

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-56993; File No. SR-CBOE-2007-104)

December 19, 2007

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change and Amendment No. 1 Thereto to List and Trade Range Options

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 September 6, 2007, the Chicago Board Options Exchange, Incorporated (the “CBOE” or “Exchange”) filed with the Securities and Exchange Commission (the “SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by the Exchange. CBOE filed Amendment No. 1 to the proposed rule change on December 3, 2007.³ The Commission is

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 1 replaces the original filing in its entirety. The purpose of Amendment No. 1 is to: (i) revise the proposed changes to CBOE Rule 12.3, Margin Requirements, to specify initial and/or maintenance margin requirements for margin and cash accounts and to conform the proposed rule text to existing rule text for other products; (ii) revise the proposed definitions of “Range Interval,” “Low Range and Low Range Exercise Value,” “High Range and High Range Exercise Value,” “Exercise Settlement Amount,” and to add a new proposed definition of “exercise price;” (iii) revise proposed CBOE Rule 20.3 to state specifically that Range Options are a separate class from other options overlying the same index; (iv) revise proposed CBOE Rules 20.6, Position Limits, and 20.7, Reports Related Position Limits and Liquidation of Positions, to provide that Range Options will be aggregated with other option contracts on the same underlying index, including other classes of Range Options overlying the same index, for position limit purposes; (v) revise proposed CBOE Rule 20.11 to reference certain rules of The Options Clearing Corporation (“OCC”); (vi) add new proposed CBOE Rule 20.12 to provide that, for purposes of Range Options, reference in the Exchange Rules to the “appropriate committee” shall be read to be the “Exchange;” (vii) provide additional information regarding FLEX options; (viii) delete footnote 2 from the original proposed rule change, because the proposal referenced therein, SR-CBOE-2006-99, is now effective (See Securities Exchange Act Release No. 56792 (November 15, 2007), 72 FR 65776 (November 23, 2007)); and (ix) make conforming changes, clarifications and corrections in the “Purpose” section of the filing.

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 Exchange proposes to amend its rules to provide for the listing and trading of Range Options that may overlie any index that is eligible for options trading on the Exchange.⁴ The text of the proposed rule change is available CBOE, the Commission's Public Reference Room, and www.cboe.org/legal.

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

In its filing with the Commission, CBOE 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. CBOE 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 states that the purpose of the proposed rule change is to enable the initial and continued listing and trading on the Exchange of Range Options that overlie any index eligible for options trading on the Exchange. Range Options are European-style options that have a positive payout if the settlement value of the underlying index falls within the specified Range Length at expiration. Range Options will be based on the same framework as existing

⁴ Range Options are European-style, cash settled options that have a payout if the settlement value of the underlying index falls within the specified Range Length at expiration. The term "Range Length" is defined in proposed CBOE Rule 20.1(c).

options that are traded on the Exchange. However, the maximum payout amount will be capped (as specified by the Exchange at listing) and the specific exercise settlement amount may vary based on where on the Range Length the settlement value of the underlying index value falls.

The Payout Structure of Range Options

The universe of possible payout amounts for Range Options resembles the shape of an isosceles trapezoid spread over a range of index values or the “Range Length.” The Range Length, or the bottom parallel (and longer) line of the trapezoid, defines the entire length of index values for which the option pays a positive amount if the settlement value of the underlying index falls within the specific Range Length. In other words, the Range Length equals the total span between two underlying index values, as set by the Exchange at listing, that is used to determine whether a Range Option is in or out of the money at expiration.

The Range Length is comprised of three segments that are defined by the “Range Interval,” which is a value that the Exchange will specify at listing and the minimum Range Interval will be at least 5 index points. Using the isosceles trapezoid diagram below, the “Range Interval,” defines congruent triangles on opposite sides of the trapezoid, which have base angles of equal degrees and equal base lengths.

The first triangle at the start of the Range Length defines the “Low Range” for the Range Option and if the settlement value of the underlying index value falls in the Low Range (the “Low Range Exercise Value”), the option will pay an amount that increases as the index value increases within the Low Range. To determine the exercise settlement amount if the settlement value of the index falls within the Low Range, the Low Range Exercise Value will be multiplied by the contract multiplier, set by the Exchange at listing.

