

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-58221; File No. SR-BSE-2008-29)

July 24, 2008

Self-Regulatory Organizations; Boston Stock Exchange, Inc.; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change Relating to Doing Business with the Public

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 July 14, 2008, the Boston Stock Exchange, Inc. (the “Exchange” or “BSE”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been substantially prepared by the Exchange. This order provides notice of the proposed rule change and approves the proposed rule change on an accelerated basis.

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

The Exchange is proposing to amend certain rules that govern an Exchange member’s conduct of doing business with the public. Specifically, the proposed rule change would require participants to integrate the responsibility for supervision of their public customer options business into their overall supervisory and compliance programs. In addition, the proposal would require members to strengthen their supervisory procedures and internal controls as related to their public customer options business. The text of the proposed rule change is available at the Exchange, the Commission’s Public

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

Reference Room, and at

<http://www.bostonstock.com/BostonstockPDF/Legal/filings/2008-29.pdf>.

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

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

a. Integration of Options Supervision

The purpose of the proposed rule change is to create a supervisory structure for options that is similar to that required by New York Stock Exchange, LLC (“NYSE”) Rule 342 and National Association of Securities Dealers, Inc. (“NASD”) (n/k/a Financial Industry Regulatory, Inc. (“FINRA”)) Rule 3010. The proposed rule change would also conform Boston Options Exchange Group, LLC (“BOX”) rules to those of the Chicago Board Options Exchange, Incorporated (“CBOE”), which has recently eliminated the requirement that participants qualified to do a public customer business in options designate a single person to act as a Senior Registered Options Principal (“SROP”) for the participant and that each such participant designate a specific individual as a Compliance Registered Options Principal (“CROP”).³ Instead, the rule requires

³ See Securities Exchange Act Release No. 56492 (September 21, 2007) 72 FR 54952 (September 27, 2007) (SR-CBOE-2007-106) (approval order).

participants to integrate the SROP and CROP functions into their overall supervisory and compliance programs.

The SROP concept was first introduced during the early years of development of the listed options market. Previously, participants were required to designate one or more persons qualified as Registered Options Principals (“ROPs”) to have supervisory responsibilities with respect to the firms’ options business. As the number of ROPs at larger firms began to increase, an additional requirement was imposed that firms designate one of their ROPs as the SROP. This was intended to eliminate confusion as to where the compliance and supervisory responsibilities lay by centralizing in a single supervisory officer overall responsibility for the supervision of a firm’s options activities.⁴ Subsequently, following the recommendation of the Special Study, the options exchanges required firms to designate a CROP to be responsible for each firm’s overall compliance program with respect to its options activities.⁵ The CROP could be the same person designated as a SROP, but while the CROP generally was not permitted to have sales functions in the firm, the SROP was not so restricted.

Since the SROP and CROP requirements were first imposed, the supervisory function with respect to options activities of most securities firms has been integrated into the matrix of supervisory and compliance functions in respect of the firms’ other securities activities. This not only reflects the maturity of the options market, but also recognizes the ways in which the uses of options themselves have become more

⁴ Securities and Exchange Commission, 96th Cong., 1st Sess., Report of the Special Study of the Options Markets (Comm. Print 1978) (“Special Study”) p. 316 fn. 11.

⁵ Id. at 335.

integrated with other securities in the implementation of particular strategies. To further reflect the trend toward integration, and to conform BOX rules to the recently amended FINRA rules, the proposed change designates all options principals as Registered Options and Security Futures Principals (“ROSFPs”).⁶ By permitting supervision of a firm’s options activities to be handled in the same manner as the supervision of its securities and futures activities, the proposed rule change would ensure that supervisory responsibility over each segment of a firm’s business is assigned to the best qualified persons in the firm, thereby enhancing the overall quality of supervision and compliance.

