot be permitted to continue to do business as a Participant with safety to investors, creditors, other Participants, or the Exchange. Accordingly, the Commission finds that it is consistent with Sections 6(b)(5) and 19(b) of the Act to approve Amendment No. 2 on an accelerated basis.

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<sup>48</sup> See CHX Art. XXVIII, Rule 4(e).

<sup>49</sup> See id.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 2, including whether Amendment No. 2 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-CHX-2005-06 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-CHX-2005-06. 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-CHX-2005-06 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>50</sup> that the proposed rule change (SR-CBOE-2005-06), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>51</sup>

Nancy M. Morris  
Secretary

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<sup>50</sup> 15 U.S.C. 78s(b)(2).

<sup>51</sup> 17 CFR 200.30-3(a)(12).