The second triangle at the end of the Range Length defines the “High Range” for the Range Option and if the settlement value of the underlying index falls in the High Range, the option will pay an amount that decreases as the index value increases within the High Range (“High Range Exercise Value”). To determine the exercise settlement amount if the settlement value of index falls within the High Range, the High Range Exercise Value will be multiplied by the contract multiplier, set by the Exchange at listing. Lastly, the Low Range and High Range are segments of equal lengths at opposite ends on the Range Length and if the settlement value of the underlying index falls at the starting value of the Low Range, at the ending value of the High Range or outside of either the Low Range or the High Range, the option will pay \$0.



The third segment of the Range Option is defined as the “Middle Range,” and its length is equal to the Range Length minus twice the Range Interval, or as illustrated in the above diagram, its length is equal to the length of the top parallel (and shorter) line of the trapezoid. If the settlement value of the underlying index falls anywhere within the Middle Range at expiration, the payout is a fixed amount (set by the Exchange at listing) and does not vary depending on where in the Middle Range the index value falls. Also, if the index value falls in the Middle Range, this will be the highest amount that can be paid out for a Range Option and is defined as the “Maximum Range Exercise Value.” To determine the exercise settlement amount if the settlement value of the index falls anywhere within the Middle Range, the Maximum

Range Exercise Value will be multiplied by the contract multiplier, set by the Exchange at listing.

Unlike other options, Range Options will only be of a single type, and there will not be traditional calls and puts. Also, the exercise or “strike” price for Range Options will be the Range Length that, akin to a regular strike price, will be used to determine if the Range Option is in or out of the money. When applicable, the “strike price” for a Range Option (i.e., the Range Length) will be used to determine the degree that the option is in-the-money (capped at the Maximum Range Exercise Value) if the settlement value of the underlying index falls within either the High or Low Range of the Range Length.

Determination and Example of Exercise Values

The examples and diagrams below demonstrate the variations of payout amounts for Range Options. Assume the Exchange identifies the S&P 500 Index (“SPX”) as the underlying index and defines the Range Length as between 1340 and 1410. Also assume that the Exchange sets the Range Interval at 10 index points and the Maximum Range Exercise Value at 10 and the contract multiplier as \$100.

Payout if Closing Value of Underling Index Falls in Low or High Ranges

Example 1: If, at expiration, the underlying index value falls in either the Low Range or the High Range, the payout will be determined based on where the settlement value falls within the respective range. If the settlement value falls within the Low Range, the Low Range Exercise Value will equal a value that falls within a progressive upward slope that ends at the beginning of the Middle Range. For example, if the settlement value of the SPX is 1342, the exercise settlement amount would be \$200 ($\100×2) or if the settlement value of the SPX is

1347, the exercise settlement would be \$700 (\$100 x 7). If at expiration, the settlement value of the SPX is 1340 or lower, the option would expire worthless.

Example 1: Low Range Exercise Value

1340 ◀-----			Low Range				-----▶ 1349		
Settlement Value of SPX									
1340	1341	1342	1343	1344	1345	1346	1347	1348	1349
Low Range Exercise Value									
0	1	2	3	4	5	6	7	8	9

Example 2: If the settlement value falls within the High Range, the High Range Exercise Value will equal a value that falls within a regressive downward slope that starts at the end of the Middle Range. For example, if the settlement value of the SPX is 1402, the exercise settlement amount would be \$800 (\$100 x 8) or if the settlement value of the SPX is 1406, the exercise settlement would be \$400 (\$100 x 4). If at expiration, the settlement value of the SPX is 1410 or higher, the option would expire worthless.

Example 2: High Range Exercise Value

1401 ◀-----			High Range				-----▶ 1410		
Settlement Value of SPX									
1401	1402	1403	1404	1405	1406	1407	1408	1409	1410
High Range Exercise Value									
9	8	7	6	5	4	3	2	1	0

Maximum, Fixed Payout if Underlying Index Value Falls in Middle Range

Example 3: If at expiration, the settlement value of the SPX is 1351, the option holder would be entitled to receive and the writer would be obligated to pay \$1,000 (\$100 x 10) and if the settlement value of the SPX is 1375, the exercise settlement amount would also be \$1,000. This is because if the settlement value of the SPX falls anywhere within the Middle Range at

expiration, the payout is a fixed amount (Maximum Range Exercise Value times the contract multiplier) and does not vary depending on where in the Middle Range the SPX value falls.

