

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50673; File No. SR-CBOE-2004-52)

November 16, 2004

Self-Regulatory Organizations; Notice of Filing of a Proposed Rule Change and Amendment No. 1 Thereto by the Chicago Board Options Exchange, Incorporated to Amend its "Trigger" Rule to Permit RAES Orders to Automatically Execute Against Orders Resting on the Exchange's Limit Order Book

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 July 30, 2004, the Chicago Board Options Exchange, Incorporated ("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 submitted Amendment No. 1 to the proposal on September 23, 2004.<sup>3</sup> 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 "Trigger" rule (CBOE Rule 6.8(d)(v)) to permit RAES orders to automatically execute against orders resting on the Exchange's limit order book. Below is the text of the proposed rule change. Proposed additions are italicized; proposed deletions are [bracketed].

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**Chicago Board Options Exchange, Incorporated  
Rules**

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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, CBOE, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated September 22, 2004 and accompanying Form 19b-4 ("Amendment No. 1"). Amendment No. 1 replaced and superseded the original filing in its entirety.

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## Chapter VI – Doing Business on the Exchange Floor

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### **Rule 6.8 RAES Operations**

(a) – (d)(iv) No change.

(d)(v) Notwithstanding sub-paragraph (d)(iv), for classes of options as determined by the appropriate Floor Procedure Committee ("FPC"), for any series of options where the bid or offer generated by Autoquote (Exchange or proprietary) is equal to or crosses the Exchange's best bid or offer as established by an order in the Exchange's limit order book, orders in the book for options of that series will be automatically executed against participants on RAES ("Trigger") up to a size not to exceed the number of contracts equal to the applicable maximum size of RAES-eligible orders for that series of options ("Trigger Volume"). The appropriate FPC is responsible for determining the Trigger Volume for a particular series of options. In the event a member in the trading crowd verbally initiates a trade with a book order prior to the time the book staff announces to the trading crowd that the order has been removed from the book by Trigger, the book staff will manually endorse the book order to that member(s). In the event the order in the book is for a larger number of contracts than the applicable Trigger Volume, the balance of the book order may be executed manually by the trading crowd. In the limited circumstance where contracts remain in the book after an execution (or partial execution) of a book order up to the applicable Trigger Volume, the bid or offer generated by Autoquote will be one-tick inferior to the price of the book order such that the disseminated quote will not cross or lock with the Autoquote bid or offer. In addition, where contracts remain in the book after an execution (or partial execution) [In these instances], or for any series where Trigger has not yet been

implemented by the appropriate FPC, orders in RAES for options of that series may either [will not] be automatically executed [but instead] or [will] be rerouted on ORS to the crowd PAR terminal or to another location in the event of system problems or contrary firm routing instructions, as determined by the appropriate FPC on a class by class basis.

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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 the proposed rule change, as amended, and discussed any comments it received on the proposed rule change, as amended. 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

The Exchange proposes to amend CBOE Rule 6.8(d)(v), which governs the operation of the Exchange's AutoQuote Triggered Ebook Execution System ("Trigger"). The proposed rule change would affect how incoming orders submitted through the Exchange's Retail Automatic Execution System ("RAES") are treated at such time a locked or crossed market exists.

Trigger is a system that allows orders resting in CBOE's electronic book to be automatically executed in the limited situation where the bid or offer for a series of options generated by CBOE's AutoQuote system ("AutoQuote"), or any CBOE-approved proprietary quote generation system used in lieu of AutoQuote, locks or crosses CBOE's best bid or offer for

that series as established by such booked orders. The Trigger functionality does not apply to options traded on CBOE's Hybrid Trading System.

The current Trigger rule (CBOE Rule 6.8(d)(v)) provides that when the quote generated by AutoQuote locks or crosses a resting order in the book, the Trigger process is initiated and the book order up to the Trigger volume, which is set by the appropriate Floor Procedure Committee ("FPC"), is immediately removed from the book and a last sale is disseminated. Where any unexecuted balance remains in the book, it may be executed manually by the trading crowd or by others. During the entire Trigger process, incoming RAES orders do not automatically execute, and instead route to the PAR terminal, where the Exchange's Designated Primary Market-Maker represents them. As soon as the entire book order is removed from the book, the new AutoQuote value, unimpeded by a crossed or locked market, is disseminated and RAES again is available for automatic executions.

Under the proposed rule change, incoming RAES orders submitted during the Trigger process would be eligible to execute against those book orders that are crossed or locked by Autoquote. Specifically, if a balance remains on the book after the Trigger volume is removed from the book, incoming RAES orders would remain eligible for execution against the book order instead of routing to the PAR terminal for manual representation. The proposed rule change does not change the existing process for incoming RAES orders that are submitted prior to a locked or crossed market; these orders would continue to be executed in accordance with the RAES procedures set forth in CBOE Rule 6.8 (i.e., if an order in the Exchange's book constitutes the best bid or offer on the Exchange, the incoming RAES order will generally execute against the order in the book). The appropriate FPC would implement this Trigger enhancement on a class-by-class basis.

The Exchange believes that by allowing incoming RAES orders submitted during a locked or crossed market to be eligible for automatic execution, the number of corresponding orders routed to PAR for manual handling would decrease. As a result, the Exchange believes that the proposed rule change provides public customers with greater access to the Exchange's markets and more efficient execution of their RAES orders.

## 2. Statutory Basis

The CBOE believes the proposed rule change, as amended, is consistent with Section 6(b) of the Act,<sup>4</sup> in general, and furthers the objectives of Section 6(b)(5),<sup>5</sup> in particular, in that it should promote just and equitable principles of trade and serve to remove impediments to and perfect the mechanism of a free and open market and a national market system.

### 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 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

No written comments were solicited or received with respect to the proposed rule change.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date 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:

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

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

- A. by order approve such 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 e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-CBOE-2004-52 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-2004-52. 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, 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 SR-CBOE-2004-52 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>6</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>6</sup> 17 CFR 200.30-3(a)(12).