

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-52766; File No. SR-CHX-2004-38)

November 10, 2005

Self-Regulatory Organizations; Chicago Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change and Amendment Nos. 1 and 2 Thereto Relating to Records of Orders and Executions

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 November 3, 2004, the Chicago Stock Exchange, Inc. (“CHX” 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 CHX. On July 3, 2005, the Exchange filed Amendment No. 1 to the proposal³ and on September 8, 2005, the Exchange filed Amendment No. 2 to the proposal.⁴ The

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, which replaced and superseded the original filing in its entirety, the Exchange amended the proposed rule text to add requirements that participants confirm whether an order was an agency or professional order; whether an order was short or short exempt; the market to which the order was transmitted; the identification of any party cancelling or modifying the order; the date and time of any order expiration; and the contra party to the execution (if applicable). The Exchange also added Interpretation and Policy .09 to confirm that the requirements of the proposed rule would not replace any record retention obligations to which the Exchange’s participants may be subject under the Act and the rules thereunder. Finally, the Exchange replaced references to the Exchange’s “members” with references to its “participants,” reflecting changes in terminology associated with the Exchange’s February 2005 demutualization. See Securities Exchange Act Release No. 51149 (February 8, 2005), 70 FR 7531 (February 14, 2005) (approval order for the Exchange’s proposed rule changes in connection with its demutualization).

⁴ In Amendment No. 2, which replaced and superseded the filing as amended by Amendment No. 1 in its entirety, the Exchange made minor changes to the proposed rule text, including (1) confirming that a participant must record any modifications to the date and time of any order expiration and (2) consistently capitalizing the word “Rule.” In addition, the Exchange conformed the footnotes in the purpose section to reflect changes made to the rule language in Amendment No. 1. The substantive changes in Amendment No. 1 were included in Amendment No. 2.

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 CHX proposes to amend its rules to require its on-floor participants to electronically record specific details about orders originating on or off the floor of the Exchange for execution on the Exchange, as well as orders issued from the floor of the Exchange to any other market or trading venue.

The text of the proposed rule change is below. Proposed new language is underlined; proposed deletions are in [brackets].

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ARTICLE XX

Regular Trading Sessions

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Records of Orders and Executions

RULE 24. (a) Every Floor Participant shall preserve for at least three years (or any longer period of time required by Exchange Act Rule 17a-4) a record, meeting the criteria set out in paragraph (b) below, of:

(1) every order originat[ed]ing [by him or it] on the Floor [and] that is given to (or received from) another Participant for execution and any execution of that order, and

(2) [of] every order [commitment or obligation to trade] issued from the Floor to any other market or trading venue and any execution of that order[through ITS or any other application of the System or pursuant to Rule 39 or Rule 40,]; and

(3) [of] every order originating off the Floor, transmitted by any person, whether or not that person is [other than]a Participant, to such Participant on the Floor and any execution of that order[, which record shall include the name and the amount of the security, the terms of the order and the time when such order was so given or transmitted];

provided, however, that the Exchange may, upon application, grant exemption from the provisions of this Rule.

(b) Subject to the exceptions set out in Interpretations .02, .04, .05 and .07 below, each Floor Participant must record, in such electronic system(s) as the Exchange shall designate, the following details about each order and execution identified in (a)(1) through (3) above:

- (1) Symbol;
- (2) Clearing Participant;
- (3) Order identifier that uniquely identifies the order;
- (4) Identification of Participant recording the order details;
- (5) Number of shares or quantity of security;
- (6) Side of market;
- (7) Designation of order type (e.g., market, limit, stop, stop limit);
- (8) Whether the order is agency or professional;
- (9) Whether the order is being handled pursuant to Exchange Act Section 11(a)(1)(G) and any applicable rules thereunder;
- (10) Whether the order is short or short exempt;
- (11) Whether the order is a bona fide arbitrage order;
- (12) Any limit price and/or stop price;
- (13) Date and time of order receipt or transmission (as applicable);

- (14) The market, off-floor firm or on-floor Participant to which the order was transmitted or from which the order was received (if applicable);
- (15) Time in force;
- (16) Designation as held or not held;
- (17) Any special conditions or instructions (including any customer do-not-display or display instructions and any all-or-none conditions);
- (18) Any modifications to the details set out in (1)-(17) above or (20) below, for all or part of the order, or any cancellation of all or part of the order;
- (19) Date and time of receipt or transmission of any modifications to the order or any cancellation of the order;
- (20) Date and time of any order expiration;
- (21) Identification of the party cancelling or modifying the order;
- (22) Transaction price (if applicable);
- (23) Number of shares executed (if applicable);
- (24) Date and time of execution (if applicable);
- (25) Contra party to the execution (if applicable);
- (26) Settlement instructions (if applicable);
- (27) System-generated time(s) of recording required information; and
- (28) Such other information as the Exchange may from time to time require.

