

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-58778; File No. SR-CBOE-2008-90)

October 14, 2008

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of a Proposed Rule Change Related to Trades in Restricted Classes

On August 29, 2008, 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”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend CBOE Rules 6.25 and 24.16 (collectively, the “Obvious Error Rules”) to permit the nullification of opening transactions that do not satisfy the requirement of CBOE Rule 5.4 (withdrawal of approval of underlying security) and to clarify certain provisions in CBOE Rule 5.4 and the Obvious Error Rules. The proposed rule change was published for comment in the Federal Register on September 13, 2008.<sup>3</sup> The Commission received no comment letters on the proposal. This order approves the proposed rule change.

The Exchange proposes to amend the Obvious Error Rules to permit the nullification of opening transactions in “restricted series” that do not satisfy the requirements of CBOE Rule 5.4.<sup>4</sup> Currently, when the Exchange makes a determination that trading in a series is restricted

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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> Securities Exchange Act Release No. 58460 (September 4, 2008), 73 FR 53060.

<sup>4</sup> In relevant part, CBOE Rule 5.4 provides that, whenever the Exchange determines that an underlying security previously approved for Exchange option transactions does not meet the then current requirements for continuance of such approval or for any other reason should no longer be approved, the Exchange will not open for trading any additional series of options of the class covering that underlying security and therefore two floor officials, in consultation with a designated senior executive officer of the Exchange, may prohibit any opening purchase transactions in series of options of that class previously opened (except that (i) opening transactions by Market-Makers executed to accommodate closing transactions of other market participants and (ii) opening transactions by CBOE

pursuant to CBOE Rule 5.4, the Exchange notifies the membership of that determination through issuance of a regulatory circular. In addition, the Exchange's systems are programmed to automatically restrict the entry of electronic opening transactions. However, opening orders entered in open outcry are not systemically prevented and, in addition, opening market-maker activity is still permitted both electronically and in open outcry. As a result, it is possible that an opening transaction that does not satisfy the requirements of CBOE Rule 5.4 may occur inadvertently. In order to address these scenarios, the Exchange proposes to permit the nullification of opening transactions in CBOE Rule 5.4 restricted series provided notification is received by designated personnel in the Exchange's control room from any member or person associated with a member that believes it participated in such transaction within the timeframes prescribed in CBOE Rules 6.25(b)(1) and 24.16(b)(1). In addition, absent unusual circumstances, designated personnel in the control room (either on their own motion or upon request of a member) would initiate action within sixty (60) minutes of such a transaction. Such actions would be reviewed and determinations rendered by the senior official in the control room. Any determinations rendered by the senior official would be subject to the same review procedures as determinations rendered by Trading Officials.

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member organizations to facilitate the closing transactions of public customers executed as crosses pursuant to and in accordance with paragraph (b) or (d) of CBOE Rule 6.74, Crossing Orders, may be permitted), to the extent it deems such action necessary or appropriate (such series are referred to herein and in the proposed new text in CBOE Rules 6.25 and 24.16 as "restricted series"); provided, however, that where exceptional circumstances have caused an underlying security not to comply with the Exchange's current approval maintenance requirements, regarding number of publicly held shares or publicly held principal amount, number of shareholders, trading volume or market price the Exchange, in the interest of maintaining a fair and orderly market or for the protection of investors, may determine to continue to open additional series of option contracts of the class covering that underlying security.

The Exchange also proposes to permit a member to initiate an Obvious Error Rule action by contacting either a Trading Official or designated personnel in the control room. Under the current rule, a member is only permitted to contact Trading Officials to initiate such action. Once either a Trading Official or a control room designee is contacted, all reviews and determinations will continue to be rendered by Trading Officials except that, as proposed herein, actions to nullify an opening trade in a restricted series will be reviewed and determinations rendered by the senior official in the control room.

Lastly, the Exchange proposes to clarify in the text of CBOE Rule 5.4 that the restrictions on opening transactions contained in the rule, as well as the related exceptions, apply to both opening purchases and opening sales in restricted series. The Exchange notes that its intention is that the restrictions, and related exceptions, also apply to opening sales; however, the current rule text indicates that the restrictions are applicable only to opening purchase transactions. Proposed changes to the rule text make this clear.

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 and, in particular, the requirements of Section 6(b) of the Act<sup>5</sup> and the rules and regulations thereunder. Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>6</sup> in that the proposal is 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.

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

<sup>6</sup> 15 U.S.C. 78f(b)(5).

The Commission notes that, in approving proposals relating to adjustment or nullification of trades involving obvious errors, it has stated that the determination of whether an obvious error has occurred and the process for reviewing such a determination should be based on specific and objective criteria and subject to specific and objective procedures.<sup>7</sup> The Commission believes that the CBOE's proposal provides specific and objective criteria for determining when transactions in restricted classes should be nullified. Specifically, under the rule, opening transactions that do not satisfy the requirement of CBOE Rule 5.4 will be nullified. Market participants will be on notice that trading in a series is restricted pursuant to CBOE Rule 5.4 through a regulatory circular. The Commission also believes that other proposed changes to the Obvious Error Rules and Rule 5.4 are specific and objective.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>8</sup> that the proposed rule change (SR-CBOE-2008-90) is hereby approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

Florence E. Harmon  
Acting Secretary

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<sup>7</sup> See, e.g., Securities Exchange Release Nos. 54228 (July 27, 2006), 71 FR 44066 (August 3, 2006) (SR-CBOE-2006-14) (approving revisions to CBOE's Obvious Error Rule) and 48097 (June 26, 2003), 68 FR 39604 (July 2, 2003) (SR-CBOE-2003-10) (approving revisions to CBOE's Obvious Error Rule).

<sup>8</sup> 15 U.S.C. 78s(b)(2).

<sup>9</sup> 17 CFR 200.30-3(a)(12).