

section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6) thereunder⁴ and is, therefore, immediately 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

CBOE proposes to amend its rules governing the settlement procedures for its index options in certain unusual circumstances. Below is the text of the proposed rule change. New language is in italics; deleted language is in brackets.

* * * * *

Rule 24.7—Trading Halts, Suspensions, or Primary Market Closure

Rule 24.7.

(a)–(d) No change.

(e) When the primary market for a security underlying the current index value of an index option does not open for trading, *halts trading prematurely, or otherwise experiences a disruption of normal trading on a given day, or if a particular security underlying the current index value of an index option does not open for trading, halts trading prematurely, or otherwise experiences a disruption of normal trading on a given day in its primary market*, the price of that security shall be determined, for the purposes of calculating the current index value at expiration, [based on the opening price of that security on the next day that its primary market is open for trading. This procedure shall not be used if the current index value at expiration is fixed] in accordance with the Rules and By-Laws of The Options Clearing Corporation.

Interpretations and Policies: No change.

* * * * *

Rule 24.9—Terms of Index Option Contracts

Rule 24.9

(a)–(1)–(3) No Change.

(4) A.M.–Settled Index Options. The last day of trading for A.M.-settled index options shall be the business day preceding the last day of trading in the underlying securities prior to expiration. The current index value at the expiration of an A.M.-settled index option shall be determined, for all purposes under these Rules and the Rules of the Clearing Corporation, on the last day of trading in the underlying

securities prior to expiration, by reference to the reported level of such index as derived from first reported sale (opening) prices of the underlying securities on such day, except that [(i)]in the event that the primary market for an underlying security does not open for trading, *halts trading prematurely, or otherwise experiences a disruption of normal trading on that day, or in the event that the primary market for an underlying security is open for trading on that day, but that particular security does not open for trading, halts trading prematurely, or otherwise experiences a disruption of normal trading on that day*, the price of that security shall be determined, for the purposes of calculating the current index value at expiration, as set forth in Rule 24.7(e).[, unless the current index value at expiration is fixed in accordance with the Rules and By-Laws of The Options Clearing Corporation. (ii) In the event that the primary market for an underlying security is open for trading on that day, but that particular security does not open for trading on that day, the price of that security, for the purposes of calculating the current index value at expiration, shall be the last reported sale price of the security.]

Remainder of Rule: 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, CBOE 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 Item IV below. 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 prospect of imminent war with Iraq has again prompted CBOE to review its settlement procedures for index options to ensure that the final settlement value of such options converges with the corresponding values of the underlying stock index or stock index future, in the event of any market disruption. The Exchange believes that ensuring this convergence is vital to eliminating any unplanned arbitrage risk for public customers and

other investors, as was set forth in greater detail in a previous CBOE filing (SR-CBOE-2000-02).⁵

SR-CBOE-2000-02 amended CBOE Rules 24.7(e) and 24.9(a)(4) to ensure convergence of the values of options and their underlying securities in the event that a primary market for one or more of the component securities of such indexes failed to open. In making these changes, CBOE noted that it recognize[d] the authority of the Options Clearing Corporation ("OCC") to establish a final settlement value for index options in the event of a primary market closure pursuant to its Rules and By-Laws. The rule change proposed here makes clear that such action by the OCC would take precedence in determining any final index settlement value.⁶

The changes that CBOE made to its settlement rules in SR-CBOE-2000-02 were designed to mirror the rules of futures markets like the Chicago Mercantile Exchange ("CME"), which trades some of the index products underlying CBOE's index options. Since the approval of SR-CBOE-2000-02, however, the CME has changed its rules again. Even more importantly, the Commission recently approved changes to the OCC's rules and by-laws in order to give OCC "broad discretionary authority to adjust settlement values for OCC-cleared index options and futures whenever, and in whatever manner, OCC deems appropriate to avoid a disconnect between the futures and options markets or among the futures markets."⁷

In light of these changes, particularly those giving the OCC authority to ensure convergence between the settlement values of OCC-cleared index options and their underlying futures or other securities, the Exchange believes it can best ensure this convergence by amending CBOE Rules 24.7(e) and 24.9(a)(4) to make clear that—in cases where either a primary market for a security underlying the current index value of an index option, or just a particular such security, does not open for trading, halts trading prematurely, or otherwise experiences a disruption of normal trading—the price of that security shall be determined, for the purposes of calculating the current index value at expiration, in accordance

⁵ See Securities Exchange Act Release No. 42857 (May 30, 2000), 65 FR 36185 (June 7, 2000) (notice of filing of and Commission order granting accelerated approval to proposed rule change).

⁶ 65 FR at 36186.

⁷ See Securities Exchange Act Release No. 46561 (September 26, 2002), 67 FR 61943, 61944 (October 2, 2002) (Commission approval of SR-OCC-2002-09).

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).