[Whenever a cancellation is entered with respect to such an order or commitment or obligation to trade, or a report of the execution of such an order or commitment or obligation to trade is received, there shall be preserved for at least three years, in addition to the record required by the foregoing paragraph, a record of the cancellation of the order or commitment or

obligation to trade or of the receipt of such report, which shall include the time of entry of such cancellation or of the receipt of such report.]

(c) Floor Participants must record the information required by (b) above immediately after such information is received or becomes available.

[c](d) Before any such order is executed, including the case where an order is to be executed by the issuance from the Floor of a commitment or obligation to trade through ITS or any other application of the System or pursuant to Rule 39 or Rule 40, there shall be placed upon the order slip or other record the name or designation of the account for which such order is to be executed. No change to the name or designation of the [in such] account for which an order is to be executed [name or designation] shall be made unless the change has been authorized by the Participant or by a partner or officer of the Participant Firm, who shall, prior to giving his approval of such change, be personally informed of the essential facts relative thereto and shall indicate his approval of such change in writing on the order.

[Exceptions

Under exceptional circumstances the Exchange may upon written request waive the requirements contained in (1)(a) above.]

• • • ***Interpretations and Policies:***

.01 Every order covered by [(1)] paragraph (a) above, which is to be executed pursuant to Section 11(a)(1)(G) of the Act and Rule 11a1-1(T) thereunder, shall bear an identifying notation that will enable the executing Participant to disclose to other Participants that the order is subject to those provisions.

.02 For purposes of this Rule, an order shall be any written, oral or electronic instruction to effect a transaction. A decision by a co-specialist, market maker or floor broker to

buy or sell securities for his or her own account on the Floor of the Exchange shall not constitute an order for which a record must be made under this Rule.

.03 Each required record of the time of an event shall be expressed in terms of hours, minutes and seconds.

.04 This Rule shall not apply to orders sent or received through the Exchange's MAX system or through any other electronic systems that the Exchange expressly recognizes as providing the required information in a format acceptable to the Exchange. The Exchange will not recognize a non-Exchange system as providing information in an acceptable format unless that system has synchronized its business clocks for recording data with reference to a time source designated by the Exchange and maintains that synchronization in conformity with procedures prescribed by the Exchange.

.05 Any orders which the Exchange has expressly recognized as incompatible for entry in an Exchange system relied on by a Floor Participant to record the details of the order in compliance with this Rule shall be exempt from the order entry requirements of paragraph (b) above; provided, however, that Floor Participants shall retain a written record of those orders which includes as much of the information set out in paragraph (b) as is possible, but no less than the name and the amount of the security, the terms of the order, the time when such order was so given or transmitted, the date and time of any modifications or cancellations of the order, the date and time of execution and the execution price.

.06 With respect to a bona fide arbitrage order, a Floor Participant may execute such order before entering the order into an electronic system as required by paragraph (b) above, but such Floor Participant must enter such order into such electronic system no later than 60 seconds after the execution of such order. With respect to an order to offset a transaction made in error, a Floor Participant may, upon discovering such error within the same trading session, effect an offsetting transaction without first entering such order into an electronic system, but such Floor Participant must enter such order into such electronic system no later than 60 seconds after the execution of such order.

.07. A Floor Participant who receives orders to buy and sell the same security and executes those orders in full immediately upon receipt shall record only the information set out in (b)(1), (2), (4), (9), (10) and (22) through (28) above.

.08. Failure to comply with the provisions of this Rule may be considered conduct inconsistent with just and equitable principles of trade, in violation of Article VIII, Rule 7.

.09 The provisions of this Rule do not replace any record retention obligations to which the Exchange's Participants may be subject under the Exchange Act and the rules thereunder.

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 CHX included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received regarding the proposal. The text of these statements may be examined at the places specified in Item IV below. The CHX 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’s on-floor participants execute trades on the Exchange and on other markets.⁵ Currently, the Exchange’s electronic systems capture information about most of the orders executed on the Exchange and about many of the orders executed in other markets. This information is used by the Exchange to conduct surveillance of its floor participants’ trading activities. In some instances, however, the Exchange does not have complete information about the orders received and executed by its participants or does not have that information in electronic form. To bolster its ability to conduct automated surveillance of its participants’ trading activities, the Exchange is proposing to require its floor participants to provide particular data about all orders originating on or off the floor of the Exchange for execution on the Exchange, as well as all orders issued from the floor of the Exchange to any other market or trading venue.⁶ For purposes of this submission, these orders will be called “covered orders.”

