

Rule 8.7 Obligations of Market Makers

- (a)–(c) No change
 (d) No Change
 (i) Market Maker Trades Less Than 20% Contract Volume Electronically: No change
 (A)–(B) No change
 (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 quote width requirements contained in Rule 8.7(b)(iv) for a minimum of ten contracts *for non-broker-dealer orders and one contract for broker-dealer orders.*
 (D) No change
 (ii) Market Maker Trades More Than 20% Contract Volume Electronically: No change
 (A)–(B) No change
 (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 *for non-broker-dealer orders and one contract for broker-dealer orders.*

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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 Exchange 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 Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**1. Purpose**

In May 2003, the Commission approved trading rules for Hybrid,⁵ a trading platform that alters the fundamental way in which the

Exchange conducts business. Hybrid merges the electronic and open outcry trading models and offers market participants the ability to stream electronically their own quotes. Previously (and currently in non-Hybrid classes), CBOE's disseminated quote represented, for the most part, the Designated Primary Market Maker's ("DPM") autoquote price. Market makers ("MMs") were able to affect changes to that quote in open outcry (or by putting up manual quotes). Hybrid offers in-crowd MMs and in-crowd DPMs the opportunity to submit their own firm disseminated market quotes that represent their own trading interest.⁶ In addition, Hybrid permits in-crowd floor brokers, who represent orders on behalf of members, broker-dealers, public customers, and the firm's proprietary account, to enter orders on behalf of their customers for display in the CBOE's best bid or offer ("BBO").⁷ Whereas, prior to Hybrid, there was only one autoquote price comprising the CBOE disseminated quote, Hybrid allows for the introduction of multiple quotes in the quoting equation.

CBOE Rules 8.7(d)(i)(C) and (d)(ii)(C), which only apply to classes trading on Hybrid, impose a 10-up size requirement for MMs responding to a request for a market in open outcry by a floor broker ("FB") representing an order as agent.⁸ CBOE represents that the intent of CBOE Rules 8.7(d)(i)(C) and (d)(ii)(C) when adopted was to ensure that FBs representing public customer orders would receive a quote of sufficient depth whenever they requested a market in open outcry. CBOE believes that the plain language of CBOE Rules 8.7(d)(i)(C) and d(ii)(C), however, is overbroad and could be interpreted to apply to broker-dealer ("BD") orders represented by FBs. Accordingly, the Exchange proposes to amend these two rule provisions to: (a) Limit the applicability of the 10-up size guarantee to public customer orders represented by FBs; and (b) provide that MMs must provide a one-up market to BD orders represented by FBs. This proposed change only affects Hybrid classes and, as such, has no applicability to non-Hybrid classes.

CBOE represents that the proposed changes do not affect the operation of

CBOE's Quote Rule (CBOE Rule 8.51), which allows the responsible BD to provide separate quote sizes to public customers and broker-dealers.⁹ FBs representing a public customer order in a Hybrid class will be able to request a quote on behalf of such public customer from MMs in the crowd and will be guaranteed to receive a firm quote for at least ten contracts. At the same time, a FB representing a BD order in a Hybrid class will be able to request a quote on behalf of a BD and will be guaranteed to receive a firm quote for at least one contract. Accordingly, allowing MMs to provide 1-up open outcry markets to BD orders is consistent with their obligations under the CBOE Quote Rule because the BD firm quote requirement, which is one contract, is satisfied.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6(b) of the Act¹⁰ in general, and furthers the objectives of section 6(b)(5) of the Act¹¹ in particular, in that it is designed to promote just and equitable principles of trade, to prevent fraudulent and manipulative acts and practices, and, in general, to protect investors and the public interest.

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

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

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

CBOE neither solicited nor received written comments with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change (1) does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) by its terms, does not become operative until 30 days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, and the Exchange provided the Commission with written notice of its intent to file

Division, CBOE, and Frank N. Genco, Attorney, Division of Market Regulation ("Division"), Commission, on August 19, 2003.

⁵ See Exchange Act Release 47959 (May 30, 2003), 68 FR 34441 (June 9, 2003) (approving File No. SR-CBOE-2002-05).

⁶ Telephone conversation between Steve Youhn, Legal Division, CBOE, and Kelly M. Riley, Senior Special Counsel, Division, on August 20, 2003.

⁷ *Id.* Pursuant to CBOE Rule 6.75, floor brokers generally may not execute any orders for which they have been vested with the discretion to choose: the class of options to buy/sell, the number of contracts to buy/sell, or whether the transaction would be one to buy or sell.

⁸ CBOE Rule 8.7(d) only applies to Hybrid classes.

⁹ The BD firm quote requirement on CBOE is one contract. See CBOE Rule 8.51.

¹⁰ 15 U.S.C. 78f(b).

¹¹ 15 U.S.C. 78f(b)(5).