

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49919; File No. SR-CBOE-2004-36)

June 25, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Chicago Board Options Exchange, Inc., Relating to a One-Month Extension of the \$5 Quote Width Pilot Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 25, 2004, the Chicago Board Options Exchange, Inc. (“CBOE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The CBOE has submitted the proposed rule change under Section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6) thereunder,⁴ which renders the proposal 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

In January 2004, the CBOE implemented a six-month pilot program (“Pilot Program”), which expires on June 29, 2004, that permits quote spread parameters of up to \$5, regardless of the price of the bid, for up to 200 options classes traded on the CBOE’s Hybrid Trading System (“Hybrid”).⁵ The CBOE subsequently expanded the Pilot Program to include all options classes

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).

⁵ See Securities Exchange Act Release No. 49153 (January 29, 2004), 69 FR 5620 (February 5, 2004) (notice of filing and immediate effectiveness of File No. SR-CBOE-2003-50) (“Pilot Notice”).

traded on Hybrid⁶ and limited the applicability of the \$5 quote spreads permitted under the Pilot Program to quotations that are submitted electronically to Hybrid.⁷ The CBOE proposes to extend the Pilot Program through July 29, 2004. To prevent a lapse of the Pilot Program, the CBOE has asked the Commission to waive the 30-day operative delay in Rule 19b-4(f)(6)(iii).⁸ The text of the proposed rule change appears below. Additions are italicized; deletions are bracketed.

Rule 8.7 Obligations of Market-Makers

- (a) No change.
- (b) No change.
- (i)-(iii) No change.
- (iv) No change.

(A) [For a six month period expiring on June 29, 2004] Until July 29, 2004, options on classes trading on the Hybrid system may be quoted electronically with a difference not to exceed \$5 between the bid and offer regardless of the price of the bid. The \$5 quote widths shall only apply to classes trading on the Hybrid system and only following the opening rotation in each security (i.e., the widths specified in paragraph (b)(iv) above shall apply during opening rotation). Quotes given in open outcry in Hybrid classes may not be quoted with \$5 widths and instead must comply with the legal width requirements (e.g., no more than \$0.25 between the bid and offer for each option contract for which the bid is less than \$2) described in paragraph (iv) and not subparagraph (iv)(A).

⁶ See Securities Exchange Act Release No. 49318 (February 25, 2004), 69 FR 10085 (March 3, 2004) (notice of filing and immediate effectiveness of File No. SR-CBOE-2004-10) (“February Notice”).

⁷ See Securities Exchange Act Release No. 49791 (June 2, 2004), 69 FR 32389 (June 9, 2004) (order approving File No. SR-CBOE-2004-20) (“June Order”).

⁸ 17 CFR 240.19b-4(f)(6)(iii).

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

The Pilot Program became effective in January 2004 and designated 200 options classes that, for a six-month period, could be quoted with a difference not to exceed \$5 between the bid and offer regardless of the price of the bid.⁹ In February 2004, the CBOE expanded the number of options classes in the Pilot Program to include all options classes trading on Hybrid.¹⁰ The CBOE subsequently limited the applicability of the \$5 quote spreads permitted under the Pilot Program to quotations that are submitted electronically to Hybrid.¹¹

The Pilot Program expires on June 29, 2004. As part of the Pilot Program, the CBOE committed to prepare and submit to the Commission a report assessing the operation of the Pilot Program and, in particular, the quality of the quotations for the options included in the Pilot Program. The CBOE is in the process of preparing the report and anticipates submitting it to the Commission shortly. Given the impending expiration of the Pilot Program, however, the CBOE requests a one-month extension of the Pilot Program, through July 29, 2004, to allow the

⁹ See Pilot Notice, supra note 5.

¹⁰ See February Notice, supra note 6.

Commission to review the report and consider a subsequent CBOE request to make the Pilot Program permanent.

2. Statutory Basis

The CBOE believes the proposed rule change is consistent with the Act and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act.¹² Specifically, the CBOE believes the proposed rule change is consistent with the Section 6(b)(5)¹³ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and, in general, to protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

The CBOE does not believe that the proposed rule change will impose any burden on competition 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.

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

The CBOE has filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act¹⁴ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹⁵ Because the foregoing proposed rule change: (1) does not significantly affect the protection of investors or the public interest; (2)

¹¹ See June Order, *supra* note 7.

¹² 15 U.S.C. 78f(b).

¹³ 15 U.S.C. 78f(b)(5).

¹⁴ 15 U.S.C. 78s(b)(3)(A).

¹⁵ 17 CFR 240.19b-4(f)(6).

does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date of filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(6) thereunder. As required under Rule 19b-4(f)(6)(iii), the CBOE provided the Commission with written notice of its intent to file the proposed rule change at least five business days prior to filing the proposal with the Commission or such shorter period as designated by the Commission.

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative prior to 30 days after the date of filing. However, Rule 19b-4(f)(6)(iii) permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The CBOE has requested that the Commission waive the 30-day operative delay to allow the CBOE to continue the Pilot Program without interruption for an additional 30 days, through July 29, 2004, while the Commission considers the Pilot Program report that the CBOE will submit to the Commission. The CBOE believes that the Pilot Program has been successful and has provided market makers with the ability to more accurately price options in all types of market conditions. For this reason, the CBOE believes that it is important from a liquidity-providing standpoint to allow the Pilot Program to continue uninterrupted.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because it will permit the Pilot Program to continue without interruption through July 29, 2004.¹⁶ For this reason, the Commission designates that the proposal become operative immediately.

¹⁶ For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

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 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-2004-36 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

All submissions should refer to File Number SR-CBOE-2004-36. 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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the 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-2004-36 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.¹⁷

Margaret H. McFarland
Deputy Secretary

¹⁷ 17 CFR 200.30-3(a)(12).