

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-69638; File No. SR-CBOE-2013-055)

May 24, 2013

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change to Amend its Rules Regarding the Trading of XSP Options

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on May 14, 2013, Chicago Board Options Exchange, Incorporated (the “Exchange” or “CBOE”) 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 prepared by the Exchange. 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

The Exchange proposes to amend its rules regarding the trading of XSP options. The text of the proposed rule change is available on the Exchange’s website (<http://www.cboe.com/AboutCBOE/CBOELegalRegulatoryHome.aspx>), at the Exchange’s Office of the Secretary, and at the Commission’s Public Reference Room.

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

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

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

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

The Exchange proposes to amend its rules regarding the trading of XSP options (which have 1/10 the value of the S&P 500 Index options). First, the Exchange proposes to amend Interpretation and Policy .14 to Rule 24.9 to state that the Exchange may list options on XSP whose exercise settlement value is derived from closing prices on the last trading day prior to expiration ("P.M.-settled"). The Exchange currently offers the SPXPM options class, which are P.M.-settled options on the S&P 500 Index. SPXPM trades on a pilot basis, which pilot period is to end 12 months from the approval date (which was February 8, 2013). The Exchange proposes to add P.M.-settled XSP options to the SPXPM pilot program (and to insert the date February 8, 2014 in place of "[insert date 12 months from approval]" to designate the end date of the pilot period). CBOE proposes to abide by the same reporting requirements for the trading of P.M.-settled XSP under this pilot program as the Exchange does for the trading of SPXPM.<sup>3</sup> Upon approval of this proposed rule change, the Exchange would change the trading symbol for A.M.-settled XSP options, allow any series with open interest in A.M.-settled XSP options to expire, delete any A.M.-settled XSP series without open interest and, going forward, only list XSP series that are P.M.-settled. The purpose of this proposed change is to permit the trading of XSP options on a P.M.-settled basis, as the Exchange believes that this will encourage greater trading in XSP options.

The Exchange proposes to make a number of corresponding amendments to its rules in

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<sup>3</sup> For the details of these reporting requirements, see Securities Exchange Act Release Nos. 68888 (February 8, 2013), 78 FR 10668 (February 14, 2013) and 68457 (December 18, 2012), 77 FR 76135 (December 26, 2012) (SR-CBOE-2012-120).

conjunction with the proposed trading of XSP options on a P.M.-settled basis.

First, Interpretation and Policy .04 to Rule 24.6 states that on the last trading day, transactions in expiring PM-settled S&P 500 Index options (SPXPM) may be effected on the Exchange between the hours of 8:30 a.m. and 3:00 p.m. (as opposed to the normal trading hours for non-expiring SPXPM options, which are from 8:30 a.m. until 3:15 p.m.).<sup>4</sup> The Exchange proposes to add P.M.-settled XSP options to this statement.<sup>5</sup>

XSP options (which are based on the S&P 500 Index) are typically priced in the market based on corresponding futures values. The primary listing markets for the component securities that comprise the S&P 500 close trading in those securities at 3:00 p.m. The primary listing exchanges for the component securities disseminate closing prices of the component securities, which are used to calculate the exercise settlement value of the S&P 500. CBOE believes that, under normal trading circumstances, the primary listing markets have sufficient bandwidth to prevent any data queuing that would cause any trades that are executed prior to the closing time from being reported after 3:00 p.m. Despite the fact that the exercise settlement value will be fixed at or soon after 3:00 p.m., if the Exchange did not close trading in expiring P.M.-settled XSP options at 3:00 p.m. on their last trading day, trading in expiring P.M.-settled XSP options would continue for an additional fifteen minutes until 3:15 p.m. and would not be priced on corresponding futures values, but rather the known cash value. At the same time, the prices of non-expiring PM-settled XSP options series would continue to move and be priced in response to changes in corresponding futures prices.

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<sup>4</sup> All times referenced are Chicago time.

<sup>5</sup> The proposed Interpretation and Policy .04 to Rule 24.6 would read: On their last trading day, transactions in expiring PM-settled S&P 500 Index options (SPXPM) and P.M.-settled XSP options may be effected on the Exchange between the hours of 8:30 a.m. (Chicago time) and 3:00 pm (Chicago time).

