

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-49555; File No. SR-CBOE-2003-59)

April 12, 2004

Self-Regulatory Organizations; Chicago Board Options Exchange, Inc.; Order Granting Approval to Proposed Rule Change and Amendment No. 1 Thereto Relating to the Exchange's Obvious Error Rule

On December 22, 2003, the Chicago Board Options Exchange, Inc. ("CBOE") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend CBOE Rule 6.25, which governs the nullification and adjustment of electronic transactions resulting from obvious error. On January 20, 2004, CBOE submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change, as amended, was published for comment in the Federal Register on February 12, 2004.<sup>4</sup> The Commission received no comments on the proposal.

The Exchange proposes to extend specified provisions of its obvious error rule to open outcry transactions. Specifically, CBOE proposes to extend the application of CBOE Rule 6.25(a)(3) (Verifiable Disruptions or Malfunctions of Exchange Systems), CBOE Rule 6.25(a)(4) (Erroneous Print in the Underlying), and CBOE Rule 6.25 (a)(5) (Erroneous Quote in the Underlying) to open outcry trades. CBOE also proposes that paragraphs (b) through (e) of CBOE Rule 6.25, which set forth the procedures for review, adjustment/nullification, and appeal of obvious error electronic transactions, apply to the

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Steve Youhn, Legal Division, CBOE, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated January 16, 2004.

<sup>4</sup> See Securities Exchange Act Release No. 49194 (February 5, 2004), 69 FR 7058.

adjustment and nullification of open outcry transactions in the same manner that they apply to electronic transactions.

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<sup>5</sup> and, in particular, the requirements of Section 6(b) of the Act<sup>6</sup> and the rules and regulations thereunder. The Commission finds that the proposed rule change is consistent with Section 6(b)(5)<sup>7</sup> of the Act, which requires that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission considers that in most circumstances trades that are executed between parties should be honored. On rare occasions, the price of the executed trade indicates an "obvious error" may exist, suggesting that it is unrealistic to expect that the parties to the trade had come to a meeting of the minds regarding the terms of the transaction. In the Commission's view, the determination of whether an "obvious error" has occurred should be based on specific and objective criteria and subject to specific and objective procedures. CBOE's proposal extends the application of three provisions of its current obvious error rule covering electronic transactions to open outcry transactions. These provisions are Verifiable Disruptions or Malfunctions of Exchange Systems,

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<sup>5</sup> In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

Erroneous Prints in the Underlying, and Erroneous Quotes in the Underlying. The determination of whether an obvious error exists for open outcry transactions for these three situations is based on the same specific and objective criteria that currently exist for electronic transactions. Also, the procedures governing the adjustment or nullification of Verifiable Disruptions or Malfunctions of Exchange Systems, Erroneous Prints in the Underlying, and Erroneous Quotes in the Underlying in open outcry transactions are the same specific and objective procedures the Exchange has in place for adjustment or nullification of these same situations in electronic transactions.<sup>8</sup>

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act<sup>9</sup>, that the proposed rule change (File No. SR-CBOE-2003-59), as amended, be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>8</sup> See Securities Exchange Act Release No. 48827 (November 24, 2003), 68 FR 67498 (December 2, 2003) (File No. SR-CBOE-2001-04).

<sup>9</sup> 15 U.S.C. 78s(b)(2).

<sup>10</sup> 17 CFR 200.30-3(a)(12).