The proposed rule change would allow firms the flexibility to assign such supervisory and compliance responsibilities, which formerly resided with the SROP and/or CROP, to more than one individual. For example, the proposed rule change would permit a participant firm to designate certain ROSFPs to be responsible for a variety of supervisory compliance functions such as approving acceptance of discretionary accounts⁷ and exceptions to a participant firm’s suitability standards for trading uncovered short options.⁸ A firm would be likely to do this in instances where it believes it advantageous to do so to enhance its supervisory or compliance structure. Typically, a firm may also wish to divide these functions on the basis of geographic region or functional considerations. BOX Rule, Chapter XI, Sec. 2 would be amended to

⁶ See Securities Exchange Act Release No. 57775 (May 5, 2008) 73 FR 26453 (May 9, 2008) (SR-FINRA-2007-035) (approval order). See also Securities Exchange Act Release No. 56663 (October 15, 2002) 67 FR 64944 (October 22, 2002) (approval order) (modifying and broadening NASD registration categories to include security futures activities by, among other things, amending the title of the Series 4 registration to Registered Options and Security Futures Principal).

⁷ See proposed BOX Rule Chapter XI, Sec. 12.

⁸ See proposed BOX Rule Chapter XI, Sec. 9(f)(iii).

clarify the qualification requirements of individuals designated as ROSFPs.⁹ BOX Rule, Chapter XI, Sec. 3 would be amended to specify the registration requirements of individuals who accept orders from non-broker-dealer customers.¹⁰

The proposed rule change would require options discretionary accounts to be accepted by individuals who are qualified ROSFPs. The proposed rule change would eliminate the requirement that discretionary options orders be approved on the day of entry by a ROSFP (with one exception as discussed below). This requirement predates the Special Study and is not consistent with the use of supervisory tools in computerized format or exception reports after the close of a trading day. No similar requirement exists for supervision of other securities accounts that are handled on a discretionary basis.¹¹ Discretionary orders must be reviewed in accordance with a participant's written supervisory procedures. The proposed rule change would ensure that supervisory responsibilities are assigned to specific ROSFP-qualified individuals, thereby enhancing the quality of supervision.

BOX Rule, Chapter XI, Sec. 12 would be revised by adding the requirement that any participant that does not utilize computerized surveillance tools for the frequent and appropriate review of discretionary account activity must establish and implement procedures to require ROSFP-qualified individuals who have been designated to review discretionary accounts to approve and initial each discretionary order on the day entered. The Exchange believes that any firm that does not utilize computerized surveillance tools

⁹ See proposed BOX Rule Chapter XI, Sec.2 (d) and (e).

¹⁰ See proposed BOX Rule Chapter XI, Sec. 3(d).

¹¹ See, e.g., NYSE Rule 408.

to monitor discretionary account activity should continue to be required to perform the daily manual review of discretionary orders.

Under the proposed rule change, firms would continue to be required to designate ROSFP-qualified individuals to provide frequent appropriate supervisory review of options discretionary accounts. This includes a review of the accounts in order to determine whether the ROSFP accepting the account had a reasonable basis for believing that the customer was able to understand and bear the risks of the proposed strategies or transactions. This requirement would provide an additional level of supervisory audit over options discretionary accounts that do not exist for other securities discretionary accounts.

In addition, the proposed rule change would require that each participant submit to the Exchange a written report by April 1 of each year that details the participant's supervision and compliance effort, including its options compliance program, during the preceding year and reports on the adequacy of the participant's ongoing compliance processes and procedures.¹²

Proposed BOX Rule Chapter XI, Sec. 10(h) would require that each participant submit, by April 1 of each year, a copy of the BOX Rule Chapter XI, Sec. 10(g) annual report to one or more of its control persons or, if the participant has no control person, to the audit committee of its board of directors or its equivalent committee or group.¹³

Further, the proposed rule would provide that a participant that specifically includes its

¹² See proposed BOX Rule, Chapter XI, Sec. 10(g), which is modeled after NYSE Rule 342.30.

¹³ See proposed BOX Rule, Chapter XI, Sec. 10(h), which is modeled after NYSE Rule 354.

options compliance program in a report that complies with substantially similar NYSE and NASD rules would be deemed to have satisfied the requirements of BOX Rules, Chapter XI, Sec. 10(g) and (h).

