

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50736; File No. SR-CBOE-2004-68)

November 24, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Chicago Board Options Exchange, Inc. to Adopt a New Marketing Fee

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 October 29, 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. On November 2, 2004, CBOE submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> 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>4</sup> and Rule 19b-4(f)(2) thereunder,<sup>5</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 adopt a new marketing fee to be imposed on transactions of Market-Makers (including Designated Primary Market-Makers, or DPMs, and

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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 Andrew D. Spiwak, Director Legal Division and Chief Enforcement Attorney, CBOE, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission, dated November 2, 2004 ("Amendment No. 1"). Amendment No. 1 replaced the originally filed proposed rule text in full.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>5</sup> 17 CFR 240.19b-4(f)(2).

electronic Designated Primary Market-Makers, or e-DPMs) other than Market-Maker-to-Market-Maker transactions. The fee will be imposed at the rate of \$.22 per contract on all classes of equity options. Below is the text of the proposed rule change. Proposed new language is italicized; proposed deletions are in [brackets].

CHICAGO BOARD OPTIONS EXCHANGE, INC.

FEE SCHEDULE

1. Unchanged
2. MARKET MAKER, e-DPM & DPM MARKETING FEE (in option classes in which a DPM has been appointed) (6) \$.~~[40]~~22
- 3.-4. Unchanged

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.] at the rate of \$.22 per contract on all classes of equity options other than Market-Maker-to-Market-Maker transactions. This fee shall not apply to index options and options on ETFs. The fee shall apply to options on HOLDRs. Should any surplus of the marketing fees at the end of each month occur, those funds would be carried forward to the following month. The Exchange would then refund such surplus at

the end of the quarter, if any, on a pro rata basis based upon contributions made by the Market-Makers, e-DPMs and DPMs.

(7) – (14) No change.

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

Currently, the CBOE imposes a marketing fee of \$.40 per option contract on Market-Maker transactions, including transactions of DPMs and e-DPMs, in all classes of options in which a DPM has been appointed. The marketing fee is 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, and only with respect to orders from customers that are for 200 contracts or less.

The CBOE proposes to replace its current marketing fee that is assessed on DPM, e-DPM and Market Maker transactions in all equity option classes.<sup>6</sup> The CBOE states

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<sup>6</sup> On August 3, 2004, the Exchange amended its marketing fee to incorporate e-DPMs as part of the existing marketing fee. See Securities Exchange Act Release No. 50212 (August 18, 2004), 69 FR 52051 (August 24, 2004) (SR-CBOE-2004-55).

that the purpose of the new marketing fee plan is to provide the members of the Exchange with the ability to compete for the opportunity to trade with those orders that might otherwise be routed to other exchanges. The proposed marketing fee would be assessed whereby DPMs, e-DPMs and Market-Makers would be debited \$.22 for every contract they enter into on the Exchange other than Market-Maker-to-Market-Maker transactions, including all transaction between any combination of DPMs, e-DPMs, and Market-Makers. This fee would not apply to index options and options on ETFs, but would apply to options on HOLDRS.<sup>7</sup>

The CBOE states that all funds generated by the marketing fee would be collected by the Exchange and recorded according to the DPM, station, and class where the options subject to the fee are traded ("Trading Crowds"). The money collected would be disbursed by the Exchange according to the instructions of the DPM. According to the Exchange, those funds would be available to the DPM solely for those Trading Crowds where the fee was assessed and could only be used by that DPM to attract orders in the classes of options for which the fee was assessed. The CBOE states that funds collected from e-DPMs would only be used to attract order flow for the classes in which the e-DPM is appointed. According to the CBOE, the Marketing Fee Oversight Committee, which the Exchange's Board of Directors has previously established, would conduct a quarterly review to determine the effectiveness of the proposed marketing fee and may recommend to the Exchange that it modify the fee in the future based upon its effectiveness.

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<sup>7</sup> HOLDRS are trust-issued receipts that represent an investor's beneficial ownership of a specified group of stocks. See Interpretation and Policy .07 to CBOE Rule 5.3.

Similar to the current marketing fee program, the Exchange states that it would not be involved in the determination of the terms governing the orders that qualify for payment or the amount of any payment. The Exchange would provide administrative support for the program in such matters as maintaining the funds, keeping track of the number of qualified orders each firm directs to the Exchange, and making the necessary debits and credits to the accounts of the traders and the payment accepting firms to reflect the payments that are made. According to the CBOE, fees collected during a calendar month would only be available to the DPM for payment for that calendar month's order flow. The Exchange believes that the rate of \$.22 would generally result in all funds being paid out at the end of the calendar month.

The CBOE states that the Marketing Fee Oversight Committee would review, on a quarterly basis, any surplus. Should any surplus of the marketing fees at the end of each month occur, those funds would be carried forward to the following month. The Exchange would then refund such surplus at the end of the quarter, if any, on a pro rata basis based upon contributions made by the Market-Makers. The Exchange believes that refunds, if any, would be de minimis. Thus, the Exchange states that refunding any surplus at the end of a quarter, rather than on a monthly basis, would be more efficient for Exchange administration.

The Exchange believes that the \$.22 per contract is an equitable allocation of a reasonable fee among CBOE members and is designed to enable the CBOE to compete with other markets in attracting options order flow in multiply traded options.

According to the CBOE, it is important to note that Exchange Market-Makers, DPMs, and e-DPMs would 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.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act<sup>8</sup> in general, and furthers the objectives of Section 6(b)(4) of the Act<sup>9</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>10</sup> and subparagraph (f)(2) of Rule 19b-4 thereunder.<sup>11</sup> Accordingly, the proposal will take effect upon filing with the Commission. At any time

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<sup>8</sup> 15 U.S.C. 78f(b).

<sup>9</sup> 15 U.S.C. 78f(b)(4).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>11</sup> 17 CFR 240.19b-4(f)(2).

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 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-2004-68 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-2004-68. 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-2004-68 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>12</sup>

Margaret H. McFarland  
Deputy Secretary

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