

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-51370; File No. SR-CBOE-2005-22)

March 15, 2005

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Incorporated to Adopt an Inactivity Fee to be Charged Against Remote Market-Makers that Fail to Commence Quoting in Their Appointed Classes

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 March 15, 2005, 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 CBOE. 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

CBOE proposes to adopt an inactivity fee to be charged against Remote Market-Makers (“RMMs”) that fail to commence quoting in their appointed classes. The text of the proposed rule change is available on the CBOE’s Web site (<http://www.cboe.com>), at the CBOE’s Office of the Secretary, and at the Commission’s Public Reference Room.

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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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 Exchange received approval of its RMM Program on March 14, 2005.³ During the next several weeks, the Exchange will begin a solicitation process whereby members that are interested in becoming an RMM will submit to the Exchange their appointment requests.⁴ As the Exchange does not have unlimited systems bandwidth capacity to support an unlimited number of members quoting electronically in each product, it was necessary to develop procedures by which electronic quoting appointments would be allocated to members in the instance where demand (i.e., the number of members requesting an appointment) exceeds supply (i.e., the actual number of appointments). CBOE Rule 8.3A describes these procedures. In order to prevent a member that obtains an electronic appointment in a product from not initiating quoting in that product, the Exchange proposes to adopt an inactivity fee that would apply in two instances, as described below.

Retaining Appointment Without Quoting

This aspect of the proposed inactivity fee is structured to apply only in those rare instances when an RMM receives an appointment, retains its appointment, but does not submit quotes in that product during any portion of the rollout of the RMM Program. If an RMM receives an appointment and does not commence quoting in that appointed product within thirty days after the termination of the rollout of the RMM Program, the RMM would be assessed a

³ See Securities Exchange Act Release No. 51366.

⁴ CBOE Rule 8.4(d) describes the appointment process for RMMs.

\$1,000 inactivity fee and the Exchange would reallocate the product to the next member on the waiting list (in accordance with proposed CBOE Rule 8.3A.) The Exchange represents that the RMM Program rollout would terminate no sooner than July 15, 2005. The inactivity fee (and subsequent reallocation) would occur on a per product basis. For example, if during the requisite measurement period an RMM does not submit quotes in five products in which it requested and received an allocation, it would be assessed a \$5,000 fee and the five products would be reallocated.

Relinquishing Appointment Without Quoting

The second instance in which the inactivity fee would apply occurs when an RMM receives an appointment in a product and subsequently relinquishes its appointment in that product (prior to termination of the RMM Program rollout) without having submitted any quotes during the requisite period. Using the example above in which an RMM requested and received an appointment in five classes, a \$1,000 inactivity fee would be assessed for each product in which the RMM terminates its appointment prior to the end of the rollout of the RMM Program provided the RMM has not submitted any quotes prior to its relinquishing the appointment.

The CBOE believes that the imposition of an inactivity fee is necessary in order to prevent members from receiving appointments in products for which they have no ability to quote or no intention of quoting. Without the fee, members could obtain multiple appointments and choose not to quote. The CBOE believes that this would affect the overall viability of the RMM Program on two fronts. First, it would deprive the Exchange of transaction revenue and, second, it would prevent other members on the waiting list from quoting. The ability of one member to hoard appointments could severely affect the amount of liquidity offered by keeping other ready, willing, and able-to-quote members from quoting. In this regard, the CBOE

believes that the \$1,000 fee represents a conservative estimate of the amount of revenue the Exchange would lose when an RMM receives an appointment in a class but chooses not to submit quotes. An RMM very easily may avoid assessment of the fee simply by submitting quotes during any point of the rollout of the RMM Program.

The CBOE represents that members would have ample time to have their systems fully operational prior to the termination of the rollout of the RMM Program. In this regard, the Exchange anticipates notifying all RMMs of the products they have received as part of their appointment by approximately April 15, 2005. The Exchange anticipates that the RMM rollout will begin April 28, 2005. Even with respect to classes that rollout towards the end of the period, RMMs would still have no fewer than 30 days during which to quote before they are subject to being assessed an inactivity fee. In the event an RMM uses a leased membership to receive appointed products, the lessee (and not the lessor) would be assessed the fee. The Exchange believes it is reasonable to assess the fee upon the lessee in this instance because it is the party that requested the appointment, received the appointment, and failed to quote the appointment.

The Exchange provides for one exception to the inactivity fee. RMM organizations that relinquish appointments during the requisite period by virtue of the fact that they obtained an appointment in the identical product either as a Designated Primary Market-Maker (“DPM”) or Electronic DPM (“e-DPM”) would not be required to pay the inactivity fee. The Exchange believes it is reasonable to exempt an RMM from payment of the fee in this limited instance because it would be required to quote the product in its new status as DPM or e-DPM.

2. Statutory Basis

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.⁵ Specifically, CBOE believes the proposed rule change is consistent with Section 6(b)(4) of the Act⁶ in that it provides for the equitable allocation of reasonable dues, fees, and other charges among CBOE members.

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

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 comments.

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:

- (A) by order approve such proposed 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:

⁵ 15 U.S.C. 78f(b).

⁶ 15 U.S.C. 78f(b)(4).

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-2005-22 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-2005-22. 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-2005-22 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.⁷

Margaret H. McFarland
Deputy Secretary

⁷ 17 CFR 200.30-3(a)(12).