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SR-CBOE-2005-19

April 26, 2005

Mr. William Brodsky
Chairman
Chicago Board Options Exchange, Inc.
400 S. La Salle Street
Chicago, IL 60603

Re: **Chicago Board of Trade Exercise Right**

Dear Chairman Brodsky:

This letter is submitted for the consideration of the CBOE Board. As the Board is aware, the Chicago Board of Trade ("CBOT") formally demutualized on Friday, April 22, 2005, by extinguishing its status as a membership organization and becoming a Delaware stock corporation. In light of the demutualization, there are no longer are any "members" of the CBOT. That status has been extinguished; it ceases to exist. This structural change of the CBOT has significant consequences for the CBOE Board, the CBOE's members, and the former members of the CBOT.

A. The CBOT demutualization extinguished the CBOT erercise rights under the CBOE's Articles of Incorporation. The CBOT's extinguishment of memberships renders the exercise right for "members of the CBOT" set forth in Articles of Incorporation nugatory. Since there are no longer any members of the CBOT, the exercise right set forth in the Articles of Incorporation no longer confers an exercise right on any person. Thus, the CBOE Board no longer is authorized under the Articles of Incorporation to recognize any exercise right for any person. Consequently, the CBOE exercise memberships that have been enjoyed in the past by CBOT members who had exercised their rights to become CBOE exercise member pursuant to the CBOE's Articles of Incorporation should no longer be recognized and the CBOE exercise members should be excluded from the CBOE unless and until they purchase or rent a seat consistent with the requirements applicable to all persons seeking to purchase or rent CBOE seats.

B. The CBOE-CBOT Letter Agreements purporting to interpret the CBOE Articles of Incorporation are outside the CBOE Board's Authority. I am aware that prior CBOE Boards entered into letter agreements with the CBOT dated October 7, 2004 and August 1, 2001 (hereinafter, collectively, the "2001 Agreement"), which purport to agree to an interpretation of the CBOE Articles of Incorporation to the effect that the exercise right for members of the CBOT will continue to be recognized for certain stockholders of the CBOT after CBOT demutualization. As you know, it has been my view that such letter agreements, and the interpretation embodied within them, are without legal authority because the purported interpretation of the Articles of Incorporation that those agreements seek to validate constitutes

an amendment to the Articles of Incorporation and the CBOE Board lacks authority to amend the Articles of Incorporation. In this connection, the Articles of Incorporation, by their terms, do not permit amendments except pursuant to an 80% affirmative vote of the membership. The constraints on the Board's authority in this regard are absolute – amendments to the Articles of Incorporation may only be effected by an 80% affirmative vote of the membership. The Board is without authority to amend the Articles of Incorporation regardless of whether or not it acts in good faith or might be considered to be acting fairly with respect to an amendment it would favor.

C. The purported interpretion of the CBOE Articles of Incorporation embodied in the August1, 2001 and October 7, 2004 letter agreements with the CBOT is not effective, at a minimum, unless and until approved by the Securities and Exchange Commission ("SEC"). Even if the current CBOE Board would seek to rely on the purported interpretation of the Articles of Incorporation set forth in the 2001 Agreement with the CBOT, the Board is without authority to do so, at a minimum, unless and until the SEC, pursuant to Section 19 of the Exchange Act, approves the interpretation. The CBOE's prior actions and public statements agree with this. The CBOE expressly advised the SEC in its October 26, 2004 submission in *In re the Petition of Marshall Spiegel*, SEC File No. SR-CBOE-2004-16 (hereinafter "SR-CBOE-2004-16") that the purported interpretation in the 2001 Agreement, by its terms, is not effective and cannot become effective unless and until the SEC approves the rule change under Section 19. The CBOE, consistent with that view, submitted the purported interpretation in the 2001 Agreement for SEC review and approval on March 31, 2005. Currently, the SEC's review process is in a stage of receiving public comment and no SEC determination has been issued.

If the CBOE Board were to act in a manner that seeks to effectuate the purported interpretation in the 2001 Agreement prior to a final SEC approval of it, the CBOE would violate Section 19 of the Exchange Act. The SEC's February 25, 2005 Order in SR-CBOE-2004-16 anticipates this issue, stating at page 16: "To the extent . . . that any part of an agreement is a 'policy, practice, or interpretation' of the CBOE's rules and that 'policy, practice, or interpretation' has not been approved by the Commission it would be a violation of Section 19(b) of the Exchange Act and the Commission could take appropriate action against the CBOE."

D. The CBOE Board may not proceed with its purchase offer for purported CBOT exercise rights, at a minimum, unless and until the SEC approves the purported interpretation set forth in the 2001 Agreement. The CBOE also is without authority to proceed with its purchase offer to purchase purported CBOT exercise rights as described in the CBOE's press releases dated April 18, 2005 and March 1, 2005. That purchase offer was commenced solely on the basis of the SEC's approval of purported interpretation of the CBOE's Articles of Incorporation set forth in the CBOE's letter agreement with the CBOT dated September 17, 2003 ("the 2003 Agreement"). That letter agreement allegedly interpreted the

Article of Incorporation to provide that only persons who possess all of the constituent rights of a CBOT full membership will be recognized as "members of the CBOT" under the Articles of Incorporation. The purported interpretation in the 2003 Agreement, by its terms, was confined to addressing the purported interpretation of "member of the CBOT" exercise rights in the context of the CBOT being a membership organization. Neither the purported interpretation in the 2003 Agreement nor the SEC's final order approving it purport to determine the meaning of "members of the CBOT" after demutualization. Accordingly, based on the fact that the CBOT has now demutualized, the purported interpretation in the 2003 Agreement no longer has any legal effect and is not a basis for proceeding with a purchase offer.

Rather, as the CBOE itself previously has recognized, following demutualization, the continuation of the exercise right is governed by the purported interpretation in the 2001 Agreement, when and if approved by the SEC. Thus, the CBOE must await final SEC approval of the purported interpretation in the 2001 Agreement, if any in fact is given in the future, before it may proceed with a purchase offer from the purported owners of purported exercise rights.

I also note that it would be a breach of fiduciary duty for the Board to proceed with the purchase offer for exercise rights prior to SEC approval of the interpretation in the 2001 Agreement. Such action not only would violate the Exchange Act, but also involve the Board in an irrational offer to pay substantial sums for exercise rights that no longer exist and to pay them to persons who are not in fact members of the CBOT as defined at the time the CBOE's Articles of Incorporation were adopted or by any other plain meaning of the term. Further, such a purchase offer would disproportionately harm CBOE treasury seat members by, among other things, subjecting them a to substantial assessments to pay for non-existent exercise rights.

E. Summary. Following the CBOT's demutualization, the CBOE Board is without power to continue to recognize any exercise right under the CBOE's Articles of Incorporation, the exercise memberships of former CBOT members obtained pursuant to the now defunct exercise right in the Articles of Incorporation are extinguished and should no longer be recognized, and the CBOE must cease all efforts to pursue its anticipated purchase offer for CBOT exercise rights. In addition, even if the Board were to disagree with the foregoing, it is

without authority to pursue the purchase offer for purported exercise rights unless and until the SEC issues a final order approving the CBOE's purported interpretation in the 2001 Agreement.

I am available at the Board's convenience to discuss these matters.

Sincerely,

Marshall Spiegel

cc: All current CBOE Board Members
Joanne Moffic-Silver, Esq.
CBOE General Counsel