

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50209; File No. SR-CBOE-2004-43)

August 18, 2004

Self Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval to Proposed Rule Change and Amendment No. 1 Thereto to Amend the Exchange's Membership Rules to Accommodate e-DPMs

On July 12, 2004, 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 its Chapter III membership rules to accommodate a new category of CBOE market-making participant - electronic Designated Primary Market-Makers ("e-DPMs"). On July 12, 2004, the CBOE filed Amendment No. 1 to the proposed rule change.<sup>3</sup>

The proposed rule change, as amended, was published for comment in the Federal Register on July 19, 2004.<sup>4</sup> The Commission received no comments on the proposal.

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange<sup>5</sup> and, in particular, the requirements of Section 6 of the

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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> See letter from David Doherty, Attorney, Legal Division, CBOE, to Deborah Flynn, Assistant Director, Division of Market Regulation, Commission, dated July 12, 2004 ("Amendment No. 1").

<sup>4</sup> See Securities Exchange Act Release No. 50007 (July 13, 2004), 69 FR 43034.

<sup>5</sup> In approving this proposed rule change, as amended, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

Act<sup>6</sup> and the rules and regulations thereunder. The Commission specifically finds that the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act<sup>7</sup> in that it is designed to promote just and equitable principles of trade, to remove impediments and to perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

In particular, the Commission believes that the CBOE's proposed amendment to CBOE Rule 3.8(a)(ii) to allow a member organization acting as an e-DPM to have one individual be the nominee for multiple memberships that are designated for use in an e-DPM capacity would not be inappropriate given that e-DPMs operate from locations outside of the trading crowds for their applicable option classes, thereby making it possible for a member to act as an nominee on more than one membership.<sup>8</sup> The Commission notes, however, that such individual cannot be the designated nominee for any of the organization's other memberships in any other market making capacity other than that of an e-DPM.

The Commission further believes that the CBOE's proposal to change the reference to "floor functions" in CBOE Rules 3.2, 3.8, and 3.9 to "trading functions" should help to clarify the applicability of these rules to e-DPMs, who would not necessarily have a floor presence.<sup>9</sup> In addition, Commission believes that the proposed

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<sup>6</sup> 15 U.S.C. 78f.

<sup>7</sup> 15 U.S.C. 78f(b)(5).

<sup>8</sup> The Commission notes that it would not be possible for an in-crowd market participant to act as nominee on more than one membership because such participant would be unable to physically be present in more than one trading crowd.

<sup>9</sup> The Commission notes that it is possible for e-DPMs to stream quotes into the Exchange from locations on the trading floor other than the trading crowds where

amendment to CBOE Rule 3.2 to clarify that a member is deemed to have an authorized “trading function” if the member is approved by the CBOE’s Membership Committee to act as a nominee or person registered for an e-DPM organization should help to ensure that e-DPMs, like other Market-Makers and CBOE Floor Brokers, would be required to comply with the CBOE Rule 3.9(g) member orientation and qualification exam requirements. Lastly, the Commission notes that the CBOE’s proposed Rule 3.28 requirement that e-DPMs provide the Exchange with a letter of guarantee from a clearing member is similar to ISE Rule 808 and PCX Rule 6.36(a) requirements, previously approved by the Commission.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>10</sup> that the proposed rule change (SR-CBOE-2004-43) and Amendment No. 1 thereto be approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>11</sup>

Margaret H. McFarland  
Deputy Secretary

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their allocated option classes are traded. In addition, for an 18-month period, e-DPMs are permitted to have no more than one Market-Maker affiliated with the e-DPM to trade on the trading floor in any specific options classes allocated to the e-DPM. CBOE Rule 8.93(vii).

<sup>10</sup> 15 U.S.C. 78s(b)(2).

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