

Board or of any other committee; and shall fix dues, fees, assessments and other charges to be paid by members, allied members, member firms and member corporations. It shall regulate the making and performance of Exchange contracts; transactions on the Exchange; access to and conduct upon the floor of the Exchange and the use of Exchange facilities; the formation, continuance and interests of members in member firms and corporations; business conduct; capital requirements and insolvency of members, member firms and member corporations; arbitration procedures; transfers of memberships and disposition of the proceeds of the sale of such memberships; the listing and delisting of and the suspension of trading in securities on the Exchange; activities of specialists and odd lot dealers; matters relating to quotations and price reports; use of ticker services; and means of communication with non-members. It may examine the financial condition and business conduct of members, member firms and member corporations and business conduct of allied members and may require any member, allied member or officer or employee of any member firm or corporation to appear before it to testify as to such financial condition or business conduct; may require that transactions in securities admitted to dealing on the Exchange be executed on the Exchange; may credit a portion of the income of the Exchange for any current year to the members proportionately in settlement of the contribution which members are obligated to make in connection with the Gratuity Fund of the Exchange; and may require that officers, appointees or employees of the Exchange give good and sufficient bonds for the faithful performance of their duties.

*At the Board of Governors' next meeting after the BOXR Nominating Committee presents its candidates for the two positions reserved on the BOXR Board for representatives of BOX Participants, and its candidate for the position on the BSE Board of Governors reserved for a representative of BOX Participants, in October of each year, the Board of Governors shall select and appoint the Board of Directors of BOXR for the following year, as set forth in the Plan of Delegation of Functions and Authority by the Boston Stock Exchange, Inc. to Boston Options Exchange Regulation, L.L.C., and in accordance with the qualification provisions set forth in Section 4 of the By-Laws of Boston Options Exchange Regulation, L.L.C., including the appointment of the candidates*

*presented by the BOXR Nominating Committee for the two BOXR Board positions reserved for representatives of BOX Participants. The Board of Governors shall also select and appoint as Governor the candidate put forth by the BOXR Nominating Committee for the position on the Board of Governors reserved for a representative of BOX Participants. Additionally, the Board of Governors shall appoint the initial Board of Directors of BOXR, in accordance with the term provisions set forth in Section 5 of the By-Laws of Boston Options Exchange Regulation, L.L.C., and the number of Directors provisions set forth in Section 3 of the By-Laws of Boston Options Exchange Regulation, L.L.C.*

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## **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 IV 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**

In order to create a new options regulatory subsidiary, the BSE proposes to transfer to BOXR, a Delaware limited liability company and a wholly-owned subsidiary of the BSE, all of the assets and liabilities that solely support the regulation of the standardized equity options trading business of the BSE. Upon this transfer, however, the BSE would continue to be the self-regulatory organization ("SRO") for BOXR and the Boston Options Exchange ("BOX"), the BSE's proposed new exchange facility for the trading of standardized equity options securities.<sup>4</sup> BOX would provide automatic order execution capabilities to BOX Options Participants ("Options Participants") for standardized equity options securities listed or traded on the BSE. BOX would be operated by Boston Options Exchange Group, L.L.C. ("BOX LLC"). The proposed rule change for

implementing the creation of BOXR includes: (i) Changes to the BSE Rules of the Board of Governors; (ii) the proposed Plan of Delegation of Functions and Authority by the Boston Stock Exchange, Inc., to Boston Options Exchange Regulation, L.L.C. ("Delegation Plan"); (iii) proposed By-Laws for BOXR; and (iv) amendments to the BSE Constitution.

### **(I) Delegation Plan**

#### **(A) Relationship of BSE, BOXR and BOX LLC**

The BSE is a founding and controlling member of BOX LLC. Pursuant to contractual agreement, the BSE has the right to appoint two representatives to the board of BOX LLC. In addition to its ownership stake in BOX LLC, the BSE has entered into various agreements with BOX LLC under which BOX LLC would operate BOX as a facility of the BSE.<sup>5</sup> Pursuant to these agreements, the BSE, through BOXR, would maintain responsibility for all regulatory functions related to the facility, and BOX LLC would be responsible for the business operations of the facility to the extent those activities are not inconsistent with the regulatory and oversight functions of the BSE and BOXR. This means that BOX LLC would not interfere with the BSE's self-regulatory responsibilities or those delegated to BOXR.

The BSE wholly owns BOXR as a subsidiary of the Exchange and proposes to delegate certain regulatory authority to BOXR for oversight of the BOX market. Under the proposal, BOXR would use its own regulatory staff, and not the employees of BOX LLC, to perform its regulatory oversight duties. In addition, BOXR would conduct all necessary surveillance of the trading effected through the BOX facility as well as enforcement of the BOX Rules, applicable BSE Rules and the federal securities laws and the rules thereunder.<sup>6</sup> Pursuant to the proposed Delegation Plan and contractual agreements, BOXR would have regulatory oversight authority over BOX LLC and its officers, directors, agents and employees, each of whom would be

<sup>4</sup> See Securities Exchange Act Release No. 47186 (Jan. 14, 2003), 68 FR 3062 (Jan. 22, 2003) (SR-BSE-2002-15) ("BOX Proposing Release").

<sup>5</sup> Under the Act, "the term 'facility' when used with respect to an exchange includes its premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any service thereof for the purpose of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service." See 15 U.S.C. 78c(a)(2).

<sup>6</sup> See BOX Proposing Release.