

orders through the auto-ex feature of Hybrid.

Rule 8.7. Obligations of Market Makers

CBOE Rule 8.7 governs market maker obligations. Market Makers on the CBOE Hybrid System will continue to be subject to the obligations imposed by this rule, as amended.

The proposed change to section (b)(ii) of CBOE Rule 8.7 clarifies that market makers will be obligated to honor their quotes for up to their disseminated size, in accordance with the Quote Rule. Under Hybrid, market makers will be deemed the "responsible broker or dealer" for quotes they cause to be disseminated. Currently, the entire trading crowd is considered the "responsible broker or dealer." This represents a fundamental change and will also be reflected in CBOE Rule 8.51.

The proposed change to section (b)(iii) of CBOE Rule 8.7 imposes upon market makers an obligation to ensure that their quotes are accurate. This section also provides guidance as to the permissible methods by which market makers may quote. Under Hybrid, market makers will be able to quote verbally by open outcry in response to a request for a market or they may quote electronically (or submit orders electronically) by use of an exchange-approved quoting device. This rule also clarifies that market makers must be physically present in the trading crowd to quote and submit orders. This is designed to prevent remote market making.

The Exchange proposes to adopt new paragraph (d) to CBOE Rule 8.7 to govern market maker obligations in Hybrid classes. The proposed obligations in paragraph (d) will only apply to market makers trading classes on the CBOE Hybrid System and only in those Hybrid classes. As such, this section has no applicability to non-Hybrid classes. Proposed paragraph (d) to CBOE Rule 8.7 clarifies that unless otherwise provided in this Rule, market makers on the Hybrid System are subject to all obligations imposed by CBOE Rule 8.7. To the extent another obligation contained elsewhere in CBOE Rule 8.7 is inconsistent with an obligation contained in paragraph (d) of Rule 8.7, paragraph (d) shall govern.

The Exchange proposes an introductory rollout period with respect to the obligations contained in paragraph (d). Accordingly, for a period of ninety (90) days commencing immediately after a class begins trading on the Hybrid System, the provisions of proposed paragraph (d)(i) shall govern trading in that class. Upon completion of this 90-day rollout period, a market

maker's electronic trading volume will determine whether (d)(i) or (d)(ii) shall govern his trading activities, as described more fully below.

The Exchange notes that the requirements in proposed paragraph (d) to CBOE Rule 8.7 will be applicable on a per class basis depending upon the percentage of volume a market maker transacts electronically versus in open outcry. In making this determination, the Exchange will monitor market makers' trading activity every calendar quarter to determine whether they exceed the thresholds established below in paragraph (d)(i). If a market maker exceeds the threshold established below, the obligations contained in (d)(ii) will be effective the next calendar quarter.

Proposed Rule 8.7(d)(i) Market Maker Trades Less Than 20% Volume Electronically

If a market maker on the CBOE Hybrid System transacts 20% or less of his contract volume electronically in an appointed Hybrid class during any calendar quarter, the following provisions shall apply to that market maker in that class:

(A) Quote Widths: With respect to electronic quoting, the market maker will not be required to comply with the quote width requirements of CBOE Rule 8.7(b)(iv).

(B) Continuous Electronic Quoting Obligation: The market maker will not be obligated to quote electronically in any designated percentage of series within that class. If a market maker quotes electronically, its undecrement quote must be for at least ten contracts.

(C) Continuous Open Outcry Quoting Obligation: In response to any request for quote by a floor broker or DPM representing an order as agent, market makers must provide a two-sided market complying with the current quote width requirements contained in CBOE Rule 8.7(b)(iv) for a minimum of ten contracts.

(D) In-Person Quoting Requirement: Any volume transacted electronically will not count towards the market maker's in-person requirement contained in CBOE Rule 8.7.03(B).

Proposed Rule 8.7(d)(ii) Market Maker Trades More Than 20% Volume Electronically

If a market maker on the CBOE Hybrid System transacts more than 20% of his contract volume electronically in an appointed Hybrid class during any calendar quarter, beginning the next calendar quarter he will be subject to the following quoting obligations in that

class for as long as he remains in that class:

(A) Quote Widths: The market maker must comply with the quote width requirements contained in Rule 8.7(b)(iv).

(B) Continuous Quoting Obligation: A market maker will be required to maintain continuous two-sided quotes for at least ten contracts (undecrement size) in a designated percentage of series within the class, in accordance with the schedule below:

| <i>% of Overall Class Volume Transacted on CBOE During the Previous Quarter that was Transacted Electronically</i> | <i>Electronic Quoting % Requirement (Percentage of series)</i> |
|--|--|
| 50% or Below | 20 |
| 51-75% | 40 |
| Above 75% | 60 |

The Exchange will monitor on a calendar quarter basis the percentage of business transacted electronically on CBOE in each particular class for the purpose of adjusting the applicable electronic quoting percentage during the next succeeding calendar quarter. For example, if during the preceding calendar quarter 83% of the volume transacted on CBOE in a particular class is done electronically, market makers subject to paragraph (d)(ii) of CBOE Rule 8.7 will have an obligation to make continuous markets in 50% of the series trading in that class.

(C) Continuous Open Outcry Quoting Obligation: In response to any request for quote by a floor broker or DPM representing an order as agent, market makers must provide a two-sided market complying with the current quote width requirements contained in Rule 8.7(b)(iv) for a minimum of ten contracts.

The Exchange proposes minor non-substantive wording changes to Interpretation .02 to CBOE Rule 8.7. First, in Interpretation .02, the Exchange removes the first six words of the sentence "although each pricing decision has many elements" as they are superfluous.

The change to Interpretation .05 imposes a minimum quote size obligation upon market makers. Specifically, market maker quotes may not be for less than ten contracts. The Exchange notes that this size obligation only applies to a market maker's initial undecrement quote. Accordingly, if a market maker puts up a quote for 20 contracts and an incoming order executes against 15 of those contracts causing the market maker's disseminated size to decline to five