SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-52011; File No. SR-CBOE-2004-63)

July 12, 2005

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Approving a Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 2 Thereto to List and Trade Short Term Option Series

I. Introduction

On October 12, 2004, the Chicago Board Options Exchange, Incorporated ("CBOE" 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 initiate a one-year pilot program that would allow the Exchange to list and trade option series that expire one week after being opened ("Short Term Option Series"). The Exchange filed Amendment No. 1 with the Commission on January 21, 2005.[3] The amended proposal was published for comment in the Federal Register on February 16, 2005.[4] The Commission received one comment letter regarding the proposal.[5] The Exchange filed Amendment No. 2 with the Commission on April 26, 2005.[6] This notice and order requests comment on Amendment No. 2 and approves the proposal, as amended, on an accelerated basis.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 Amendment No. 1 replaced the original filing in its entirety.

4 See Securities Exchange Act Release No. 51172 (February 9, 2005), 70 FR 7979.

5 See letter from Michael J. Ryan, Executive Vice President and General Counsel, American Stock Exchange, to Jonathan G. Katz, Secretary, Commission, dated March 10, 2005 ("Amex Letter").

6 Amendment No. 2 replaced the original filing and Amendment No. 1 in their entirety. Amendment No. 2 proposes that Short Term Option Series listed on currently approved option classes would settle in the same manner (i.e., with respect to A.M. or P.M. settlement and cash or physical settlement) as do the monthly expiration series in the same option class.

II. Description of Proposed Rule

CBOE proposes to amend its rules to establish a pilot program to list and trade Short Term Option Series, which would expire one week after the date on which a series is opened. Under the proposal, the Exchange could select up to five approved option classes[7] on which Short Term Option Series could be opened. A series could be opened on any Friday that is a business day and would expire at the close of business on the next Friday that is a business day. If a Friday were not a business day, the series could be opened (or would expire) on the first business day immediately prior to that Friday.

Under the pilot program, the Exchange also could list and trade Short Term Option Series on any option class that is selected by another exchange that employs a similar pilot program. Limiting the number of such option classes would ensure that the addition of new series through the pilot program would have only a negligible impact on the Exchange's and the Options Price Reporting Authority's ("OPRA") quoting capacity. Also, limiting the term of the pilot program to a period of one year would allow the Exchange and the Commission to determine whether the Short Term Option Series program should be extended, expanded, and/or made permanent.

As originally proposed, all Short Term Option Series would be P.M.-settled. However, in Amendment No. 2, CBOE revised the proposal so that a Short Term Option Series would be settled in the same manner as the monthly expiration series in the same class. If the monthly option contract for a particular class were A.M.-settled, as most index options are,[8] the Short

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[7] A Short Term Option Series could be opened in any option class that satisfied the applicable listing criteria under CBOE rules (i.e., stock options, options on exchange-traded funds as defined under Interpretation and Policy .06 to CBOE Rule 5.3, or options on indexes).

[8] The Exchange notes, however, that certain monthly expiration index options—specifically, American- and European-style options on the S&P 100 Index (OEX and

Term Option Series for that class also would be A.M.-settled; if the monthly option contract for a particular class were P.M.-settled, as most non-index options are, the Short Term Option Series for that class also would be P.M.-settled. Similarly, Short Term Option Series for a particular class would be physically settled or cash-settled in the same manner as the monthly option contract in that class. The Exchange usually would open five Short Term Option Series for each expiration date in that class. The strike price of each Short Term Option Series would be fixed at a price per share, with at least two strike prices above and two strike prices below the value of the underlying stock or calculated index value at about the time that the Short Term Option Series is opened. CBOE would not open a Short Term Option Series in the same week that the corresponding monthly option series is expiring, because the monthly option series in its last week before expiration is functionally equivalent to the Short Term Option Series. The interval between strike prices on Short Term Option Series would be the same as with the corresponding monthly option series. CBOE would aggregate a Short Term Option Series with its corresponding monthly option series for purposes of the Exchange's rules on position limits.

The Exchange represented that it has the system capacity to adequately handle the new option series contemplated by this proposal. The Exchange provided to the Commission information in a confidential submission to support that representation.

CBOE proposed that the pilot program extend one year from the date of this approval.

III. Discussion

After careful review, the Commission finds that the proposal, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national

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XEO, respectively)—are P.M.-settled. Therefore, the Short Term Option Series in these index options would also be P.M.-settled.

securities exchange.[9] In particular, the Commission believes that the proposal is consistent with the requirements of Section 6(b)(5) of the Act,[10] which requires, among other things, that the rules of a national securities exchange be designed to remove 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 Commission believes that listing and trading Short Term Option Series, under the terms described in CBOE's proposal, will further the public interest by offering investors new means of managing their risk exposures and carrying out their investment objectives. The Commission also believes that the pilot program strikes a reasonable balance between the Exchange's desire to offer a wider array of investment opportunities and the need to avoid unnecessary proliferation of option series that could compromise options quotation capacity. The Commission expects CBOE to monitor the trading and quotation volume associated with the additional option series created under the pilot program and the effect of these additional series on the capacity of the Exchange's, OPRA's, and vendors' systems.

The Commission received one comment letter on the proposed rule change.[11] The commenter questioned the appropriateness of P.M. settlement for Short Term Option Series on indexes, given the Commission's historical concern that P.M.-settled index options have the potential to increase volatility in the underlying equity market.

The Commission shares the commenter's concern. In Amendment No. 2, CBOE revised its proposal so that all Short Term Option Series will be settled in the same manner as the

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

10 15 U.S.C. 78f(b)(5).

11 See Amex Letter, supra note 5.

corresponding monthly expiration series in the same class. Consequently, the majority of Short Term Option Series on indexes will be A.M.-settled, as are the majority of regular index options. The Commission believes that this amendment adequately addresses any concerns regarding settlement time.

Pursuant to Section 19(b)(2) of the Act,[12] the Commission finds good cause for approving the amended proposal prior to the thirtieth day after the publication of Amendment No. 2 in the Federal Register. Amendment No. 2 proposes that Short Term Option Series listed on currently approved option classes will settle in the same manner (i.e., with respect to A.M. or P.M. settlement and cash or physical settlement) as do their corresponding monthly expiration series in the same option class. The Commission finds good cause to accelerate approval of the amended proposal because CBOE's approach to settlement times for the new Short Term Option Series is consistent with prior Commission guidance regarding options settlement times generally.

IV. Solicitation of Comments Concerning Amendment No. 2

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 2, including whether it 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-2004-63 on the subject line.

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12 15 U.S.C. 78s(b)(2).

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-CBOE-2004-63. 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. Copies of such 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-2004-63 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[13] that the proposed rule change (File No. SR-CBOE-2004-63), as amended, is approved, and that Amendment No. 2 thereto is approved on an accelerated basis, as a pilot program, through July 12, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[14]

Jill M. Peterson
Assistant Secretary

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13 Id.

14 17 CFR 200.30-3(a)(12).