

*the OTC Bulletin Board, Pink Sheets or similar trading system, and opening transactions have been prohibited pursuant to CBOE Rule 5.4, the Exchange shall monitor the activity or condition of the market and paragraph (e)(4) of this Rule shall not apply.*

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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 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. 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 proposed rule change would amend CBOE Rule 5.4 and add an interpretation to CBOE Rule 8.51 to address certain issues dealing with options that have closing-only restrictions. The proposed change to CBOE Rule 5.4 would give two floor officials, in consultation with a designated senior executive officer of the Exchange, the authority to prohibit opening purchase transactions for equity options whenever the Exchange has determined that an underlying security previously approved for Exchange option transactions does not meet the current requirements for continuance of such approval. For example, the proposed rule change would be applicable when a security underlying an option has been delisted and is subsequently traded on the OTC Bulletin Board, Pink Sheets or similar trading system. In the aforementioned situation, the rule would also permit certain types of opening transactions by members to accommodate the closing transactions of other market participants. Specifically, in these situations, the rule would permit: (i) Opening transactions by market-makers executed to accommodate closing transactions of other market participants and (ii) opening transactions by CBOE member organizations to facilitate the closing transactions of public customers executed as crosses pursuant to and in accordance with CBOE Rule 6.74(b) or (d) (Crossing Orders). Similar changes

are proposed to Interpretations and Policies .05 (to lift restrictions on opening transactions if the underlying security, which previously did not meet the Exchange's listing standards, again meets the Exchange's listing standards), .08 (for securities consisting of shares or other securities that represent interests in registered investment companies organized as open-end management investment companies, unit investment trusts or similar entities) and .09 (for Trust Issued Receipts). Currently, the Exchange has the authority to prohibit an opening purchase transaction in an option, but must seek approval through the Office of the Chairman. This proposed rule change to grant this authority to two floor officials and a senior executive officer of the Exchange would make CBOE Rule 5.4 consistent with other CBOE rules involving trading halts and similar types of actions for index options and provides for greater efficiency when invoking a restriction or prohibition in a delisted or restricted option class.<sup>4</sup>

The proposed change to Interpretation and Policy .11 under CBOE Rule 8.51 deals with the implementation of non-firm mode for options that are restricted to closing-only transactions. Currently, CBOE Rule 8.51(e)(4) requires that when a series or class of option is in non-firm mode for purposes of the firm quote rule, the DPM and floor officials must review and reaffirm the condition of the market every 30 minutes. The proposed change to the interpretation and policies of CBOE Rule 8.51 sets forth that in situations in which opening transactions have been prohibited in an option where the underlying security has been delisted and is subsequently traded on the OTC Bulletin Board, Pink Sheets or a similar trading system, and the Exchange has invoked that only closing transactions may occur, as set forth above, the Exchange would monitor the activity or condition of the market. However, the DPM and floor officials would not be required to review and reaffirm the market conditions causing the non-firm mode designation every 30 minutes. The Exchange believes it is necessary to invoke non-firm mode pursuant to Exchange Rule 8.51(e) when a security is no longer listed on a national securities exchange or traded through a national securities association and reported as a national market system security, due to the fact that the Exchange is unable to directly receive an electronic quotation feed from the

OTC Bulletin Board or Pink Sheets. The Exchange believes that in these specific situations, the Exchange is incapable of collecting quotations in the underlying security that accurately reflect the true state of the market. For these options, the market conditions that caused the non-firm mode designation will not change. Therefore, the Exchange believes that the need to review market conditions every 30 minutes is not necessary.<sup>5</sup> In addition, the Exchange would be required to notify investors of the non-firm mode through the dissemination of a message code via OPRA. Furthermore, the Exchange would issue a Regulatory Circular to its members reflecting trading restrictions as described above.

#### **2. Statutory Basis**

The Exchange believes the proposed rule change is consistent with Section 6(b) of the Act<sup>6</sup> in general and furthers the objectives of Section 6(b)(5)<sup>7</sup> in particular in that it promotes just and equitable principles of trade and protects investors and the public interest. Further, the Exchange believes that the proposed rule change to CBOE Rule 5.4 promotes just and equitable principles of trade by granting floor officials authority along with a senior executive officer of the Exchange, which is consistent with authority granted to floor officials and a senior executive officer of the Exchange in other Exchange rules dealing with similar situations, such as trading halts and those applicable to index options.

The proposed change to the Interpretation and Policy .11 of CBOE Rule 8.51 is designed to protect investors and the public interest. Since the market conditions for options that are subject to closing-only restrictions are not likely to change, the need to review and reaffirm the market conditions every 30 minutes is not necessary in a closing transaction only restriction situation.

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

The CBOE believes that the proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

<sup>5</sup> The Exchange represents, and the proposed rule would require, that the Exchange would monitor the market conditions, as is required by Rule 11Ac1-1 under the Act. 17 CFR 240.11Ac1-1.

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

<sup>4</sup> See Exchange Rules 6.3 Trading Halts and Rule 24.7 Trading Halts, Suspensions, or Primary Market Closure.