

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55025; File No. SR-CBOE-2006-96)

December 29, 2006

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order
Approving a Proposed Rule Change Regarding Allocation of Stocks to CBSX DPMs

I. Introduction

On November 20, 2006, 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” or “Exchange Act”)¹ and Rule 19b-4 thereunder,² a proposal relating to the allocation of stocks for the CBOE Stock Exchange (“CBSX”). The proposal was published for comment in the Federal Register on November 27, 2006.³ The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

The purpose of this filing is to adopt rules that would allow for the allocation of stocks to CBSX DPMs.

The Exchange has represented that it intends to submit a proposal to modify Chapters 50-55 of its rules, which govern the trading of non-option securities on the Exchange,⁴ in connection with the establishment of CBSX (the “CBSX Trading Rules Proposal”). In addition, the Exchange has proposed rules to establish CBSX as a facility of the Exchange (the “CBSX

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 54792 (November 20, 2006), 71 FR 68659.

⁴ See Securities Exchange Act Release No. 54422 (September 11, 2006), 71 FR 54537 (September 15, 2006) (approving SR-CBOE-2004-21). See also Securities Exchange Act Release No. 54526 (September 27, 2006), 71 FR 58646 (October 4, 2006) (approving SR-CBOE-2006-70).

Facility Proposal”).⁵ If the Commission approves these proposals, CBSX would be a facility of the Exchange and would serve as the Exchange’s vehicle for trading non-option securities. In addition, the Exchange has filed for immediate effectiveness a proposal to appoint CBSX DPMs (the “CBSX DPM Appointment Proposal”).⁶ Any appointments under the CBSX DPM Appointment Proposal and any allocations made to such DPMs under this proposal would be contingent on Commission approval of the CBSX Trading Rules Proposal—in particular, those rules governing DPM trading procedures and obligations on CBSX—and the CBSX Facility Proposal.

Initial CBSX DPM stock allocations would be handled pursuant to proposed CBOE Rule 53.54. For the initial launch, and potentially in instances where CBSX seeks to commence trading a number of new securities at one time, CBSX would conduct a “draft” for eligible CBSX DPMs to select available stocks. The draft order would be determined randomly. In connection with the initial launch, the draft would apply to the first 500 securities selected.⁷ The remaining securities slated for trading on CBSX would be allocated randomly by CBSX to the CBSX DPMs equally.

CBSX would utilize proposed CBOE Rule 53.54 for future stock allocations as well. In those cases, a draft could be employed or CBSX could allocate the stocks based on any one or more of the following: performance, volume, capacity, market performance commitments,

⁵ See SR-CBOE-2006-110 (filed December 26, 2006).

⁶ See Securities Exchange Act Release No. 54831 (November 29, 2006), 71 FR 70814 (December 6, 2006) (notice of filing and immediate effectiveness of SR-CBOE-2006-100).

⁷ Telephone conversation between Angelo Evangelou, Assistant General Counsel, CBOE, and Nathan Saunders, Special Counsel, Division of Market Regulation, Commission, November 20, 2006.

operational factors, efficiency, competitiveness, expressed preferences of issuers, and the best interest of CBSX.

The Exchange is seeking to launch trading on CBSX on February 5, 2007. The Exchange has stated that allocating stocks to CBSX DPMs ahead of the launch date would allow it and the CBSX DPMs to be prepared to commence trading on CBSX immediately if and when the Commission approves the CBSX Trading Rules Proposal and the CBSX Facility Proposal.

III. Discussion

After careful review, 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.⁸ In particular, the Commission believes that the proposal is consistent with the requirements of Section 6(b)(5) of the Act,⁹ in that it has been designed to promote just and equitable principles of trade, to protect investors and the public interest, and is not designed to permit unfair discrimination between CBSX DPMs.

The Commission believes that the CBOE's proposal to employ a randomly-set draft rotation for allocating non-option securities is reasonably designed to promote just and equitable principles of trade and to avoid unfair discrimination. Moreover, the Commission believes that the additional proposed criteria for allocating non-option securities to CBSX DPMs when a draft is not appropriate are reasonable and consistent with the Act. These additional criteria are similar to the options allocation criteria set forth in CBOE Rule 8.95(a) and (b), which the

⁸ 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).

⁹ 15 U.S.C. 78f(b)(5).

Commission has previously approved.¹⁰

The Commission notes that all allocations of securities to CBSX DPMs under this proposal are contingent on Commission approval of the CBSX Trading Rules Proposal and the CBSX Facility Proposal. Moreover, in approving CBOE's proposal to establish rules for allocating stocks on CBSX, the Commission is not prejudging CBOE's other pending proposals relating to CBSX. If the Commission were not to approve the CBSX Trading Rules Proposal and the CBSX Facility Proposal, any allocations made pursuant to this proposal would be meaningless. Approving the CBSX allocation rules does, however, afford CBOE an opportunity to prepare for the possibility that the Commission will approve the CBSX Trading Rules Proposal and the CBSX Facility Proposal, and would reduce the time between any such approvals and the commencement of trading on CBSX.

¹⁰ See Securities Exchange Act Release No. 39879 (April 16, 1998), 63 FR 20227 (April 23, 1998) (order approving SR-CBOE-98-03). Several of the factors that CBSX may consider in the allocation process are adopted from CBOE Rule 8.95: performance, volume, capacity, market performance commitments, operational factors, efficiency, competitiveness, and expressed preferences of issuers. The Commission believes that these criteria should be used by CBOE solely for the purpose of allocating non-option securities to CBSX DPMs. The Commission emphasizes that CBOE should not use the proposed criteria—especially the “market performance commitments” and “best interest of CBSX” criteria—to directly or indirectly attempt to restrict a market participant that is appointed as a CBSX DPM from performing market-making or specialist activities on other markets.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹¹ that the proposed rule change (File No. SR-CBOE-2006-96) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹²

Florence E. Harmon
Deputy Secretary

¹¹ Id.

¹² 17 CFR 200.30-3(a)(12).