A potential pricing divergence could occur between 3:00 p.m. and 3:15 p.m. on the final trading day in expiring P.M.-settled XSP options (e.g., switch from pricing off of futures to cash). Further, the switch from pricing off of futures to cash can be a difficult and risky switchover for liquidity providers. As a result, without closing expiring contracts at 3:00 p.m., it is foreseeable that Market-Makers would react by widening spreads in order to compensate for the additional risk. Therefore, the Exchange believes that, in order to mitigate potential investor confusion and the potential for increased costs to investors, it is appropriate to cease trading in the expiring P.M.-settled contracts of SPXPM and XSP with P.M.-settlement, as they are based on the S&P 500 Index, at 3:00 p.m. The Exchange does not believe that the proposed change will impact volatility on the underlying cash market at the close on third Fridays. Further, the Exchange already closes trading on the last trading day for transactions in expiring SPXPM options at 3:00 p.m.

The Exchange also proposes to amend Interpretation and Policy .03 to Rule 6.42 regarding minimum increments for bids and offers for XSP options. Currently, the minimum increments for bids and offers for XSP options are \$0.01 for all option series quoted below \$3 (including LEAPS) and \$0.05 for all option series \$3 and above (including LEAPS).<sup>6</sup> However, the current minimum increments for bids and offers for SPY options, which is an exchange-traded fund that tracks the performance of 1/10th the value of the S&P 500 Index, is \$0.01 regardless of whether option series is quoted above, at, or below \$3.<sup>7</sup> Because both XSP options and SPY options prices are based, in

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<sup>6</sup> This minimum increment pricing regime for XSP options was established in 2007, and was established in the same amounts that were concurrently approved for physically settled options on the SPDR S&P 500 ETF (“SPY”). See Securities Exchange Act Release No. 56565 (September 27, 2007), 72 FR 56403 (October 3, 2007) (approval of SR-CBOE-2007-98, which extended and expanded the Penny Pilot Program).

<sup>7</sup> The minimum increment for all option series in the SPY option class became \$0.01 in 2010. See Securities Exchange Act Release No. 61478 (February 3, 2010), 75 FR 6762 (February 10, 2010) (SR-CBOE-2010-009).

some manner, on 1/10th the price of the S&P 500 Index, the Exchange believes that it is important that these products have the same minimum increments for consistency and competitive reasons. As such, the Exchange proposes to state that for so long as SPY options participate in the Penny Pilot program, the minimum increments for XSP are \$0.01 for all options series (including LEAPS).<sup>8</sup>

The Exchange also proposes to amend its rules regarding strike price intervals for XSP options. Currently, Interpretation and Policy .11 to Rule 24.9 states that [n]otwithstanding Interpretation and Policy .01(a) to Rule 24.9, the interval between strike prices of series of XSP options will be \$1 or greater, subject to a number of somewhat-involved conditions.<sup>9</sup> The Exchange proposes to simplify these rules and provide that the interval between strike prices of series of XSP options will be \$1 or greater where the strike price is \$300 or less and \$5.00 or

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<sup>8</sup> The proposed Interpretation and Policy .03 to Rule 6.42 would read: For so long as SPDR options (SPY) and options on Diamonds (DIA) participate in the Penny Pilot Program, the minimum increments for Mini-SPX Index Options (XSP) are \$0.01 for all options series (including LEAPS) and for options on the Dow Jones Industrial Average (DJX) are \$0.01 for all option series quoted below \$3 (including LEAPS), and \$0.05 for all option series \$3 and above (including LEAPS).

<sup>9</sup> Those conditions are:

- (a) The Exchange may list series at \$1 or greater strike price intervals on Mini-SPX options with strike prices that are no more than 20% away from one-tenth of the current value of the Standard & Poor's 500 Stock Index ("S&P 500 Index"). FOR EXAMPLE, if the current value of the S&P 500 Index is at 1,200.00, the Exchange may only list new series at \$1 strike price intervals in Mini-SPX options that are between \$96 and \$144 strike prices.
- (b) The Exchange may list series at \$3 or greater strike price intervals on Mini-SPX options with strike prices that are no more than 25% away from one-tenth of the current value of the S&P 500 Index.
- (c) The Exchange may list series at \$5 or greater strike price intervals on Mini-SPX options that are more than 25% away from one-tenth of the current value of the S&P 500 Index.
- (d) The Exchange shall not list LEAPS or reduced-value LEAPS on Mini-SPX options at intervals less than \$5.

greater where the strike price is greater than \$300. Along with simplifying XSP's strike price interval rules, allowing strike price intervals of as little as \$1 up to a strike price of \$300 will allow for greater granularity and more trading options in XSP, which is currently trading at around \$163. Only allowing strike price intervals of \$5 or greater beginning at \$200 would limit the ability of the Exchange to offer more relevant and tailored trading options for investors. Options on the S&P 500 Index (SPX or SPXPM) have strike price intervals of \$5 or greater, but XSP options, which as a Mini S&P 500 Index has 1/10th the value of the S&P 500 Index options, should therefore be permitted smaller strike price intervals than the S&P 500 Index options.

