

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-61336; File No. SR-CBOE-2009-092)

January 12, 2010

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change to Amend Rule 8.91 – Limitations on Dealings of DPMs and Affiliated Persons of DPMs

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 December 23, 2009, Chicago Board Options Exchange, Incorporated (“CBOE” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by CBOE. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and is approving 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 Rule 8.91 – Limitations on Dealings of DPMs and Affiliated Persons of DPMs. The text of the proposed rule change is available on the Exchange’s website (<http://www.cboe.org/Legal>), at the Office of the Secretary, CBOE and at the Commission.

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 self-regulatory organization 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 those statements may be examined at the places

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

specified in Item III below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

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

1. Purpose

CBOE proposes to amend Rule 8.91 – Limitation on Dealings of DPMs and Affiliated Persons of DPMs and Rule 8.93 – e-DPM Obligations. Specifically, CBOE proposes to delete all of existing Rule 8.91, including the Guidelines for Exemptive Relief Under Rule 8.91(e) for Members Affiliated with DPMs (“Guidelines for Exemptive Relief”), and replace those provisions with the specific requirement applicable to e-DPMs set forth in Rule 8.93(x) relating to the adoption of information barriers and compliance with Rule 4.18. CBOE also proposes to adopt in both Rule 8.91 and Rule 8.93 a limited exception for integrated market making in broad-based, highly capitalized and liquid ETFs and trust issued receipts (“TIRs”).

CBOE Rule 8.91 and the Guidelines for Exemptive Relief under Rule 8.91 were adopted in 1999, although the provisions contained therein were initially promulgated in 1987.³ Since that time, there have been very few changes to Rule 8.91 and the Guidelines for Exemptive Relief. Recently, members have requested that CBOE evaluate Rule 8.91 and the Guidelines for Exemptive Relief to determine whether any changes would be appropriate given that the rule has been in effect in its current form for many years and the functions and responsibilities of DPMs have changed over time. For example, in 2005 CBOE amended its rules to eliminate the DPM’s responsibility to act as agent in the options in which it is assigned.⁴ As a result, DPMs

³ See Securities Exchange Act Release No. 43004 (6/30/00), 65 FR 43060 (7/12/00), approving SR-CBOE-98-54.

⁴ See Securities Exchange Act Release No. 52798 (11/18/05), 70 FR 71344 (11/28/05), approving SR-CBOE-2005-46.

essentially act as market-makers in their assigned classes, with higher quoting obligations than market-makers and additional responsibilities for which they receive a participation entitlement. Also, the prior restriction on Market-Makers affiliated with a DPM holding an appointment and submitting electronic quotations in an affiliated DPM's class has been eliminated (provided CBOE uses an algorithm in the class that does not allocate trades, in whole or in part, in an equal percentage based on the number of market participants quoting at the best bid or offer).⁵ DPMs also can request to operate away from CBOE's trading floor as an Off-Floor DPM, similar to an e-DPM.⁶

In 2004, CBOE established a new category of market-making participant called e-DPMs, who are member organizations appointed to operate on CBOE as competing DPMs/specialists in a broad number of option classes.⁷ e-DPMs have specific obligations set forth in Rule 8.93, and are otherwise not subject to the provisions in Rule 8.91 and the Guidelines for Exemptive Relief. Rather, under Rule 8.93(x), e-DPMs are required to "maintain information barriers that are reasonably designed to prevent the misuse of material, non-public information with any affiliates that may conduct a brokerage business in option classes allocated to the e-DPM or act as specialist or Market-Maker in any security underlying options allocated to the e-DPM, and otherwise comply with the requirements of Rule 4.18 regarding the misuse of material non-public information."

⁵ See Securities Exchange Act Release No. 59539 (3/9/09), 74 FR 11143 (3/16/09), granting immediate effectiveness to SR-CBOE-2009-015; Securities Exchange Act Release No. 57742 (4/30/08), 73 FR 25067 (5/6/08), granting immediate effectiveness to SR-CBOE-2008-50.

⁶ See Securities Exchange Act Release No. 57568 (3/26/08), 73 FR 18016 (4/2/08), granting immediate effectiveness to SR-CBOE-2008-032.

⁷ See Securities Exchange Act Release No. 50003 (7/12/04), 69 FR 43028 (7/19/04), approving SR-CBOE-2004-24.

Rule 4.18 requires all members (other than lessor members who are not registered as broker-dealers) to establish, maintain and enforce written policies and procedures reasonably designed to prevent the misuse of material, nonpublic information by such member or persons associated with such member. For purposes of Rule 4.18, conduct constituting the misuse of material non-public information includes, but is not limited to: (i) trading in any securities issued by a corporation, partnership, TIR or ETF or similar entities, or in any related securities or related options or other derivative securities, while in possession of material, nonpublic information concerning that corporation, partnership, TIR or ETF or similar entities; (ii) trading in any underlying security or related options or other derivative securities, while in possession of material, nonpublic information concerning imminent transactions in the above; and (iii) disclosing to another person or entity any material, non-public information involving a corporation, partnership, TIR or ETF or similar entities or an imminent transaction in an underlying security or related securities for the purpose of facilitating the possible misuse of such material, non-public information. Rule 4.18 also requires members to establish, maintain and enforce specific policies and procedures for compliance with Rule 4.18.