Example 3: Underlying index value falls within Middle Range

1340 ◀-----	Range Length	-----▶ 1410
Low Range	Middle Range Maximum Range Exercise Value = 10	High Range
1340 1349	1350 1400	1401 1410
	SPX = 1351 SPX = 1375	

Benefits of Range Options

The Exchange believes that the introduction of Range Options will provide advantages to the investing public that are not provided for by other index options. First, the Exchange believes that Range Options offer investors a relatively low risk security where the risk reduction results from knowing the maximum risk exposure when the contract is written. While there may be variations in the exercise settlement amount, the maximum exercise settlement amount is set at listing and the maximum risk therefore is limited and known at listing. Second, Range Options are structured similar to two-sided European binary options that provide additional flexibility because the option pays a reduced amount if the underlying index settles outside the main range covered by the option.

Proposed New Rules

To accommodate the introduction of Range Options, the Exchange proposes to adopt new Chapter XX to its rules and to make amendments to existing CBOE Rules 6.1, Days and Hours of Business, and 12.3, Margin Requirements. An introductory paragraph to Chapter XX will explain that the proposed rules in the proposed Chapter are applicable only to Range Options. Trading in Range Options will also be subject to the rules in Chapter I through XIX, XXIV,

XXIVA and XXIVB, in some cases supplemented by the proposed rules in the Chapter, except for existing rules that will be replaced by the proposed rules in the Chapter and except where the context otherwise requires. As proposed, the majority of the rules governing index options will equally apply to Range Options. Those new proposed rules and those proposed amendments to existing rules pertaining to Range Options are described below.

(a) Definitions (Proposed CBOE Rule 20.1)

Proposed Chapter XX includes new definitions applicable to Range Options in CBOE Rule 20.1. In particular, the terms “Range Option,” “settlement value,” “Range Length,” “Range Interval,” “Low Range and Low Range Exercise Value,” “High Range and High Range Exercise Value,” “Middle Range and Maximum Range Exercise Value,” “contract multiplier,” “exercise settlement amount,” and “exercise price” are proposed to be defined.

(b) Days and Hours of Business (Proposed CBOE Rule 20.2 and Amendment to CBOE Rule 6.1)

Proposed CBOE Rule 20.2 and an amendment to CBOE Rule 6.1, Days and Hours of Business Days and Hours of Business, provide that transactions in Range Options may be effected during normal Exchange option trading hours for other options on the same index.

(c) Designation of Range Option Contracts and Maintenance Listing Standards (Proposed CBOE Rules 20.3 and 20.4)

Proposed CBOE Rule 20.3 provides that the Exchange may from time to time approve for listing and trading on the Exchange Range Option contracts that overlie any index that is eligible for options trading on the Exchange. Range Options will be a separate class from other options overlying the same index. The Exchange may add new series of Range Options of the same class (i.e., overlying the same index) as provided for by the rules governing options on the

same underlying index. Additional series of Range Options may be opened for trading on the Exchange when the Exchange deems it necessary to maintain an orderly market or to meet customer demand. The opening of a new series of Range Options on the Exchange will not affect any other series of options of the same class previously opened.

Proposed CBOE Rule 20.4 provides that the maintenance listing standards with respect to options on indexes set forth in CBOE Rule 24.2 and the Interpretations and Policies thereunder will be applicable to Range Options on indexes. CBOE Rule 24.2, Designation of the Index, sets forth initial and maintenance listing criteria for index options.

(d) Limitation of Liability of Exchange and of Reporting Authority (Proposed CBOE Rule 20.5)

Proposed CBOE Rule 20.5 provides that CBOE Rule 6.7, Exchange Liability, will be applicable in respect of any class of Range Options and that CBOE Rule 24.14, Disclaimers, will be applicable in respect of any reporting authority that is the source of values of any index underlying any class of Range Options.

(e) Position Limits, Reporting Relating to Position Limits and Liquidation of Positions and Exercise Limits (Proposed CBOE Rules 20.6 – 20.8)

Proposed CBOE Rule 20.6 provides that in determining compliance with CBOE Rules 4.11, Position Limits, 24.4, Position Limits for Broad-Based Index Options, 24.4A, Position Limits for Industry Index Options, and 24.4B, Position Limits for Options on Micro Narrow-Based Indexes as Defined Under Rule 24.2(d), cash-settled Range Options will have a position limit equal to those for options on the same underlying index. In determining compliance with the applicable position limits, Range Options shall be aggregated with other option contracts on the same underlying index, including other classes of Range Options overlying the same index.

