

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-56245; File No. SR-CBOE-2006-104)

August 14, 2007

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change and Amendment No. 1 Thereto to Codify the Hybrid Price Check Parameter

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> notice is hereby given that on December 7, 2006, the Chicago Board Options Exchange, Incorporated (“CBOE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by the Exchange. On August 1, 2007, the Exchange filed Amendment No. 1 to the proposed rule change. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Exchange proposes to amend Rule 6.13, CBOE Hybrid System’s Automatic Execution Feature, in order to codify an automated system feature that prevents executions at potentially erroneous prices.

The text of the proposed rule change is available on the Exchange’s Web site (<http://www.cboe.com>), at the Exchange’s principal office, and at the Commission’s Public Reference Room.

---

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

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

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 Exchange 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 these 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 aspects of such statements.

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

1. Purpose

Orders that are eligible for automatic execution through the CBOE Hybrid Trading System ("Hybrid") may be automatically executed in accordance with the provisions of CBOE Rule 6.13. Orders that are not eligible for automatic execution route on a class by class basis to PAR (the public automated routing system) or BART (the booth automated routing terminal) or, at the order entry firm's discretion, to the order entry firm's booth printer.

The purpose of the proposed rule change is to amend CBOE Rule 6.13 to codify a description of the Exchange's price check parameter functionality, which is a functionality that could be activated in certain series of a given options class that would prevent an automatic execution of a market order from occurring outside a prescribed market width. The Exchange represents that the price check parameter is designed to help maintain a fair and orderly market. Specifically, the functionality would not automatically execute eligible orders that are market orders if the width between the Exchange's best bid and best offer is not within an acceptable price range. The applicable price ranges will be determined by the appropriate Exchange

Procedure Committee on a series by series basis and will be announced to the membership via Regulatory Circular generally at least one day in advance.

For purposes of this provision, an “acceptable price range” shall be no less than 1.5 times the corresponding bid/ask differentials in CBOE Rule 8.7(b)(iv)(A).<sup>3</sup> In addition, the Exchange is proposing that the senior official in CBOE’s Control Room or two Floor Officials may grant intra-day relief by widening the acceptable price range for one or more option series. If intra-day relief is granted, it will be announced via verbal message to the trading crowd, printer message to member organizations on the trading floor, and electronic message to members that request to receive such messages. The granting of this intra-day relief will be for no more than the duration of the particular trading day. Any decision to extend relief beyond an intra-day basis would be announced to the membership via Regulatory Circular. Market orders that trigger the applicable price check parameter and, thus, that are not eligible for automatic execution, will be routed on a class by class basis to PAR or BART or, at the order entry firm’s discretion, to the order entry firm’s booth printer.

For example, the Exchange may determine to set a price check parameter that provides that market orders would not automatically execute if the width between the Exchange’s best bid and best offer is \$0.40 or more in a series where the bid is less than \$2 (\$0.40 is more than 1.5 X the standard bid/ask differential of \$0.25). Assume that the market in the series is \$1.65 - \$1.85; the bid is for 10 contracts, the next best bid is \$1.50 for 10 contracts, and the next best bid is \$0.50 for 10 contracts. An incoming sell order for 50 contracts would trade against the \$1.65 for

---

<sup>3</sup> CBOE Rule 8.7(b)(iv)(A) sets forth the bid/ask differentials for open outcry trading, which are as follows: No more than \$0.25 between the bid and offer for each option contract for which the bid is less than \$2, no more than \$0.40 where the bid is at least \$2 but does not exceed \$5, no more than \$0.50 where the bid is more than \$5 but does not exceed \$10, no more than \$0.80 where the bid is more than \$10 but does not exceed \$20, and no more than \$1.00 where the bid is more than \$20.

10 contracts and the \$1.50 for 10 contracts.<sup>4</sup> When the bid moves to \$0.50, the price check parameter would be triggered because the width between the best bid (\$0.50) and best offer (\$1.85) is wider than the acceptable \$0.40 price range. As a result, the remaining 30 contracts would route to PAR, BART, or the booth.<sup>5</sup>

The Exchange believes that the proposed rule change is consistent with the firm quote requirements of CBOE's Rule 8.51, Firm Disseminated Market Quotes, and the Commission's Rule 602 under Regulation NMS.<sup>6</sup> In that regard, the Exchange notes that the Quote Rule does not require an automatic execution.<sup>7</sup> The Exchange also notes that it would not be disengaging its auto-ex system by this proposed rule change, but merely amending the rule to provide for certain circumstances in which market orders may not receive an automatic execution.

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act<sup>8</sup> and the rules and regulations under the Act applicable to national securities exchanges and, in particular, the

---

<sup>4</sup> This example assumes that CBOE is at the national best bid or offer ("NBBO") at each price point. If CBOE is not at the NBBO, the order would not be automatically executed at prices inferior to the NBBO and instead would route to PAR, BART, or the Hybrid Agency Liaison ("HAL"), which is a feature within Hybrid that provides automated handling in designated Hybrid option classes for qualifying electronic orders that are not automatically executed. See CBOE Rules 6.13(b)(iv) and 6.14.

<sup>5</sup> Following from the example above, on an intra-day basis the senior official or two Floor Officials may determine based on market conditions to grant relief by widening the acceptable price range from \$0.40 (e.g., the range might be temporarily widened so that automatic executions would not occur if the width between the best bid and best offer is \$0.80 or more).

<sup>6</sup> 17 CFR 242.602.

<sup>7</sup> See Securities Exchange Act Release No. 47959 (May 30, 2003), 68 FR 34441 (June 9, 2003) (SR-CBOE-2002-05) (order approving Hybrid, including Hybrid's automatic execution feature).

<sup>8</sup> 15 U.S.C. 78s(b)(1).

requirements of Section 6(b) of the Act.<sup>9</sup> Specifically, the Exchange believes the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>10</sup> which requires that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, to remove impediments to and to perfect the mechanism for a free and open market and a national market system, and, in general, to 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

No written comments were solicited or received with respect to the proposed rule change.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

---

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

<sup>10</sup> 15 U.S.C. 78f(b)(5).

#### 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](mailto:rule-comments@sec.gov). Please include File No. SR-CBOE-2006-104 on the subject line.

##### Paper comments:

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

All submissions should refer to File Number SR-CBOE-2006-104. 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-2006-104 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.<sup>11</sup>

Florence E. Harmon  
Deputy Secretary

---

<sup>11</sup> 17 CFR 200.30-3(a)(12).