

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50212; File No. SR-CBOE-2004-55)

August 18, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Chicago Board Options Exchange, Inc. to Incorporate Electronic DPMs

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> notice is hereby given that on August 3, 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, II and III below, which Items have been prepared by the CBOE. The CBOE has designated this proposal as one establishing or changing a due, fee, or other charge imposed by the CBOE under Section 19(b)(3)(A)(ii) of the Act,<sup>3</sup> and Rule 19b-4(f)(2) thereunder,<sup>4</sup> 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

The CBOE proposes to amend its marketing fee to incorporate newly established electronic DPMs (“e-DPMs”) as part of the existing marketing fee.<sup>5</sup> Below is the text of

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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> 15 U.S.C. 78s(b)(3)(A)(ii).

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

<sup>5</sup> On July 12, 2004, the Commission approved the establishment of e-DPMs. See Securities Exchange Act Release No. 50003 (July 12, 2004), 69 FR 43028 (July 19, 2004) (SR-CBOE-2004-24).

the proposed rule change. Proposed new language is italicized.

CHICAGO BOARD OPTIONS EXCHANGE, INC.

FEE SCHEDULE

1. No Change.
2. MARKET MAKER, e-DPM & DPM MARKETING FEE (in option classes in which a DPM has been appointed) (6) \$ .40
- 3.-4. No Change.

NOTES:

- (1)–(5) No Change.
- (6) The Marketing Fee will be assessed only on transactions of Market-Makers, e-DPMs and DPMs resulting from customer orders from payment accepting firms with which the DPM has agreed to pay for that firm’s order flow, and with respect to orders from customers that are for 200 contracts or less.
- (7) – (13) No change.

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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 CBOE included statements concerning the purpose of and basis for its proposal and discussed any comments it had received regarding the proposal. The text of these statements may be examined at the places specified in Item IV below. The CBOE 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

Effective June 1, 2003, the Exchange reinstated its marketing fee program in order for the CBOE to compete with other markets in attracting options order flow in multiply traded options from firms that include payment as a factor in their order routing decisions in designated classes of options.<sup>6</sup> The Exchange proposes to incorporate e-DPMs in the existing marketing fee program. The CBOE states that, in all other respects, the marketing fee program would continue to function and operate in the same manner as the existing marketing fee program.<sup>7</sup>

The Exchange would impose the fee at a rate of \$.40 per contract on Market-Maker transactions, including DPMs and e-DPMs, in all classes of options in which a DPM has been appointed, as described below. According to the CBOE, this program, like the CBOE's prior marketing fee program, provides for the equitable allocation of a reasonable fee among the CBOE's members and is designed to enable the CBOE to compete with other markets in attracting options order flow in multiply traded options from firms that include payment as a factor in their order routing decisions in designated classes of options. The CBOE proposes that the marketing fee be assessed only on those Market-Maker, DPM, and e-DPM transactions resulting from orders from customers of payment accepting firms ("payment accepting firms") with which the DPM has agreed to pay for that firm's order flow.

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<sup>6</sup> See Securities Exchange Act Release No. 47948 (May 30, 2003), 68 FR 33749 (June 5, 2003) (SR-CBOE-2003-19).

<sup>7</sup> Id.

The Exchange states that it would not have any role with respect to the negotiations between DPMs and payment accepting firms on the amount of the payment, including which payment accepting firms DPMs negotiate with to send their order flow to CBOE and the amount of the payment. Rather, the Exchange proposes to facilitate payment to payment accepting firms from fees collected from Market-Makers, e-DPMs, and DPMs. In those classes for which a DPM has advised the Exchange that it has negotiated with a payment accepting firm to pay for that firm's order flow, the Exchange would provide administrative support for the program. Specifically, the Exchange would keep track of the number of qualified orders each payment accepting firm directs to the Exchange, and would make the necessary debits and credits to the accounts of the DPMs, e-DPMs, Market-Makers, and the payment accepting firms to reflect the payments that are to be made. The Exchange represents that all of the funds generated by the fee would be used only to pay the firms for the order flow sent to the Exchange.

The Exchange believes that the \$.40 per contract is an equitable allocation of a reasonable fee among the CBOE's members. The CBOE states that it has designed this program to enable it to compete with other markets in attracting options order flow in multiply traded options. If a DPM advises the Exchange that it has negotiated a lower amount, the Exchange would refund to Market-Makers, e-DPMs, and DPMs the excess fee collected.

The CBOE proposes that the marketing fee be assessed only on transactions of Market-Makers (including e-DPMs and DPMs) resulting from orders for 200 contracts or less from customers of payment accepting firms. In the CBOE's view, because the marketing fee will be passed through to only those Market-Makers' transactions resulting

from orders from customers of a payment accepting firm that the DPM has independently negotiated with to pay for that firm's order flow, there will be a direct and fair correlation between those members who pay the costs of the marketing program funded by the fee and those who receive the benefits of the program.

According to the CBOE, it is important to note that although Market-Maker, DPM, and e-DPM transactions resulting from customer orders from firms that do not accept payment for their orders are not subject to the fee, Exchange Market-Makers, DPMs, and e-DPMs will have no way of identifying prior to execution whether a particular order is from a payment-accepting firm, or from a firm that does not accept payment for their order flow.<sup>8</sup>

## 2. Statutory Basis

The CBOE believes that because this marketing fee will serve to enhance the competitiveness of the Exchange and its members, this proposal is consistent with and furthers the objectives of the Act, including specifically Section 6(b)(5) thereof,<sup>9</sup> which requires the rules of exchanges to be designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, and Section 11A(a)(1) thereof,<sup>10</sup> which reflects the finding of Congress that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly

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<sup>8</sup> The Exchange has reinstated, in Interpretation and Policy .12 to CBOE Rule 8.7, the Marketing Fee Voting Procedures as a six-month pilot program by which a trading crowd may determine whether or not to participate in the Exchange's marketing fee program and to include e-DPMs into the Marketing Fee Voting Procedures. See Securities Exchange Act Release No. 50130 (July 30, 2004), 69 FR 47965 (August 6, 2004) (SR-CBOE-2004-47).

<sup>9</sup> 15 U.S.C. 78f(b)(5).

<sup>10</sup> 15 U.S.C. 78k-1(a)(1).

markets to assure fair competition among brokers and dealers and among exchange markets. The Exchange also believes that the proposed rule change is consistent with Section 6(b) of the Act,<sup>11</sup> and furthers the objectives of Section 6(b)(4) of the Act<sup>12</sup> in particular, in that it is designed to provide for the equitable allocation of reasonable dues, fees, and other charges among the CBOE's members.

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

The Exchange 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.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

The CBOE neither solicited nor received written comments with respect to the proposed rule change.

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

Because the foregoing rule change establishes or changes a due, fee, or other charge imposed by the Exchange, it has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act<sup>13</sup> and subparagraph (f) of Rule 19b-4 thereunder.<sup>14</sup> At any time within 60 days after the filing of the proposed rule change, the Commission may summarily abrogate the 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

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

<sup>12</sup> 15 U.S.C. 78f(b)(4).

<sup>13</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>14</sup> 17 CFR 240.19b-4(f).

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](mailto:rule-comments@sec.gov). Please include File Number SR-CBOE-2004-55 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-2004-55. 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 Room. Copies of the

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-2004-55 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.<sup>15</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>15</sup> 17 CFR 200.30-3(a)(12).