Participants would be required to designate a single general partner or executive officer to assume overall authority and responsibility for internal supervision, control of the organization and compliance with securities laws and regulations.¹⁴ Participants would also be required to designate specific qualified individuals as having supervisory or compliance responsibilities over each aspect of the firm's options activities and to set forth the names and titles of these individuals in their written supervisory procedures.¹⁵

The Exchange believes the proposed rule changes would increase accountability and eliminate impractical and unrealistic supervisory standards applicable solely to listed options. The Exchange believes that the proposed rule changes are appropriate and would not materially alter the supervisory operations of firms.

b. Supervisory Procedures and Internal Controls

The Exchange is also proposing to amend certain rules to strengthen participants' supervisory procedures and internal controls relating to a participant's public customer options business. The proposed rule changes discussed below are modeled after NYSE and NASD rules approved by the Commission in 2004.¹⁶ This proposal is appropriate and consistent with the proposal discussed above to integrate the responsibility for

¹⁴ See proposed BOX Rule, Chapter XI, Sec. 10(a).

¹⁵ See proposed BOX Rule, Chapter XI, Sec. 10(i).

¹⁶ See Securities Exchange Act Release Nos. 49882 (June 17, 2004), 69 FR 35108 (June 23, 2004) (SR-NYSE-2002-36 (approval order), 49883 (June 17, 2004), 69 FR (June 23, 2004)(SR-NASD-2002-162) (approval order).

supervision of a participant firm's public customer options business into its overall supervisory and compliance program.

The Exchange is proposing to revise BOX Rule, Chapter XI, Sec. 10(a) to require the development and implementation of written policies and procedures reasonably designed to supervise sales managers and other supervisory personnel who service customer options accounts.¹⁷ This requirement would apply to branch office managers, sales managers, regional/district sales managers, or any person performing a similar supervisory function. Such policies and procedures are expected to encompass all options sales-related activities. Proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(i) would require that supervisory reviews of producing sales managers be conducted by a qualified ROSFP who is either senior to, or otherwise "independent of," the producing manager under review. This provision is intended to ensure that all options sales activity of a producing manager is monitored by persons who do not have a personal interest in such activity.

Proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(ii) would provide an exception for participants so limited in size and resources that there is no qualified person senior to, or otherwise independent of, the producing manager to conduct the review. In this case, the review would be conducted by a qualified ROSFP to the extent practicable. Under proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(iii), a participant relying on the limited size and resources exception must document the factors used to determine that compliance with each of the "senior" or "otherwise independent" standards of proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(i) is not possible, and that the required supervisory

¹⁷ Proposed BOX Rule, Chapter XI, Sec. 10(a) is modeled after NYSE Rule 342.19.

systems and procedures in place, with respect to any producing manager, comply with the provisions of proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(i) to the extent practical.¹⁸

Proposed BOX Rule, Chapter XI, Sec. 10(c)(1) would require participants to develop and maintain adequate controls over each of their business activities. The proposed rule would further require that such controls include the establishment of procedures to independently verify and test the supervisory systems and procedures for those business activities. A participant would be required to include in the annual report, prepared pursuant to proposed BOX Rule, Chapter XI, Sec. 10(g), a review of the participant's efforts in this regard, including a summary of the tests conducted and significant exceptions identified. The Exchange believes proposed BOX Rule, Chapter XI, Sec. 10(c)(1) would enhance the overall quality of each participant's supervision and compliance function.¹⁹

Proposed BOX Rule, Chapter XI, Sec. 10(d) would establish requirements for branch office inspections similar to the requirements of NYSE Rule 342.24. Specifically BOX Rule, Chapter XI, Sec. 10(d) would require a participant to inspect, at least annually, each supervisory branch office and inspect each non-supervisory branch office at least once every three years.²⁰ The proposed rule would further require persons who

¹⁸ Proposed BOX Rule, Chapter XI, Sec. 10(a)(3)(iv) would provide that a participant that complies with the NYSE or NASD rules that are substantially similar to the requirements in BOX Rules, Chapter XI, Secs. 10(a)(3)(1) and (a)(3)(2) and (a)(3)(3) will be deemed to have met such requirements.

¹⁹ Proposed BOX Rule, Chapter XI, Sec. 10(c)(1) is modeled after NYSE Rule 342.23. Paragraph (c)(2) of proposed BOX Rule, Chapter XI, Sec. 10(c)(1) would provide that a participant complies with NYSE or NASD rules that are substantially similar to the requirements in paragraph (c)(1) of proposed BOX Rule, Chapter XI, Sec 10 will be deemed to have met such requirements.