Proposed CBOE Rule 20.7 provides that Range Options will be subject to the same reporting and other requirements triggered for options on the same underlying index. In computing reportable Range Options, Range Options will be aggregated with other option contracts on the same underlying index, including other classes of Range Options overlying the same index.

Proposed CBOE Rule 20.8 provides that exercise limits for Range Options will be the same as those for other options on the same underlying index. To illustrate, CBOE Rule 24.4 provides that the standard position limit for options on the CBOE Russell 2000 Volatility Index (“RVX”) is 50,000 contracts, and the near-term position limit is 30,000 contracts. Therefore, the standard position limit for Range Options overlying the RVX would also be 50,000 contracts, and the near-term position limit would be 30,000 contracts. The 30,000 contract near-term position limit would also be the applicable exercise limit for Range Options on the RVX.⁵

For the purpose of determining compliance with the above limits, Range Options on the RVX would be aggregated with all other options on the RVX, including all series of Range Options on the RVX. This same aggregation would also be utilized to calculate the reporting requirements set forth in CBOE Rule 4.13, Reports Related to Position Limits.⁶

⁵ See CBOE Rule 24.5, Exercise Limits, which provides, *inter alia*, that in determining compliance with CBOE Rule 4.12, exercise limits for index option contracts shall be applicable to the position limits prescribed for option contracts with the nearest expiration date in CBOE Rules 24.4 or 24.4A.

⁶ CBOE Rule 4.13 sets forth the general reporting requirement for customer accounts that maintain a position in excess of 200 contracts (long or short) in any single class of option contracts.

(f) Determination of Settlement Value of the Underlying Index (Proposed CBOE Rule 20.9)

Proposed CBOE Rule 20.9 provides that Range Options that are “in-the-money,” or “out-of-the-money” are a function of the settlement value of the underlying index and whether at expiration the settlement values falls within or outside of the Range Length.

(g) Premium Bids and Offers; Minimum Increments (Proposed CBOE Rule 20.10)

Proposed CBOE Rule 20.10 provides that all bids or offers made for Range Option contracts will be deemed to be for one contract unless a specific number of option contracts is expressed in the bid or offer. A bid or offer for more than one option contract, which is not made all-or-none, will be deemed to be for that amount or any lesser number of option contracts. An all-or-none bid or offer will be deemed to be made only for the amount stated. Proposed CBOE Rule 20.10 also provides that all bids or offers made for Range Option contracts will be governed by the CBOE Rule 24.8, Meaning of Premium Bids and Offers, as that rule applies to index options.

(h) Exercise of Range Options (Proposed CBOE Rule 20.11)

Proposed CBOE Rule 20.11 provides that Range Options will be exercised at expiration if the settlement value of the underlying index falls within the Range Length, and that Range Options shall be subject to the exercise by exception processing procedures set forth in OCC Rules 805 and 1804. OCC Rules 805 and 1804 contain provisions which, inter alia, permit option holders to give instructions to not exercise an option contract.

(i) Exchange Authority (Proposed CBOE Rule 20.12)

Proposed CBOE Rule 20.12 provides that for purposes of Range Options, references in the Exchange Rules to the appropriate committee shall be read to be the Exchange.⁷ The Exchange is proposing this provision because it may determine to assign the applicable authorities with respect to Range Options to committees and/or Exchange staff. This provision will provide the Exchange with flexibility to delegate the authorities under the rules with respect to Range Options to an appropriate committee or appropriate Exchange staff and will not have to make a rule change merely to accommodate the reassignment of such authority. For example, the Exchange may determine to delegate the authority to determine the applicable opening parameter settings to the Office of the Chairman.

(j) FLEX Trading (Proposed CBOE Rule 20.13)

Proposed CBOE Rule 20.13 provides that Range Options will be eligible for trading as Flexible Exchange Options as provided for in Chapter XXIVA and XXIVB.⁸ For purposes of CBOE Rules 24A.4 and 24B.4, the parties will designate the Range Length, Range Interval and Maximum Exercise Value. CBOE Rules 24A.9 and 24B.9, regarding the minimum quote width, will not apply to Range Options.