Given that the functions and obligations of DPMs and e-DPMs are substantially similar, CBOE believes that it would be appropriate for DPMs and e-DPMs to be subject to the same requirements relating to the maintenance of information barriers with any affiliates that may conduct a brokerage business⁸ in option classes allocated to the DPM or act as a specialist or market-maker in any security underlying options allocated to the DPM. CBOE also notes that DPMs do not have any advantages regarding relevant trading information provided by the Exchange vis-à-vis other members in their appointed classes. Accordingly, CBOE proposes to

⁸ The reference to “brokerage business” includes conducting an investment banking business or a public securities business.

delete the existing provisions in Rule 8.91 and the Guidelines for Exemptive Relief, and replace them with the provisions in Rule 8.93(x) relating to the maintenance of information barriers and compliance with Rule 4.18. Rule 8.91(a), as amended, provides that a DPM shall provide its information barriers to the Exchange and obtain prior written approval, which is consistent with the current provisions of Rule 8.91(e).⁹

In addition to the above, CBOE proposes to adopt an exception to the requirement that a DPM or e-DPM in an option overlying a broad-based and highly capitalized ETF or TIR is required to maintain information barriers with any affiliate that acts as a specialist or market-maker in the underlying broad-based ETF or TIR. CBOE notes that this exception currently exists for CBSX DPMs and CBOE DPMs (see Rule 54.7), and believes it is consistent with what the SEC has previously approved.¹⁰

2. Statutory Basis

The Exchange believes the rule proposal is consistent with the Securities Exchange Act of 1934 (the “Act”) and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act.¹¹ Specifically, the Exchange believes that the proposed rule change is consistent with the Section 6(b)(5) Act¹² requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and, in general, to protect investors and the

⁹ If a DPM’s “Chinese Wall” procedures were previously approved by the Exchange pursuant to Rule 8.91(e), the procedures do not need to be re-approved by the Exchange as a result of this rule change unless the procedures are subsequently modified.

¹⁰ See Securities Exchange Act Release No. 55392 (3/2/07), 72 FR 10572 (3/8/07), approving SR-CBOE-2006-112; Securities Exchange Act Release No. 54422 (9/11/06), 71 FR 54537 (9/15/06), approving SR-CBOE-2004-21; Securities Exchange Act Release No. 47200 (1/15/03), 68 FR 3907 (1/27/03), approving SR-CBOE-2002-63.

¹¹ 15 U.S.C. 78f(b).

¹² 15 U.S.C. 78f(b)(5).

public interest. Deleting existing Rule 8.91 and replacing those provisions with the specific requirement applicable to e-DPMs set forth in Rule 8.93(x) should clarify the regulatory obligations of DPMs while retaining an appropriate regulatory requirement relating to the adoption of information barriers and compliance with CBOE Rule 4.18.

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

CBOE does not believe that the proposed rule change will impose any burden on competition 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. 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-CBOE-2009-092 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-CBOE-2009-092. 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 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 publicly available. All submissions should refer to File Number SR-CBOE-2009-092 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission's Findings and Order Granting Accelerated Approval of the Proposed Rule Change

After careful consideration, 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.¹³ The Commission believes that the proposal is consistent with Section 6(b)(5)¹⁴ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, to remove

¹³ In approving this rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁴ 15 U.S.C. 78f(b)(5).

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.

The Exchange is proposing to eliminate the requirement that DPMs maintain certain specifically-prescribed information barriers as described in CBOE Rule 8.91. In its place, the Exchange proposes to amend CBOE Rule 8.91. Amended CBOE Rule 8.91 will continue to require information barriers, but will permit a Designated Primary Market Maker to develop and apply its own policies and procedures to, among other things, prevent the misuse of material nonpublic information. CBOE Rule 8.91 addresses concerns arising from the potential for the sharing of material non-public information between a DPM's market making activities and other business activities of the DPM or its affiliates. For instance, one such concern is that the DPM or affiliate engaging in other business activities might use non-public information that was acquired by the DPM through its role as a market maker, such as trading based on information on the DPM's book. Another concern is that the DPM might use material non-public information received from the entity engaging in other business activities, such as trading based on a change in the firm's buy or sell recommendation.¹⁵

While amended CBOE Rule 8.91 will no longer prescribe the specific information barriers a DPM must establish, the rule will require that such information barriers be reasonably designed to prevent the misuse of material non-public information by the member or persons associated with the member. Amended CBOE Rule 8.91 also will explicitly reference current CBOE Rule 4.18, which among other things, provides that the misuse of material non-public information includes trading in a security or related option or other derivative security while in

¹⁵ See Securities Exchange Act Release No. 58328 (August 7, 2008), 73 FR 48260 (August 18, 2008) (SR-NYSE-2008-45) (articulating concerns in the context of approving changes to NYSE Rule 98).

possession of material non-public information concerning imminent transactions in the security, related option, or other derivative securities.¹⁶ In addition, the proposed rule change requires that the member provide a copy of its information barrier policies and procedures to the Exchange for prior written approval. The Commission believes that, with adequate oversight by the Exchange of its members and prior review and approval of a DPM's information barrier, the amendment of CBOE Rule 8.91 should not materially increase the potential for the misuse of nonpublic information.

