SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-64189; File No. SR-CBOE-2011-008)

April 5, 2011

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of Proposed Rule Change to Permit the Listing of Series with $0.50 and $1 Strike Price Increments on Certain Options Used to Calculate Volatility Indexes

I. Introduction

On February 4, 2011, 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 expand the $2.50 Strike Price Program. The proposed rule change was published for comment in the Federal Register on February 24, 2011.[3] The Commission received no comment letters on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

CBOE has proposed to amend Rules 5.5 and 24.9 to permit the listing of strike prices in $0.50 intervals where the strike price is less than $75, and strike prices in $1.00 intervals where the strike price is between $75 and $150 for option classes used to calculate volatility indexes. The Exchange also proposed to amend Interpretation and Policy .08 to Rule 5.5 to permit $0.50 strike price intervals where the strike price is less than $75 for options on exchange-traded funds ("ETFs") that are used to calculate a volatility index.

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

2 17 CFR 240.19b-4.

3 Securities Exchange Act Release No. 63927 (February 17, 2011), 76 FR 10412 ("Notice").

In its proposal, CBOE seeks to apply its VIX methodology[4] to options on certain ETFs and individual equity securities, and believes that it is appropriate to designate strike price intervals and ranges for series in such options that are comparable to those strike price intervals and ranges in effect for the SPX option series. The Exchange hopes that this will permit calculation of volatility index values that are recognized to be as accurate and reliable as the VIX values. The Exchange stated that allowing smaller strike price intervals for options overlying single stocks, ETFs, and indexes with prices of $150 or less will allow the Exchange to calculate volatility indexes that are better estimates of the expected volatility of option classes with underlying prices that are low relative to the level of the S&P 500.

The Exchange also stated its belief that the expansion of strike prices resulting from the proposal is limited because the proposal will apply only to options that are used to calculate a volatility index. CBOE further stated that it has analyzed its capacity and represented that it believes that the Exchange and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the listing series with strike prices in $0.50 intervals where the strike price is less than $75, and series with strike prices in $1.00 intervals where the strike price is between $75 and $150 for option classes used to calculate volatility indexes that would result from the Exchange's proposal.

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4 The VIX methodology is derived from a body of research showing that it is possible to create pure exposure to volatility by assembling a special portfolio of options. While the price of a single option depends on both the underlying price and volatility, this special portfolio is constructed, in the aggregate, to eliminate the stock price dependence. In theory, this option portfolio would be comprised of an infinite number of options with continuous strike prices. In practice, however, the options that are used to calculate VIX – as well as other volatility indexes – are finite in number and are subject to a minimum interval between strike prices. The narrower this minimum interval, the more accurate the expression of volatility should be.

III. Discussion

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.[5] Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,[6] which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts, 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 proposal appears to strike a reasonable balance between the Exchange's desire to offer a wider array of investment opportunities and the need to avoid unnecessary proliferation of options series and the corresponding increase in quotes and market fragmentation. The Commission expects the Exchange to monitor the trading volume associated with the additional options series listed as a result of this proposal and the effect of these additional series on market fragmentation and on the capacity of the Exchange's, OPRA's, and vendors' automated systems. The Commission notes that CBOE has represented that it believes the Exchange and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the newly permitted listings.

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5 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).

6 15 U.S.C. 78f(b)(5).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[7] that the proposed rule change (SR-CBOE-2011-008) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[8]

Cathy H. Ahn
Deputy Secretary

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[7] 15 U.S.C. 78s(b)(2).

[8] 17 CFR 200.30-3(a)(12).