

out, and when to roll them out, will be made by the Equity Floor Procedures Committee. The Exchange hopes to expand the rollout to the Top 200 classes by January 2004 and by the fourth quarter of 2004, to expand the rollout to the 500 most active equity options. The Exchange intends to implement Hybrid floor-wide in all classes by the fourth quarter of 2006.

#### *Non-Hybrid Classes*

For classes in which Hybrid is not yet operational, market makers will continue to be able to input manual quotes and receive allocations of incoming orders that execute against those quotes, as prescribed by existing CBOE Rule 6.8(d)(vi). Following is a descriptive summary of the new rules and the amended rules for the new Hybrid System.

#### **Rule 6.13 CBOE Hybrid System's Automatic Execution Feature**

This rule governs the automatic execution of incoming electronic customer and certain broker-dealer ("BD") orders. Just as CBOE Rule 6.8 has no application to classes trading on Hybrid, this Rule is only applicable to classes trading on Hybrid. The allocation of electronically executed orders in Hybrid shall be pursuant to new CBOE Rule 6.45A.

Proposed section (b) governs aspects of the automatic execution feature, including defining eligible orders and eligible order size, the process for automatic execution, split price executions, and executions against orders in the electronic book.

#### *Eligible Orders and Order Size*

This section clarifies that eligible orders may be automatically executed in accordance with the provisions of this Rule. Hybrid creates two broad categories of orders that will be eligible for automatic execution. First, orders from non-broker-dealer public customers and non-market maker broker-dealers will be eligible for automatic execution for the same number of contracts. Second, consistent with current CBOE Rule 6.8.01, the appropriate floor procedure committee ("FPC") may determine that orders from market makers and specialists may be eligible for automatic execution. Orders not eligible for automatic execution instead will route to PAR, BART, or to the order entry firm's booth printer.<sup>6</sup> All BD orders of a particular origin code

will be routed to the same location (e.g., all orders designated by the "N" origin code (non-CBOE market makers) will route to the firm's booth). Any changes to the routing parameters of non-auto-ex eligible BD orders will be made by the appropriate FPC and announced to the membership via regulatory circular.

As is the case today, the appropriate FPC shall determine on a class-by-class basis the maximum size of orders entitled to receive automatic execution through Hybrid. If the eligible order size exceeds the disseminated size, incoming eligible orders shall be entitled to receive an automatic execution up to the disseminated size. Similarly, if the appropriate FPC determines to allow market makers to access the automatic execution feature of Hybrid, it may also determine to establish the maximum order size eligibility for such orders at a level lower than the maximum order size eligibility for non-broker-dealer public customers and non-market-maker broker-dealers.

#### *Split-Price Executions*

Eligible orders will be automatically executed. Eligible orders for a size greater than the disseminated size will be automatically executed in part, up to the disseminated size. The balance of the order if marketable will execute automatically at the revised disseminated price up to the revised disseminated size (provided it does not violate NBBO, in which case it will route to PAR or BART).<sup>7</sup> If not marketable, the balance of the order will book electronically.

#### *Automatic Executions at Prices Inferior to NBBO*

When CBOE is not the NBBO, eligible orders will not automatically execute and instead, shall route to the DPM's PAR terminal for non-automated handling. Alternatively, order entry firms will have the ability, at their discretion, to have these orders route to the firm's booth instead of PAR. Eligible orders received while the CBOE market is locked (e.g., \$1.00 bid—\$1.00 offered) shall be eligible for automatic execution on CBOE at the disseminated quote, provided that CBOE's disseminated quote is not inferior to the NBBO, in which case the order will either route to the DPM's PAR terminal or the firm's booth.

#### *Users, Order Entry Firms, and Prohibited Practices*

CBOE Rule 6.13(c) defines "User" as any person or firm that obtains

electronic access to the automatic execution feature of the CBOE Hybrid System through an Order Entry Firm. The term "Order Entry Firm" ("OEF") means a member organization of the Exchange that is able to route orders to the Exchange's Order Routing System.

Order Entry Firms are required to comply with all applicable CBOE options trading rules and procedures. They are required to provide written notice to all Users regarding the proper use of the CBOE Hybrid System, including any automated execution features. The Rule also requires OEFs to Maintain adequate procedures and controls that will permit the OEF to effectively monitor and supervise the entry of electronic orders by all Users. OEFs must monitor and supervise the entry of orders by Users to prevent the prohibited practices set forth below. These requirements are identical to those contained in CBOE Rule 6.8(e).

This section also incorporates the provisions found in current CBOE Rules 6.8 and 6.8A regarding prohibited practices. In this respect, prohibited practices include but are not limited to the following:

1. Dividing an order into multiple smaller orders for the purpose of meeting the eligible order size requirements for automatic execution ("unbundling").
2. The electronic generation and communication of orders (and cancellations) in violation of CBOE Rule 6.8A by non-trading crowd participants.
3. Effecting transactions that constitute manipulation as provided in CBOE Rule 4.7 and Rule 10b-5 under the Act.

#### *Trade Nullification Procedure*

A trade executed on the CBOE Hybrid System may be nullified if the parties to the trade agree to the nullification. When all parties to a trade have agreed to a trade nullification, one party must contact the Help Desk, which will confirm the agreement and disseminate cancellation information in prescribed OPRA format.

#### *Removal of Unreliable Quotes*

The Exchange incorporates from existing CBOE Rule 6.8.02 language pertaining to the removal of unreliable quotes or markets from NBBO calculation. To summarize, floor officials may remove unreliable quotes in one or more options classes upon: (1) Direct communication from the affected market or the dissemination through OPRA of a message indicating that disseminated quotes are not firm; or (2) direct communication from the affected market that it is experiencing systems or

<sup>6</sup> BART is the Booth Automated Routing Terminal that enables firms to maintain orders in electronic format. Orders routed to the firm's booth, as opposed to BART, will print at the booth and must be handled by the firm manually.

<sup>7</sup> The balance of the order will only route to BART if the order entry firm so requests.