

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 also will be available for inspection and copying at the principal office of the CBOE. 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-2006-82 and should be submitted on or before November 20, 2006.

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

Nancy M. Morris,  
Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54642; File No. SR-CHX-2006-30]

### Self-Regulatory Organizations; Chicago Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change To Permit Routing From the Matching System to a Destination Selected by a Participant

October 23, 2006.

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 October 19, 2006, 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. 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 CHX proposes to amend its rules to permit its participants to identify a

destination to which an order should be routed when its execution would improperly trade through other markets or its display would improperly lock or cross other markets. The text of the proposed rule change appears below. Additions are *italicized*; deletions are [bracketed].

#### RULES OF CHICAGO STOCK EXCHANGE, INC.

##### ARTICLE 20

##### Prevention of Trade-Throughs

\* \* \* \* \*

RULE 5.a. An inbound order for at least a round lot is not eligible for execution on the Exchange if its execution would cause an improper trade-through of another ITS market or, when Reg NMS is implemented for a security, if its execution would be improper under Rule 611 (but not including the exception set out in Rule 611(b)(8)) (together an "improper trade-through"). As described in Interpretation and Policy .03, if the execution of all or part of an inbound order for at least a round lot on the Exchange would cause an improper trade-through, that order (or the portion of that order that would cause a trade-through) shall be routed to another appropriate market or, if designated as "do not route," automatically cancelled; provided, however, that if an undisplayed order is resting in the Matching System and the execution of an inbound round lot order (that is not an IOC or FOK order) against the undisplayed resting order would cause an improper trade-through, the resting order shall be cancelled to the extent necessary to allow the inbound order to be executed or quoted.

b. Inbound odd lot orders and odd lot crosses shall be eligible for execution on the Exchange even if the execution would trade through another market's bid or offer.

##### \* \* \* Interpretations and Policies:

\* \* \* \* \*

.03 Routing to other markets when execution in Matching System would cause a trade-through. *As described above, an inbound round lot order is not eligible for execution on the Exchange if its execution would cause an improper trade-through of another market's quotations. If the execution of all or a part of an inbound round-lot order on the Exchange would cause an improper trade-through, that order (or a portion of that order) shall be routed to another destination or, if designated as "do not route," automatically cancelled. Routing to other destinations ("Routing Services") shall occur as follows:*

*a. Cross with satisfy/outbound ISO. If a Participant has submitted a cross with satisfy or an outbound ISO and its execution would cause an improper trade-through, the Matching System shall execute that order and simultaneously route orders or commitments necessary to satisfy the bids or offers of other markets [(the "Routing Services")]. The Exchange's systems will determine when, how and where these orders (or commitments) should be routed. These orders will be routed, at the Participant's election, either through the NMS Linkage System (or any later linkage that supersedes the NMS Linkage System) or through the connectivity provided by a routing services provider with whom the Exchange has negotiated an access agreement.*

*b. All other situations. In all other situations, if the execution of all or a part of an inbound round lot order would cause a trade-through, and the Participant has not identified the order as "do not route," the Matching System shall route the order to another venue, according to each Participant's instructions. The Participant will be responsible for ensuring that it has a relationship with its chosen destination to permit the requested access. The Exchange shall not have responsibility for the handling of the order by the other destination, but will report any execution or cancellation of the order by the other destination to the Participant that submitted the order and will notify the other venue of any cancellations or changes to the order submitted by the order-sending Participant.*

*c [a]. The Exchange will provide its Routing Services pursuant to the terms of three separate agreements, to the extent that they are applicable to a specific routing decision: (1) an agreement between the Exchange and each Participant on whose behalf orders will be routed ("Participant-Exchange Agreement"); (2) an agreement between each Participant and a specified third-party broker-dealer that will use its routing connectivity to other markets and serve as a "give-up" in those markets ("Give-Up Agreement"); and (3) an agreement between the Exchange and the specified third-party broker-dealer ("Routing Connectivity Agreement") pursuant to which the third-party broker-dealer agrees to provide routing connectivity to other markets and serve as a "give-up" for the Exchange's Participants in other markets. The Routing Connectivity Agreement will include terms and conditions that enable the Exchange to comply with this Interpretation and Policy .03.*

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

<sup>14</sup> 15 U.S.C. 78s(b)(1).

