

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48855; File No. SR-BSE-2003-07]

Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 1 Thereto by the Boston Stock Exchange, Inc. To Amend Its Listed Securities Requirements Relating to the Mandatory Establishment of Independent Audit Committees for All Listed Issuers

December 1, 2003.

I. Introduction

On July 16, 2003, the Boston Stock Exchange, Inc. ("BSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission"), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to add new requirements concerning audit committees to its Listed Securities Requirements in Section 10 of Chapter XXVII of the Rules of the Board of Governors of the BSE ("BSE Rules"). The proposed rule change would require each issuer listed on the BSE to establish an independent audit committee and to comply with other specified standards relating to audit committees, as mandated by section 10A(m) of the Act³ and Rule 10A-3 thereunder.⁴ The proposed rule change also includes certification, enforcement, and other compliance requirements, as well as a provision that sets forth the operative dates for the new requirements. The Exchange also committed to adopt additional listing policies and requirements pertaining to issuer corporate governance.

The proposed rule change was published for comment in the **Federal Register** on October 28, 2003.⁵ The Commission received no comments on the proposal. On November 19, 2003, the BSE submitted an amendment to the proposed rule change.⁶ This order

approves the proposal, publishes notice of Amendment No. 1, and approves Amendment No. 1 on an accelerated basis.⁷

II. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.⁸ Specifically, the Commission finds that the proposal relating to independent audit committees for listed companies is consistent with section 6(b)(5) of the Act,⁹ which requires, among other things, that the BSE's rules be designed to prevent fraudulent and manipulative acts and practices, and, in general, to protect investors and the public interest. Moreover, the Commission believes that the BSE's proposal to add the new requirements concerning audit committees is appropriate and consonant with section 10A(m) of the Act¹⁰ and Rule 10A-3 thereunder relating to audit committee standards for listed issuers. The Commission notes that the BSE intends to file an additional rule proposal relating to other corporate governance listing standards.¹¹

Furthermore, the Commission finds good cause, consistent with section 19(b)(2) of the Act,¹² to approve Amendment No. 1 to the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. In Amendment No. 1, the BSE expanded, with respect to investment companies, the scope of the proposed provision regarding complaint procedures. Rule 10A-3 requires audit committees to establish procedures for "the confidential, anonymous submission by employees of the listed issuer of concerns regarding questionable accounting or auditing matters."¹³ The amended BSE proposal would require that audit committees of investment

procedures for the confidential, anonymous submission of concerns regarding questionable accounting or auditing matters.

⁷ Rule 10A-3 requires each national securities exchange and national securities association to have rules that comply with its requirements approved by the Commission no later than December 1, 2003. By the Commission approving the proposed rule change, the Exchange can comply with this deadline.

⁸ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁹ 15 U.S.C. 78f(b)(5).

¹⁰ 15 U.S.C. 78j-1(m).

¹¹ See Notice at note .

¹² 15 U.S.C. 78s(b)(2).

¹³ 17 CFR 240.10A-3(b)(3)(ii).

companies also establish procedures for the confidential, anonymous submission of such concerns by employees of the investment adviser, administrator, principal underwriter, or any other provider of accounting related services for the investment company, as well as employees of the investment company. This revision responds to a recommendation by the Commission that self-regulatory organizations take into account, in adopting rules to comply with Rule 10A-3, the fact that most services are rendered to an investment company by employees of third parties, such as the investment adviser, rather than by employees of the investment company.¹⁴ In Amendment No. 1, the Exchange also made several technical revisions to the rule text. The Commission believes that it is appropriate to accelerate approval of this amendment, because it conforms the rule text to similar rules of the New York Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. that were approved by the Commission,¹⁵ and the amendment raises no new substantive issues.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 filings will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-BSE-2003-07 and should be submitted by December 26, 2003.

¹⁴ See Securities Act Release No. 8220, Securities Exchange Act Release No. 47654, and Investment Company Act Release No. 26001 (April 9, 2003), 68 FR 18788 (April 16, 2003) (release adopting Rule 10A-3).

¹⁵ See Securities Exchange Act Release Nos. 48745 (November 4, 2003), 68 FR 64154 (November 12, 2003) (approval of, among other proposals, File Nos. SR-NYSE-2002-33 and SR-NASD-2002-141).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78j-1(m).

⁴ 17 CFR 240.10A-3.

⁵ See Securities Exchange Act Release No. 48668 (October 21, 2003), 68 FR 61494 ("Notice").

⁶ See letter from John Boese, Vice President, Legal and Compliance, BSE, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated November 18, 2003 ("Amendment No. 1"). In Amendment No. 1, the BSE made minor, non-substantive changes to the text of the proposed rule and, with respect to investment companies, expanded the scope of the requirement that audit committees establish

IV. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹⁶ that Amendment No. 1 is approved on an accelerated basis, and that the proposed rule change (File No. SR-BSE-2003-07) be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁷

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48858; File No. SR-CBOE-2003-07]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Amendment No. 1 by the Chicago Board Options Exchange, Inc., Relating to the Trading of Ratio Orders

December 1, 2003.

I. Introduction

On February 24, 2003, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("Commission" or "SEC"), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to allow ratio orders to be executed through the CBOE. The CBOE filed Amendment No. 1 to the proposal on October 8, 2003.³

The proposed rule change and Amendment No. 1 were published for comment in the *Federal Register* on October 28, 2003.⁴ The Commission received no comments regarding the proposal. This order approves the proposed rule change, as amended.

