

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55971; File No. SR-CBOE-2007-66)

June 28, 2007

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Regarding its Open Outcry Allocation Rules

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 18, 2007, the Chicago Board Options Exchange, Incorporated (“CBOE” or “Exchange”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I, II and III below, which Items have been substantially prepared by CBOE. The Exchange filed the proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act³ and Rule 19b-4(f)(6) thereunder,⁴ which renders it effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

CBOE proposes to amend its open outcry allocation rules for classes trading on the Hybrid Trading System (“Hybrid”). The text of the proposed rule change is available at CBOE, the Commission's Public Reference Room, and (<http://www.cboe.org/Legal>).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(iii).

⁴ 17 CFR 240.19b-4(f)(6).

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 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 those statements may be examined at the places specified in Item IV 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 the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange is proposing to modify its open outcry allocation rules for Hybrid classes, which are contained in paragraph (b) of Rules 6.45A, Priority and Allocation of Equity Option Trades on the CBOE Hybrid System, and 6.45B, Priority and Allocation of Trades in Index Options and Options on ETFs on the CBOE Hybrid System, as applicable. Under the existing allocation rules, at the same execution price: (i) public customer orders in the electronic book have first priority, with multiple public customer orders prioritized based on time priority; (ii) in-crowd market participants and broker-dealer orders resting in the electronic book collectively have second priority, with the broker-dealer orders getting a “book market participant” share;⁵ and (iii) electronic quotes of Market-Makers have third

⁵ Under the existing allocation rules, the cumulative number of broker-dealer orders in the electronic book at the best price are deemed to be one “book market participant” regardless of the number of broker-dealer orders in the book. Also under the existing rules, the allocation due the broker-dealer orders in the electronic book by virtue of their being deemed a “book market participant” is as follows: If two or more bids (offers) represent the best price, one of which represents a book market participant, priority is afforded to the in-crowd market participants in the sequence in which their bids (offers) were made; provided, however, that (i) the first in-crowd market participant to respond is entitled to 70% of the order; (ii) the second in-crowd market participant to respond (if ascertainable) is entitled to 70% of the remainder of the

priority, with multiple bids or offers prioritized based on the electronic allocation algorithm in effect for the option class.⁶

The Exchange is proposing to revise the priority levels so that, at the same execution price: (i) public customer orders in the electronic book would continue to have first priority, with multiple public customer orders prioritized based on time priority; (ii) in-crowd market participants would have second priority, with multiple bids or offers prioritized based on the allocation algorithm provided in Rule 6.45(A) or (B);⁷ and (iii) broker-dealer orders resting in the electronic book and electronic quotes of Market-Makers would collectively have third

order (*i.e.*, 70% of 30%); and (iii) the balance of the order is apportioned equally among the remaining in-crowd market participants bidding (offering) at the same price and the book market participant share. If it is not possible to determine the order in which in-crowd market participants responded, the balance of the order shall be apportioned equally among the remaining market participants bidding (offering) at the same price and, if applicable, the book market participant. If two or more bids (offers) represent the best price, each of which is NOT a book market participant, priority is afforded to the in-crowd market participants in accordance with the allocation principles contained in CBOE Rule 6.45(a) or (b), which generally provide that priority is afforded to such bids (offers) in the sequence in which they are made or, if the bids were made at the same time or in the event the sequence cannot be reasonably determined, priority is apportioned equally. See existing CBOE Rules 6.45A(b) and 6.45B(b).

⁶ The particular algorithm is determined on a class-by-class basis and can be based on either price-time priority, pro-rata priority or the Ultimate Match Algorithm (“UMA”). The UMA allocation formula has a component based on the number of market participants quoting at the best price (“Component A”) and a component based on the size of market participant quotes. Depending on the particular algorithm and class, additional priority overlays pertaining to public customer orders, Market-Maker participation entitlements and market turner may also apply. See CBOE Rule 6.45A(a) or 6.45B(a), as applicable.