²⁰ Proposed BOX Rules, Chapter XI, Secs. 10(d)(1)(i) and (ii) would provide

conduct a participant's annual branch office inspection to be independent of the direct supervision or control of the branch office (i.e., not the branch office manager, or any person who directly or indirectly reports to such manager, or any person to whom such manager directly reports). The Exchange believes that requiring branch office inspections to be conducted by someone who has no significant financial interest in the success of a branch office should lead to more objective and vigorous inspections.

Under proposed BOX Rule, Chapter XI, Sec. 10(e), any firm seeking an exemption, pursuant to BOX Rule, Chapter XI, Sec. 10(d)(1)(ii), from the annual branch office inspection requirement would be required to submit to the Exchange written policies and procedures for systematic risk-based surveillance of its branch offices, as defined in BOX Rule, Chapter XI, Sec. 10(e). Proposed BOX Rule, Chapter XI, Sec. 10(f) would require the annual branch office inspection program to include, at a minimum, testing and verification of specified internal controls.²¹ Proposed BOX Rule, Chapter XI, Sec. 10(d)(3) would provide that a participant that complies with the requirements of NASD or the NYSE that are substantially similar to the requirements of BOX Rule, Chapter XI, Sec. 10(d)(e) and (f) would be deemed to have met such requirements. The Exchange is also proposing to amend BOX Rule, Chapter XI, Sec. 10 to define "branch office" in a way that is substantially similar to the definition of branch office in NYSE Rule 342.10.

members with two exceptions from the annual supervisory branch office inspection requirements.

²¹ Proposed BOX Rule, Chapter XI, Sec. 10(f) is modeled after NYSE Rules 342.25 and 342.26.

Proposed BOX Rule, Chapter XI, Sec. 10(g)(4) would require a firm to designate a Chief Compliance Officer (CCO). Proposed BOX Rule, Chapter XI, Sec. 10(g)(5) would require each firm's Chief Executive Officer (CEO), or equivalent, to certify annually that the participant organization has in place processes to: (1) establish and maintain policies and procedures reasonably designed to achieve compliance with applicable Exchange rules and federal securities laws and regulations, (2) modify such policies and procedures as business, regulatory, and legislative changes and events dictate, and (3) test the effectiveness of such policies and procedures on a regular basis, the timing of which is reasonably designed to ensure continuing compliance with Exchange rules and federal securities laws and regulations.²²

Proposed BOX Rule, Chapter XI, Sec. 10(g)(5) would also require the CEO to attest (1) that the CEO has conducted one or more meetings with the CCO in the preceding 12 months to discuss the compliance processes in proposed BOX Rule, Chapter XI, Sec. 10(g)(5)(i), (2) that he or she has consulted with the CCO and other officers to the extent necessary to attest to the statements in the certification, and (3) that the compliance processes are evidenced in a report, reviewed by the CEO, CCO and such other officers as the participant firm deems necessary to make the certification, that is provided to the participant firm's board of directors and audit committee (if such committee exists).

Under proposed BOX Rule, Chapter XI, Sec. 10(b)(2)(g), a participant, upon a customer's written instructions, may hold mail for a customer who will not be at his or her usual address for no longer than two months if the customer is on vacation or

²² Proposed BOX Rule, Chapter XI, Sec. 10(g)(5) is modeled after NASD Rule 3013 and NYSE Rule 342.30(e).

traveling, or for three months if the customer is going abroad. This provision would help ensure that participants that hold mail, for customers who are away from their usual addresses, do so only pursuant to the customer's written instructions and for a specified, relatively short period of time.²³

Proposed BOX Rule, Chapter XI, Sec. 10(b)(3) would require that, before a customer options order is executed, the account name or designation must be placed upon the memorandum for each transaction. In addition, only a qualified ROSFP would be permitted to approve any changes in account names or designations. The ROSFP would be required to document the essential facts relied upon in approving the changes and maintain the record in an easily accessible place. A participant would be required to preserve any documentation which provides for an account designation change for a period of not less than three years, with the documentation preserved for the first two years in an easily accessible place, as the term "easily accessible place" is used in Rule 17a-4 of the Act. The Exchange believes the proposed rule would help to protect account name and designation information from possible fraudulent activity.²⁴

Proposed BOX Rule, Chapter XI, Sec. 12(d) would allow a participant to exercise time and price discretion on orders for the purchase or sale of a definite number of options contracts in a specified security. The Exchange proposes to limit the duration of this discretionary authority to the day it is granted, absent written authorization to the contrary. Additionally, the proposed rule would require any exercise of time and price

²³ Proposed BOX Rule, Chapter XI, Sec. 10(b)(2)(g) is modeled after NASD Rule 3110(i).