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

d [b]. The Exchange will provide Routing Services in compliance with these rules and with the provisions of the Act and the rules thereunder, including, but not limited to, the requirements of sections 6(b)(4) and (5) of the Act that the rules of a national securities exchange provide for the equitable allocation of reasonable dues, fees and other charges among its members and issuers and other persons using its facilities, and not be designed to permit unfair discrimination between customers, issuers, brokers or dealers.

[c. In providing the Routing Services, the Exchange will use its own systems to determine when, how and where orders (or commitments) are routed away to other markets.]

[d. The Routing Connectivity Agreement will include terms and conditions that enable the Exchange to comply with this Interpretation and Policy .03.]

e. The Exchange will establish and maintain procedures and internal controls reasonably designed to adequately restrict the flow of confidential and proprietary information between the Exchange (including its facilities) and the third-party broker-dealer, and, to the extent the third-party broker-dealer reasonably receives confidential and proprietary information, that adequately restrict the use of such information by the third party broker-dealer to legitimate business purposes necessary to provide routing connectivity and to serve as a "give-up."

[(In addition to these Routing Services, the Exchange is developing a functionality that would, in all other situations where the execution of all or a part of an inbound order for at least a round lot would cause a trade-through, and the Participant has not identified the order as "do not route," route all or a part of the order to another destination, according to each Participant's instructions. This functionality will only be implemented if these rules are amended to define the functionality in more detail).]

\* \* \* \* \*

#### Locked and Crossed Markets

RULE 6. a.–c. No change to text.

d. Matching System operation. Except as permitted in paragraph (c) above, an order is not eligible for display on the Exchange if its display would improperly lock or cross the ITS best bid or offer, or, when Reg NMS is implemented for a security, if its display would lock or cross a protected quotation. These orders shall be routed, pursuant to the provisions of Rule 5, Interpretation .03 above, to another

destination of the Participant's choice [appropriate market] or, if designated as "do not route," automatically cancelled.

\* \* \* \* \*

## 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 on the proposed rule change. 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

Under the Exchange's new trading model rules, the Exchange's Matching System will not execute an order if its execution would cause an improper trade-through of another ITS market or, when Regulation NMS is implemented, if its execution would be improper under Rule 611 of Regulation NMS<sup>3</sup> (together an "improper trade-through").<sup>4</sup> Similarly, the Exchange's Matching System will not display an order if its display would improperly lock or cross other markets.<sup>5</sup>

Through this proposal, the Exchange seeks to adopt rules that would allow the Exchange, in these situations, to either cancel the order back to the participant that submitted it or to route the order to the destination of the participant's choice, all at the direction of the participant. Under this proposal, the participant would be responsible for ensuring that it has a relationship with its chosen destination to permit the requested access.<sup>6</sup> The Exchange would not be involved in the execution of the order—any execution of the order would be the responsibility of the destination to which the order was sent. The Exchange, however, would report any execution or cancellation of the order by the other destination to the participant that submitted the order and would notify the other venue of any cancellations or changes to the order submitted by the order-sending

<sup>3</sup> 17 CFR 242.611.

<sup>4</sup> See CHX Article 20, Rule 5.

<sup>5</sup> See CHX Article 20, Rule 6.

<sup>6</sup> See CHX Article 20, Rule 5, proposed Interpretation and Policy .03(b).

participant.<sup>7</sup> The Exchange would provide these routing services pursuant to these proposed rules and a separate agreement between the Exchange and each participant on whose behalf orders would be routed.<sup>8</sup>

The Exchange believes that the proposed routing of orders as set forth above would be a facility of the Exchange, but that the destinations chosen by each participant would not constitute an Exchange facility. As a result, the Exchange would submit fee changes, and any applicable changes to its rules, to the Commission as required by Rule 19b-4 under the Act in connection with its routing.<sup>9</sup> The Exchange's rules and fees, however, would not address the fees or manner of operation of any destination to which the participant asked that an order be routed. Additionally, the Exchange would provide these routing services in compliance with its rules and with the provisions of the Act and the rules thereunder, including, but not limited to, the requirements of Sections 6(b)(4) and (5) of the Act,<sup>10</sup> which require that the rules of a national securities exchange provide for the equitable allocation of reasonable dues, fees and other charges among its members and issuers and other persons using its facilities, and not be designed to permit unfair discrimination between customers, issuers, brokers or dealers.<sup>11</sup>

#### 2. Statutory Basis

The CHX believes that 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).<sup>12</sup> The CHX believes that the proposal is consistent with Section 6(b)(5) of the Act<sup>13</sup> in that it is designed 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 by confirming that, when the execution of an order would improperly trade through another market (or the display of an order would improperly lock or cross another market), the Exchange may follow a participant's instructions

<sup>7</sup> See CHX Article 20, Rule 5, proposed Interpretation and Policy .03(b).