⁷ Allocation among the in-crowd market participants in this manner is consistent with the existing CBOE Rule 6.45A(b) and 6.45B(b) allocation procedures that apply when there is NOT a book market participant. See note 5, supra.

priority, with multiple bids or offers prioritized based on the electronic allocation algorithm in effect for the option class.⁸

In addition, in order to transact proprietary orders⁹ on the floor of the Exchange pursuant to Rule 6.45A(b) or 6.45B(b), members must also ensure that they qualify for an exemption from Section 11(a)(1) of the Act.¹⁰ Members relying on Section 11(a)(1)(G) of the Act¹¹ and Rule 11a1-1(T) thereunder (commonly known as the “G exemption rule”)¹² as an exemption must comply with the requirements of that exemption before executing a proprietary order, including the requirement to yield priority to any bid or offer at the same price for the account of a person who is not, or is not associated with, a member (a “non-member”), irrespective of the size of any such bid or offer or the time when entered.

Because CBOE’s electronic book does not distinguish between member and non-member broker-dealer orders, the revised priority provisions would further provide that members

⁸ If the UMA algorithm is in effect, the cumulative number of broker-dealer orders in the electronic book at the best price are deemed one “market participant” for purposes of calculating Component A. See note 6, supra. In revising the priority algorithm to provide that in-crowd market participants have priority over the trading interests of both broker-dealer orders resting in the electronic and electronic quotes of Market-Makers, the Exchange notes that at least one other options exchange already has in place rules that afford in-crowd participants priority over electronic trading interests. See Rule 6.76(d) of NYSE Arca Inc. In addition, this change in the priority algorithm will make the open outcry priority rules for non-crossing transactions more consistent with the Exchange’s open outcry priority rules for crossing transactions, which currently provide for in-crowd market participants to have priority over the trading interests of both broker-dealer orders resting in the electronic book and electronic quotes of Market-Makers. See CBOE Rule 6.74, Crossing Orders.

⁹ For purposes of CBOE Rule 6.45A(b) or 6.45B(b), a “proprietary order” will mean an order for a member’s own account, the account of an associated person, or an account with respect to which it or an associated person thereof exercises investment discretion.

¹⁰ 15 U.S.C. 78k(a)(1).

¹¹ 15 U.S.C. 78k(a)(1)(G).

¹² 17 CFR 240.11a1-1(T).

relying on the G exemption rule must yield priority to any bid (offer) at the same price of public customer orders and broker-dealer orders (whether non-member or member) resting in the electronic book, as well as any other bids and offers that would otherwise have priority over such broker-dealer orders under Rule 6.45A(b) or 6.45B(b).¹³

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with Section 6(b) of the Act¹⁴ in general and furthers the objectives of Section 6(b)(5) of the Act¹⁵ in particular in that it is designed to promote just and equitable principles of trade, serve to remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

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 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

The Exchange neither solicited nor received comments on the proposal.

¹³ Thus, for example, a Floor Broker that is relying on the G exemption rule must first yield priority to any same priced public customer orders and broker-dealer orders resting in the electronic book, as well as any in-crowd market participants that would otherwise have priority over those broker-dealer orders, before executing a proprietary order. In such a scenario, the Rule 6.45A(b) or Rule 6.45B(b) priority sequence described above is modified so that, at the same price, public customer orders resting in the book would have first priority, then the in-crowd market participants (to the extent each such market participant also qualifies for an exemption from Section 11(a)(1) but is not relying on the G exemption rule), then broker-dealer orders resting in the book, then the Floor Broker's proprietary order (along with any other in-crowd market participants also relying on the G exemption rule). To the extent there may be any further remaining balance, same priced electronic quotes of Market-Makers would have priority to trade next.

¹⁴ 15 U.S.C. 78f(b).

¹⁵ 15 U.S.C. 78f(b)(5).

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (1) significantly affect the protection of investors or the public interest; (2) impose any significant burden on competition; and (3) become operative for thirty days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁶ and Rule 19b-4(f)(6)¹⁷ thereunder.¹⁸

At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in the furtherance of the purposes of the Act.

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:

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-

¹⁶ 15 U.S.C. 78s(b)(3)(A).

¹⁷ 17 CFR 240.19b-4(f)(6).

¹⁸ Pursuant to Rule 19b-4(f)(6)(iii), the Exchange has given the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date on which the Exchange filed the proposed rule change. See 17 CFR 240.19b-4(f)(6)(iii).

2007-66 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-CBOE-2007-66. 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 am and 3:00 pm. 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 available publicly.

All submissions should refer to File Number SR-CBOE-2007-66 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁹

Florence E. Harmon
Deputy Secretary

¹⁹ 17 CFR 200.30-3(a)(12).