

regarding the non-eligibility of BD orders for entry into the book.

The changes to proposed section (b) clarify that orders from market participants may be placed in the book (whether the order first routes to the OBO or directly into the book). The Exchange proposes to limit the applicability of paragraph (g) to non-Hybrid classes because "live ammo" functionality will not be available in Hybrid.

The Exchange proposes to delete existing Interpretation .05 to CBOE Rule 7.4 as obsolete. The Order Support System has been absent from the Exchange for more than ten years. Finally, the Exchange amends current Interpretation .07 by renumbering it as .06 and by adding reference to the automatic execution provisions of new CBOE Rules 6.13 and 6.45A.

Rule 7.7 Displaying Bids and Offers in the Book

The exchange also amends CBOE Rule 7.7 regarding the display of orders in the book. Specifically, the Exchange removes as obsolete the section of the rule that allows the OBO to display indications of book size when the book contains orders for at least 25 contracts. Because the Exchange currently disseminates the actual size of orders in the book, this section is obsolete. The Exchange also deletes Interpretation .01 in its entirety as obsolete.²²

Rule 8.51 Firm Disseminated Market Quotes

The Exchange proposes to amend CBOE Rule 8.51(a)(1) to clarify that in Hybrid classes, the market participant who submits a quote that is disseminated shall be the responsible broker or dealer for that quote. In paragraph (c)(1), the Exchange removes the sentence indicating it will periodically publish the firm quote requirement for both BD and public customer orders. In this respect, the Exchange notes that in new subparagraph (c)(1)(a)(i) to CBOE Rule 8.51 the firm quote requirement for customer orders shall be the size disseminated to vendors. In subparagraph (a)(ii), the Exchange clarifies that the firm quote requirement for BD orders will be the lesser of the size it disseminates to vendors or publishes in a different manner. This is almost identical to the current rule except that it provides flexibility to

allow the Exchange to disseminate its BD firm quote size (rather than publish it).

The Exchange also strikes existing Rule 8.51(c)(2)(a) as obsolete. In this respect, the Exchange disseminates actual size regardless of whether that size represents autoquote, an order in the book, or both. In any instance, the Exchange is firm for its disseminated size, as required by proposed CBOE Rule 8.51(c)(1)(a)(i).

The Exchange proposes to delete current Interpretation .01 and replace it with the definition of "Responsible broker or dealer" contained in Rule 11Ac1-1(a)(21) under the Act. The Exchange deletes the existing portion of Interpretation .01 as obsolete. In this respect, the Exchange disseminates the actual size of its firm quote obligation that, intuitively, can never be less than the disseminated size. The Exchange also amends Interpretation .02 to replace reference to the terms floor broker, DPM, or OBO with the term market participant. Because under Hybrid, the market participant will be the responsible broker or dealer, it will be responsible for removing its quote.

The proposed amendment to Interpretation .08 does not change the intent of the rule: that the responsible broker or dealer not be required to honor quotes that are erroneous as the result of a third party. Because the trading crowd will not be the responsible broker or dealer in Hybrid, however, the Exchange amends the rule to remove reference to the trading crowd.

Finally, CBOE proposes a change to Interpretation .10 to clarify the timing of when firm quote obligations attach. Currently, firm quote obligations attach to an order received on a PAR station at the time the order is received on PAR. This interpretation remains intact for non-Hybrid classes. For Hybrid classes, firm quote obligations will attach to an order received on a PAR station depending upon who is the responsible broker or dealer. If the responsible broker or dealer is not the DPM, firm quote will attach when the order is announced to the trading crowd. If, however, the DPM is a responsible broker or dealer for that order, firm quote obligations attach at the time of receipt of that order on PAR. The Exchange notes that in instances when an order is received on PAR when the disseminated quote represents the DPM and other market makers, there will be two separate firm quote obligations: the DPM's firm quote obligation will attach at the time the order is received on PAR while the market makers' firm quote

obligations will attach when the order is announced to the crowd.²³

Rule 8.85 DPM Obligations

To accommodate Hybrid, the Exchange proposes to amend CBOE Rule 8.85 regarding DPM obligations. First, the Exchange proposes to amend CBOE Rule 8.85(a)(i) to indicate that a DPM has a continuous quoting obligation with respect to its assigned classes. This ensures the DPM will quote at all times. Second, the Exchange clarifies subsection (ii) to indicate that the DPM must assure that each of its quotations is honored in accordance with the requirements of the Quote Rule. This change clarifies that DPMs must ensure their own compliance with the Quote Rule. Finally, the Exchange restricts the applicability of subparagraph (x) to non-Hybrid classes. In Hybrid, all market participants will have their own proprietary quoting systems. It would be anticompetitive to require the DPM to disclose its pricing formula to other members. In non-Hybrid classes, because there is only one autoquote that binds the entire crowd, this requirement remains.

2. Statutory Basis

The CBOE Hybrid System will provide investors with deeper and more liquid markets, will provide market participants with substantially enhanced incentives to quote competitively, and will provide order entry firms with a trading platform the exchange believes is most conducive to satisfying their best execution and due diligence obligations. For these reasons, the Exchange believes the proposed rule change is consistent with the Act and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act.²⁴ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)²⁵ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative

²³ Market makers in the crowd have no control over PAR and no access to PAR. They will be completely unaware that an order resides on PAR until that order is announced to them. Contrast this to the present situation where even though a market maker may be unaware of the receipt of an order on PAR, because the disseminated quote represents the entire trading crowd, the entire crowd is deemed to receive the order upon receipt of the order on PAR. In Hybrid, each quote represents a completely different entity and not the crowd.

²⁴ 15 U.S.C. 78f(b).

²⁵ 15 U.S.C. 78f(b)(5).

²² Exchange quote display systems automatically incorporate into the disseminated market quote all booked orders that improve the market (price or size). For this reason, the OBO does not have any ability to display the full (or less than full) size of an order.