Aside from the proposed changes outlined above, trading in P.M.-settled XSP options will operate in the same manner as trading currently operates in A.M.-settled XSP options. The trading symbol will remain XSP, and XSP will continue to trade on the Exchange's Hybrid Trading System ("Hybrid"). XSP options will still have a \$100 multiplier and European-style exercise. Expiration processing would occur on Saturday following the third Friday of the month. No position or exercise limits will be in effect for XSP options, and the same position reporting and margin requirements will apply.

Finally, in preparing this proposed rule change, the Exchange noticed an erroneous reference in Interpretation and Policy .10 to Rule 5.5, which states that the intervals between strike prices of XSP series shall be determined in accordance with Interpretation and Policy .14 to Rule 24.9. However, it is Interpretation and Policy .11, not Interpretation and Policy .14, to Rule 24.9 that discusses strike price intervals for XSP options. As such, the Exchange proposes to correct this reference in Interpretation and Policy .10 to Rule 5.5 to refer to Interpretation and Policy .11 to Rule 24.9.

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.<sup>10</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>11</sup> requirements 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. The Exchange believes that the introduction of P.M. settlement for XSP options in the manner proposed does not raise any prohibitive regulatory concerns. Further, the Exchange believes that the proposal will not adversely impact fair and orderly markets on third (“expiration”) Fridays for the underlying stocks comprising the S&P 500 index. The Exchange believes that CBOE has experienced no meaningful regulatory concerns, nor an adverse impact on fair and orderly markets, in connection with the CBOE pilot program that permits trading of SPXPM (which is P.M.-settled), nor in connection with the previous pilot program that permitted trading of SPXPM on C2 Options Exchange, Incorporated. Additionally, the proposed rule change would provide TPHs and investors with an opportunity to trade XSP options with a P.M. settlement feature on CBOE subject to transparent exchange-based rules. Investors would also benefit from the opportunity to trade in association with this product on third (“expiration”) Fridays thereby removing impediments to a free and open market consistent with the Act.

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

<sup>11</sup> 15 U.S.C. 78f(b)(5).

The proposal to end trading at 3:00 p.m. on the last trading day for transactions in expiring P.M.-settled XSP options will prevent continued trading on a product after the exercise settlement value has been fixed. This eliminates potential confusion and thereby protects investors and the public interest. The Exchange believes that the proposal to match up the rules regarding minimum increments for bids and offers for XSP options with those for SPY options perfects the mechanism for a free and open market and a national market system because both products are based, in some manner, on  $1/10^{\text{th}}$  the price of the S&P 500 Index, and therefore it makes sense to have the same minimum increments of bids and offers for both. The correcting of the reference in Interpretation and Policy .10 to Rule 5.5 will eliminate any potential confusion, thereby removing impediments to and perfecting the mechanism for a free and open market and a national market system, and, in general, protecting investors and the public interest. The Exchange believes that the proposal to amend the strike price intervals for XSP options rule perfects the mechanism for a free and open market system. Along with simplifying the strike price interval rules for XSP options, allowing strike price intervals of as little as \$1 up to a strike price of \$300 will allow for greater granularity and will hopefully generate more trading in XSP options, which is currently trading at around \$163. Only allowing strike price intervals of \$5 or greater beginning at \$200 would limit the ability of the Exchange to offer more relevant trading options for investors. Options on the S&P 500 Index (SPX or SPXPM) have strike price intervals of \$5 or greater, but XSP, which as a Mini S&P 500 Index has  $1/10^{\text{th}}$  the value of the S&P 500 Index options, should therefore be permitted smaller strike price intervals than the S&P 500 Index options.

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. The Exchange does not believe the proposed changes will impose any unnecessary or inappropriate burden on intramarket competition because they will apply equally to all CBOE market participants and P.M.-settled XSP options will be available to all CBOE market participants. The Exchange believes that the proposed changes to minimum pricing (e.g., matched between SPY and XSP options) will enhance competition and is necessary for consistency. To the extent that the advent of XSP options trading in a P.M.-settled manner, or any other proposed rule changes described herein, may make CBOE a more attractive marketplace to market participants at other exchanges, such market participants may elect to become CBOE market participants.

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 proposed rule change.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

- A. by order approve or disapprove such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

#### 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 Number SR-CBOE-2013-055 on the subject line.

##### Paper comments:

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

All submissions should refer to File Number SR-CBOE-2013-055. 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 website (<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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, D.C. 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. 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-2013-055, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>12</sup>

Jill M. Peterson  
Assistant Secretary

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