⁷ Thus, for example, references to determinations regarding the applicable opening parameter settings established by the “appropriate Procedure Committee” in CBOE Rule 6.2B, Hybrid Opening System (“HOSS”), shall be read to be by the “Exchange.” See e.g., Securities Exchange Act Release No. 55919 (June 18, 2007), 72 FR 34495 (June 22, 2007) (rule change providing, inter alia, that for purposes of Credit Options, references in the Exchange Rules to the appropriate committee shall be read to be the Exchange.).

⁸ FLEXible EXchange® Options (FLEX Options) are customized equity or index option contracts that provide investors with the ability to customize key contract terms, like exercise prices, exercise styles and expiration dates. More information about FLEX options may be found at: <http://www.cboe.com/institutional/IndexFlex.aspx>.

(k) Margin (Proposed Amendment to CBOE Rule 12.3)

The Exchange is proposing to amend CBOE Rule 12.3, Margin Requirements, to include requirements applicable to Range Options.⁹ Under the proposed requirements, for a margin account, no Range Option carried for a customer will be considered of any value for purposes of computing the margin requirement in the account of such customer and each Range Option carried for a customer will be margined separately. The initial and maintenance margin required on any Range Option carried long in a customer's account will be 100% of the purchase price of such Range Option. The initial and maintenance margin required on any Range Option carried short in a customer's account will be the Maximum Range Exercise Value times the contract multiplier.

For a cash account, a Range Option carried short in a customer's account will be deemed a covered position, and eligible for the cash account if either one of the following is held in the account at the time the option is written or is received into the account promptly thereafter:

(i) cash or cash equivalents equal to 100% of the Maximum Range Exercise Value times the contract multiplier; or (ii) an escrow agreement. The escrow agreement must certify that the bank holds for the account of the customer as security for the agreement: (A) cash, (B) cash equivalents, (C) one or more qualified equity securities, or (D) a combination thereof having an aggregate market value of not less than 100% of the Maximum Range Exercise Value times the contract multiplier and that the bank will promptly pay the member organization the cash settlement amount in the event the account is assigned an exercise notice.

⁹ The Exchange is proposing the addition of new subparagraph (n) to CBOE Rule 12.3 for Range Options and is proposing to reserve subparagraph (m). The Exchange is seeking to reserve subparagraph (m) because the Exchange previously proposed to use that paragraph to codify margin requirements for a product that is the subject of a pending rule filing. See SR-CBOE-2006-105 (proposal to list and trade binary options on broad based indexes).

The Exchange believes that these proposed levels are appropriate because risk exposure is limited with Range Options and the proposed customer initial and maintenance margin is equal to the maximum risk exposure.¹⁰

(l) Options Disclosure Document

In order to accommodate the listing and trading of Range Options, it is expected that OCC will amend its By-Laws and Rules to reflect the different structure of Range Options. In addition, it is expected that OCC will seek a revision to the Options Disclosure Document (“ODD”) to incorporate Range Options.

(m) Systems Capacity

The Exchange represents that it believes the Exchange and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the listing and trading of Range Options as proposed herein. The Exchange does not anticipate that there will be any additional quote mitigation strategy necessary to accommodate the trading of Range Options.

(n) Surveillance Program

The Exchange represents that it will have in place adequate surveillance procedures to monitor trading in Range Options prior to listing and trading such options, thereby helping to ensure the maintenance of a fair and orderly market for trading in Range Options.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the

¹⁰ In accordance with CBOE Rule 12.10, Margin Required is Minimum, the Exchange has the ability to determine at any time to impose higher margin requirements than those described above in respect of any Range Option position when it deems such higher margin requirements are appropriate.

requirements of Section 6(b) of the Act. Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5) Act¹¹ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, to remove impediments to and to perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

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

CBOE believes that the proposed rule change will not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

No written comments were solicited or received with respect to the proposed rule change.

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 CBOE 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:

¹¹ 15 U.S.C. 78f(b)(5).

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-CBOE-2007-104 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-CBOE-2007-104. 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 a.m. and 3 p.m. 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-CBOE-2007-104 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹²

Florence E. Harmon
Deputy Secretary

¹² 17 CFR 200.30-3(a)(12).