Specifically, through this submission, the Exchange is proposing to require floor participants to record, in electronic systems designated by the Exchange, the following details

⁵ On February 9, 2005, the Exchange’s proposal to demutualize took effect. Under the Exchange’s new rules, the Exchange’s members are referred to as “participants.”

⁶ The proposed rule, for example, would require a floor broker who receives an order from another participant (whether the participant is on-floor or off-floor) to record detailed information relating to the order, any changes to the order, and its execution. Similarly, if a floor broker receives an order and then transmits it to another market, he would be required to record information not only about the order, but about its transmission to another market and any execution that it received in that market. The proposed rule change is designed to provide a complete record of the handling of orders received by the Exchange’s floor participants and, together with a recently-adopted rule, will provide a complete record of any orders sent by the Exchange’s floor participants to other trading venues. See Securities Exchange Act Release No. 52534 (September 29, 2005), 70 FR 58500 (October 6, 2005) (SR-CHX-2004-25) (rule change relating to a prohibition on using a layoff service unless the service provides required information to the Exchange).

about each covered order: (1) the symbol of the security; (2) the clearing participant; (3) an order identifier that uniquely identifies the order;⁷ (4) the identity of the participant recording the order details; (5) the number of shares or quantity of the security; (6) the side of the market (i.e., whether the order is a buy or sell order); (7) a designation of the order type (e.g., market, limit, stop, stop limit); (8) whether the order is agency or professional;⁸ (9) whether the order is being handled pursuant to Section 11(a)(1)(G) of the Act and any applicable rules thereunder; (10) whether the order is short or short exempt; (11) whether the order is a bona fide arbitrage order; (12) any limit price and/or stop price; (13) the date and time of order receipt or transmission (as applicable); (14) the market, off-floor firm, or on-floor participant to which the order was transmitted or from which the order was received (if applicable); (15) the order's time in force; (16) any designation as held or not held; (17) any special conditions or instructions (e.g., any customer display or do-not-display instructions or any all-or-none conditions); (18) any modifications that are made to the details set out in (1) through (17) or (20) below, for all or part of the order, or any cancellation of all or part of the order; (19) the date and time of receipt or transmission of any modifications to, or cancellation of, the order; (20) the date and time of any order expiration; (21) the identity of the party cancelling or modifying the order; (22) the transaction price, if applicable; (23) the number of shares executed, if applicable; (24) the date and time of execution, if applicable; (25) the contra party to the execution (if applicable); (26) the settlement instructions associated with the order, if applicable; (27) system-generated time(s) of recording required information; and (28) any other information that may be required by the

⁷ This order identifier does not change when modifications are made to the order, or when it is cancelled, allowing any changes to be tracked back to the original order.

⁸ The Exchange's rules define a "professional" order as one that is for the account of a broker-dealer, the account of an associated person of a broker-dealer, or any account in

Exchange from time to time.⁹ Floor participants would be required to record this information immediately after that information is received or becomes available.¹⁰

Proposed Interpretations and Policies .01 to .09 to the proposed rule change contain additional information about the information that participants must record and preserve. Among other things, these interpretations confirm that each required record of the time of an event must be expressed in terms of hours, minutes, and seconds. These interpretations also provide a definition of the term “order” and identify particular items of information that must be provided by participants who receive orders to buy and sell a security and immediately execute those orders.¹¹ The remaining interpretations note that participants will not be required to record

which a broker-dealer or an associated person of a broker-dealer has any direct or indirect interest. See CHX Article XXX, Rule 2, Interpretation and Policy .04.

⁹ See CHX Article XX, Proposed Rule 24(b).

¹⁰ See CHX Article XX, Proposed Rule 24(c).

¹¹ Proposed Interpretation and Policy .02 defines an order as “any written, oral or electronic instruction to effect a transaction.” This interpretation also notes that a decision by a co-specialist, market maker or floor broker to buy or sell securities for his or her own account on the floor of the Exchange would not constitute an order for purposes of the rule’s data recording requirements. This exception for principal trading on the Exchange’s floor is designed to recognize that all necessary information about a floor participant’s own trading is already captured by the Exchange’s trade reporting systems.