²⁴ Proposed BOX Rule, Chapter XI, Sec. 10(b)(3) is modeled after NASD Rule 3110(j).

discretion to be reflected on the customer order ticket. The proposed one-day limitation would not apply to time and price discretion exercised for orders effected with or for an institutional account (as defined in the Rule) pursuant to valid Good-Till-Cancelled instructions issued on a “not held” basis. The Exchange believes that investors will receive greater protection by clarifying the time such discretionary orders may remain pending.²⁵

The Exchange believes the proposed rule changes recognize that options have become more integrated with other securities in the implementation of particular strategies, and thus should not continue to be regulated as though they are a new and experimental product. The Exchange further asserts that the supervisory and compliance structure in place for non-options products at most participant firms is not materially different from the structure in place for options. The proposed rule change would also provide conformity of the BOX Rules to those of the CBOE. Accordingly, the Exchange submits that the proposed rule changes are appropriate and would not materially alter the supervisory operations of participants.

2. Statutory Basis

The Exchange believes that the proposal is consistent with the requirements of Section 6(b) of the Act,²⁶ in general, and Section 6(b)(5) of the Act,²⁷ in particular, in that it will result in consistency and uniformity among the competing options exchanges and it is designed to promote just and equitable principles of trade, to

²⁵ Proposed BOX Rule, Chapter XI, Sec. 12(d) is modeled after NASD Rule 2510(d)(1).

²⁶ 15 U.S.C. 78f(b).

²⁷ 15 U.S.C. 78f(b)(5).

prevent fraudulent and manipulative acts, 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. Specifically, the Exchange believes this proposed rule change would achieve these ends by integrating the supervision and compliance functions relating to participants' public customer options activities into their overall supervisory structure, thereby eliminating any uncertainty over where supervisory responsibility lies, and by fostering the strengthening of participant organizations' internal controls and supervisory systems.

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

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

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

The Exchange has neither solicited nor received comments on the proposed rule change.

III. 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-BSE-2008-29 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-BSE-2008-29. 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, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of BSE, located at 100 Franklin Street, Boston, MA 02110. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-BSE-2008-29 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission Findings

The Commission has carefully reviewed the proposed rule change and finds that it is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.²⁸ In particular, the Commission believes that the proposed rule change would help to better integrate the supervisory and compliance functions of a firm's public customer options activities into the firm's overall supervisory and compliance functions, thereby eliminating any uncertainty about where supervisory responsibility lies. Therefore, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,²⁹ which requires, among other things, that Exchange rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The Commission also finds good cause to approve the proposed rule change prior to the thirtieth day after the date of publication of notice of filing in the Federal Register. The proposed rule change is substantially similar to recent CBOE and FINRA rule amendments concerning options supervision, which were approved by the Commission.³⁰ The Commission believes that approving the proposed rule change will simplify firms' compliance, and is consistent with the public interest and the investor protection goals of

²⁸ In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

²⁹ 15 U.S.C. 78f(b)(4).

³⁰ See Securities Exchange Act Release No. 56971 (December 14, 2007), 72 FR 72804 (December 21, 2007) (approval order for File No. SR-CBOE-2007-106) and Securities Exchange Act Release No. 57775 (May 5, 2008) 73 FR 26453 (May 9, 2008) (approval order for File No. SR-FINRA-2007-035).

the Act. Finally, the Commission finds that it is in the public interest to approve the proposed rule change as soon as possible to expedite its implementation.

Accordingly, the Commission believes good cause exists, consistent with Sections 19(b)(2) of the Act,³¹ to approve the proposed rule change on an accelerated basis.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-BSE-2008-29) be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³²

Florence E. Harmon
Acting Secretary

³¹ 15 U.S.C. 78s(b)(2).

³² 17 CFR 200.30-3(a)(12).