Pursuant to this proposal rule change, members may utilize the flexible, principles-based approach to modify their information barriers as appropriate to reflect changes to their business model, business activities, or to the securities market itself. A member should be proactive in assuring that its information barriers reflect the current state of its business and continue to be reasonably designed to achieve compliance with applicable federal securities law and regulations, and with applicable Exchange rules.

The Commission believes that the regulatory approach in this proposed rule change is similar to the regulatory approach of NYSE Arca, Inc. In particular, the CBOE approach, like the NYSE Arca approach, does not require market makers to maintain certain specifically-prescribed information barriers.¹⁷ Unlike NYSE Arca's approach, however, CBOE's rules continue to require all DPMs to maintain information barriers.¹⁸ The basis for this difference is that NYSE Arca's market makers and Lead Market Makers do not have any advantages regarding relevant trading information provided by NYSE Arca, either at, or prior to, the point of

¹⁶ See CBOE Rule 4.18, Interpretations and Policies .01.

¹⁷ See Securities Exchange Act Release No. 60604 (September 1, 2009), 74 FR 46272 (September 8, 2009) (SR-NYSEArca-2009-78).

¹⁸ Id.

execution vis-à-vis other market participants. CBOE, on the other hand, represented only that its DPMs do not have any advantages regarding relevant trading information provided by the Exchange vis-à-vis other members in their appointed classes.¹⁹

CBOE also proposes to exempt DPMs and e-DPMs in an option overlying a broad-based ETF or TIR from the requirement to maintain barriers between it and any affiliates that act as a specialist or market-maker in the underlying broad-based ETF or TIR, provided that the capitalization and liquidity requirements for the component securities of the broad-based ETF or TIR set forth in CBOE Rule 54.7, Interpretation and Policy .03 are satisfied. The Commission believes that this exemption to the information barrier requirements is consistent with the Act. The Commission notes that this exemption is currently available to CBSX DPMs.²⁰ In addition, CBOE Rule 54.7, Interpretation and Policy .03 contains capitalization and liquidity requirements for the component securities of the broad-based ETFs and TIRs, which, together with the proposed exemption, are consistent with what the Commission has previously approved.²¹ As the Commission noted previously, these capitalization and liquidity requirements for the component securities should reduce the likelihood that any market participant has an unfair informational advantage about the ETF, TIR, its related options, or its component securities, or

¹⁹ CBOE members have access to auctions that other market participants do not, including, for example, the Automated Improvement Mechanism (“AIM”) (CBOE Rule 6.74A), and the Solicitation Auction Mechanism (CBOE Rule 6.74B).

²⁰ See CBOE Rule 54.7(d).

²¹ See Securities Exchange Act Release No. 54422 (September 11, 2006), 71 FR 54537 (September 15, 2006) (SR-CBOE-2004-21) (approving CBOE Rule 54.7); Securities Exchange Act Release No. 46213 (July 16, 2002), 67 FR 48232 (July 23, 2002) (SR-Amex-2002-21) (permitting side-by-side trading and integrated market making in broad-based ETFs and TIRs without information or physical barriers or other restrictions).

that a market participant would be able to manipulate the prices of the ETFs, TIRs, or their related options.²²

The Commission also finds good cause, pursuant to Section 19(b)(2) of the Act,²³ for approving the proposed rule change prior to the 30th day after the date of publication of notice in the Federal Register. Although this proposed rule change does not require that DPMs maintain certain specifically-prescribed information barriers, it does require that DPMs establish and maintain information barriers that are reasonably designed to achieve compliance with applicable securities law and regulations, and with applicable Exchange rules. In addition, the rule requires that such barriers be pre-approved by the Exchange. The revised rule thus does not represent a significant change from the current rule, and is at least as stringent as the approach currently employed by NYSE Arca and Nasdaq.²⁴ The Commission believes that, with Exchange approval and oversight, elimination of prescriptive information barrier requirements should not reduce the effectiveness of the CBOE rules which would now permit a DPM to develop and apply its own policies and procedures to, among other things, prevent the misuse of material nonpublic information.

²² See Securities Exchange Act Release No. 46213 (July 16, 2002), 67 FR 48232 (July 23, 2002) (SR-Amex-2002-21) (permitting side-by-side trading and integrated market making in broad-based ETFs and TIRs without information or physical barriers or other restrictions).

²³ 15 U.S.C. 78s(b)(2).

²⁴ See Securities Exchange Act Release No. 53128 (Jan. 13, 2006), 71 FR 3550 (January 23, 2006) (adopting Nasdaq IM-2110-2; IM-2110-3; IM-2110-4, and Rule 3010); see also supra note 17.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²⁵ that the proposed rule change (SR-CBOE-2009-092) be, and it hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁶

Florence E. Harmon
Deputy Secretary

²⁵ 15 U.S.C. 78s(b)(2).

²⁶ 17 CFR 200.30-3(a)(12).