Proposed Interpretation and Policy .07 confirms that a floor participant who receives orders to buy and sell the same security and who executes those orders in full immediately upon receipt, would be required to record information only about the security’s symbol, the clearing organization, the identity of the participant firm recording the order details, whether the order is short or short exempt, whether the order is being handled pursuant to Section 11(a)(1)(G) of the Act, the transaction price, the number of shares executed, the date and time of execution, settlement instructions, the contra side to the execution, a system-generated time of recording the required information and any other information required from the Exchange from time to time. This requirement is designed to recognize that the Exchange currently believes that it may not be necessary for the Exchange’s participants to record detailed order information about orders that are immediately executed; at the same time, however, the Exchange has retained the ability (through paragraph (b)(28)) to require participants to provide additional information

information with respect to orders sent or received through the Exchange's MAX® system or through any other electronic systems that the Exchange recognizes as providing the required information in an acceptable format and set out two limited exceptions to the data-recording requirements.¹²

The Exchange believes that these proposed requirements appropriately permit the Exchange to collect the electronic information needed to conduct automated surveillance of its participants' trading activities.¹³ The Exchange has worked to tailor the rules so that they require participants to record and retain information needed to conduct appropriate surveillance, without imposing unnecessary data-collection requirements.¹⁴ Moreover, the Exchange is working to

about those orders, including information that is set out in other provisions of paragraph (b).

¹² See Proposed Interpretations and Policies .04 (regarding orders sent and received through certain systems), .05 (regarding orders that the Exchange expressly recognizes as incompatible for entry into an Exchange system) and .06 (regarding bona fide arbitrage orders and orders to offset a transaction made in error). As set forth below in note 13, the Exchange believes that these exceptions are appropriately tailored to ensure that the Exchange's participants are not required to enter unnecessary information about orders, while still providing information necessary for the Exchange's surveillance efforts.

¹³ Moreover, this proposal is consistent with recommendations made by the independent consultant retained by the Exchange under its recent settlement agreement with the Commission. See Securities Exchange Act Release No. 48566 (September 30, 2003), Administrative Proceeding File No. 3-11282.

¹⁴ For example, Proposed Interpretation and Policy .04 recognizes that participants are not required to record information that is already captured by the Exchange's systems or by other systems that the Exchange expressly recognizes as providing the required data in an acceptable format. (The Exchange's MAX system already captures all of the information required by this rule). Other exceptions to the recording requirements – such as the exceptions for bona fide arbitrage orders and for orders offsetting transactions made in error – are designed to recognize participants' need to immediately execute certain types of orders, while still requiring prompt input of required order information to permit the Exchange to conduct appropriate surveillance. Finally, Proposed Interpretation and Policy .05 – a general provision that would allow the Exchange to identify specific types of orders that might be exempt from the data-recording requirements when they are incompatible for entry into Exchange systems – is designed to cover those rare situations

complete changes to its existing Brokerplex® system, so that that system can be used by CHX floor brokers and market makers to record all required order details.¹⁵ As a result, the Exchange's on-floor participants will not be required to develop their own data-recording systems in response to this rule.¹⁶

2. Statutory Basis

The CHX believes the proposal is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b).¹⁷ In particular, the CHX believes that the proposed rule change is consistent with Section 6(b)(5) of the Act in that it is designed to promote just and equitable principles of trade, to remove impediments and to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest by permitting the Exchange to require its participants to provide

where, due to unexpected consequences of unrelated systems changes or a software failure, participants cannot enter data about a particular type of order into the Exchange's systems for a limited period of time. This exception is not intended to allow participants to avoid the recording requirements of the rule; indeed, it requires participants to record as much information about these orders as possible. The Exchange anticipates that both it and its participants would work quickly to correct any software or systems problems that prevented some or all of the required information from being transmitted to, or received by, the Exchange.

¹⁵ The CHX has represented that these changes would not delay the implementation of the proposed rule change once approved by the Commission. Telephone conversation between Ellen J. Neely, President and General Counsel, CHX, and Richard Holley III, Special Counsel, Division of Market Regulation, Commission, on September 16, 2005. The Exchange's Brokerplex system currently can be used by CHX floor brokers to manage their orders, route orders to the Exchange's co-specialists for execution and report executed trades.

¹⁶ The Exchange's staff will present to the Exchange's Board of Directors a separate rule that confirms the record-keeping obligations of its off-floor participants.

¹⁷ 15 U.S.C. 78f(b).

the Exchange with data necessary to conduct appropriate surveillance of its participants' trading activities.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition.

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

Written comments were neither solicited nor received by the Exchange.

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 self-regulatory organization consents, the Commission will:

- (A) by order approve such proposed rule change, as amended, or
- (B) institute proceedings to determine whether the proposed rule change, as amended, 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, 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. Please include File Number SR-CHX-2004-38 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 No. SR-CHX-2004-38. 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 such filing will also be available for inspection and copying at the principal office of the CHX. 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 No. SR-CHX-2004-38 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.¹⁸

Jonathan G. Katz
Secretary

¹⁸ 17 CFR 200.30-3(a)(12).