II. Description of the Proposal

The CBOE proposes to amend CBOE Rule 6.53, "Certain Types of Orders Defined," to allow ratio orders with certain permissible ratio limits, as

defined below, to be executed through the CBOE. In addition, the CBOE proposes to revise paragraph (e) of CBOE Rule 6.45, "Priority of Bids and Offers—Allocation of Trades," to include these types of permissible ratio orders in CBOE Rule 6.45(e), thereby providing such ratio orders with the exception to the priority rules that CBOE Rule 6.45(e) provides currently for spread, straddle, and combination orders.⁵ The CBOE believes that because ratio orders are slight variations on the types of complex orders currently permitted on the CBOE, it is appropriate to treat ratio orders like spread, straddle, and combination orders for purposes of CBOE Rule 6.45(e).

CBOE Rule 6.53 lists and defines several types of orders that are executed through the CBOE including, among others, three types of complex orders: spread orders, combination orders, and straddle orders. The CBOE proposes to add certain ratio orders within permissible established limits to the list of orders included in CBOE Rule 6.53. CBOE Rule 6.53(n) would define a ratio order as either a spread, straddle, or combination order in which the stated number of option contracts to buy (sell) is not equal to the stated number of option contracts to sell (buy), provided that the number of contracts differs by a permissible ratio. Under CBOE Rule 6.53(n), a permissible ratio would be any ratio that is equal to or greater than one-to-three (.333) or less than or equal to three-to-one (3.0). For example, a one-to-two (.5) ratio, a two-to-three (.667) ratio, or a two-to-one (2.0) ratio is permissible, whereas a one-to-four (.25) ratio or a four-to-one (4.0) ratio is not.

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange⁶ and, in particular, with the requirements of section 6(b)(5) of the

Act,⁷ which requires, among other things, that the rules of a national securities exchange be 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 to protect investors and the public interest.

The proposal will allow certain ratio orders to be executed through the CBOE. As described above, a ratio order is a spread, straddle, or combination order in which the stated number of option contracts to buy (sell) is not equal to the stated number of option contracts to sell (buy), provided that the number of contracts differs by a permissible ratio.⁸ The Commission believes that ratio orders within certain permissible ratios may provide market participants with greater flexibility and precision in effectuating trading and hedging strategies. In addition, the Commission believes that including such ratio orders in the exception to the priority rules provided in CBOE Rule 6.45(e) will facilitate the execution of ratio orders. In this regard, the Commission believes that the procedures governing the execution of complex orders, such as ratio orders, serve to reduce the risk of incomplete or inadequate executions while increasing efficiency and competitive pricing by requiring price improvement before the order can receive priority over other orders.⁹ The Commission also notes that the rules of other options exchanges treat certain ratio orders like other complex orders for purposes of their priority rules.¹⁰

The CBOE's rule also provides specific examples of permissible ratio orders. Specifically, the rule provides that a permissible ratio is any ratio that is equal to or greater than one-to-three and less than or equal to three-to-one. For example, as indicated in the rule, a one-to-two ratio, a two-to-three ratio, or a two-to-one ratio is permissible, whereas a one-to-four ratio or a four-to-one ratio is not. This should help to provide guidance to CBOE members of the permissible ratios allowed under CBOE rules for such ratio orders.

The Commission believes that permitting ratio orders to have ratios equal to or greater than one-to-three or

¹⁶ 15 U.S.C. 78s(b)(2).

¹⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See letter from James M. Flynn, Attorney II, Legal Division, CBOE, to Yvonne Fraticelli, Division of Market Regulation, Commission, dated October 6, 2003 ("Amendment No. 1"). Amendment No. 1 revises the proposal to provide that the permissible ratio for a ratio order is any ratio that is equal to or greater than one-to-three (.333) and less than or equal to three-to-one (3.0).

⁴ See Securities Exchange Act Release No. 48672 (October 21, 2003), 68 FR 61499.

⁵ CBOE Rule 6.45(e), "Complex Order Priority Exception," currently states that: "A member holding a spread, straddle, or combination order (or a stock-option order as defined in Rule 1.1(ii)(b)) and bidding (offering) on a net debit or credit basis (in a multiple of the minimum increment) may execute the order with another member without giving priority to equivalent bids (offers) in the trading crowd or in the book provided at least one leg of the order betters the corresponding bid (offer) in the book. Stock-option orders, as defined in Rule 1.1(ii)(a), have priority over bids (offers) of the trading crowd but not over bids (offers) of public customers in the limit order book."

⁶ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁷ 15 U.S.C. 78f(b)(5).

⁸ Under the proposal, a permissible ratio is any ratio that is equal to or greater than one-to-three (.333) or less than or equal to three-to-one (3.0).

⁹ See, e.g., CBOE Rule 6.45(e). See also Securities Exchange Act Release No. 44955 (October 18, 2001), 66 FR 53819 (October 24, 2001) (order approving File No. SR-ISE-2001-18).

¹⁰ See, e.g., ISE rule 722(b)(2), "Complex Order Priority," and PHLX Rule 1033(g), "Ratio Spread Type Priority."