<sup>8</sup> See CHX Article 20, Rule 5, proposed Interpretation and Policy .03(c).

<sup>9</sup> 17 CFR 240.19b-4.

<sup>10</sup> 15 U.S.C. 78f(b)(4)–(5).

<sup>11</sup> See CHX Article 20, Rule 5, proposed Interpretation and Policy .03(d).

<sup>12</sup> 15 U.S.C. 78f(b).

<sup>13</sup> 15 U.S.C. 78f(b)(5).

in either cancelling the order back to the participant or routing the order to a destination of the participant's choice.

#### *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.

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

No written comments were either solicited or received.

### **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 such 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](mailto:rule-comments@sec.gov). Please include File Number SR-CHX-2006-30 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-2006-30. 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-2006-30 and should be submitted on or before November 20, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Nancy M. Morris,**

*Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-54644; File No. SR-ISE-2004-17]

### **Self-Regulatory Organizations; International Securities Exchange, Inc.; Order Approving a Proposed Rule Change and Amendment No. 1 Thereto Relating to Market Maker Orders**

October 23, 2006.

#### **I. Introduction**

On May 26, 2004, the International Securities Exchange, Inc. ("ISE" 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 eliminate the restriction on Electronic Access Members ("EAMs") representing ISE market maker orders, provided that such orders are identified as orders for the account of an ISE market maker. The Exchange filed Amendment No. 1 with

the Commission on August 14, 2006.<sup>3</sup> The amended proposal was published for comment in the **Federal Register** on September 14, 2006.<sup>4</sup> The Commission received no comments on the proposal. This order approves the proposal, as amended.

#### **II. Description of the Proposal**

The Exchange proposes to amend ISE Rule 717(g) to eliminate the restriction on EAMs representing ISE market maker orders, provided that such orders are identified as orders for the account of an ISE market maker. Currently, under ISE Rules, EAMs generally are not permitted to represent orders for the account of an ISE market maker. In its filing with the Commission, the Exchange stated that it initially included this restriction in its rules due to a system limitation. Specifically, allowing ISE market makers to enter orders through another member instead of directly might have created an opportunity for ISE market makers to avoid certain limitations on market maker trading contained in the Exchange's Rules.<sup>5</sup>

The Exchange represents that it has developed the capability for EAMs to mark orders to show that they are for the account of an ISE market maker. A marked order can be tracked through the Exchange's surveillance system as if it were directly entered by the market maker. Therefore, the Exchange proposes to eliminate the prohibition against EAMs entering orders for the account of ISE market makers in most circumstances. However, the proposal would continue to prohibit an EAM from entering an order solicited from an ISE market maker into the Solicited Order Mechanism and the Price Improvement Mechanism—functionalities that are designed to expose solicited transactions to the market—if the market maker is assigned to the options class that is the subject of the order.<sup>6</sup>

#### **III. Discussion**

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the

<sup>3</sup> Amendment No. 1 replaced and superceded the original filing in its entirety.

<sup>4</sup> See Securities Exchange Act Release No. 54415 (September 7, 2006), 71 FR 54321.

<sup>5</sup> See, e.g., ISE Rule 805 (Market Maker Orders).

<sup>6</sup> This limitation on entering orders solicited from market makers assigned to the options class was included in a rule change by the CBOE (the "Automated Improvement Mechanism" or "AIM") recently approved by the Commission. See Securities Exchange Act Release No. 53222 (Feb. 3, 2006), 71 FR 7089 (Feb. 10, 2006). The execution of solicited transactions through AIM is similar to the execution of orders through the ISE's Price Improvement Mechanism.

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

<sup>27</sup> 17 CFR 240.19b-4.