

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-56792; File No. SR-CBOE-2006-99)

November 15, 2007

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Amendment Nos. 2 and 3 to Proposed Rule Change Relating to FLEX Options Trading and Order Granting Accelerated Approval to Proposed Rule Change as Amended

I. Introduction

On November 27, 2006, the Chicago Board Options Exchange, Incorporated ("Exchange" or "CBOE") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change providing for the trading of Flexible Exchange ("FLEX") Options on a new electronic platform, and to make certain corresponding revisions to its existing open-outcry FLEX rules. On August 17, 2007, CBOE filed Amendment No. 1 to the proposed rule change. On August 30, 2007, the proposed rule change, as amended, was published for comment in the Federal Register.³ No comments were received on the proposal. On November 7, 2007 and November 15, 2007, CBOE filed Amendment Nos. 2 and 3, respectively, to the proposed rule change.⁴ This notice and order solicits comments from interested persons on Amendment Nos. 2 and 3 and grants accelerated approval to the proposed rule change, as amended.

II. Description of Proposal

FLEX Options provide investors with the ability to customize basic option features including size, expiration date, exercise style, and certain exercise prices. Currently,

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Securities Exchange Act Release No. 56311 (August 23, 2007), 72 FR 50133.

⁴ See infra Section II(D).

Exchange members may trade FLEX Options in open outcry. Markets are created when a member submits a request for quotes ("RFQ") to the crowd. This system is referred to herein as the "FLEX RFQ System." The Exchange has proposed an alternate framework for trading FLEX Options using a "hybrid" platform, which will incorporate both open outcry and electronic trading functionality (referred to herein as the "FLEX Hybrid Trading System" or the "System"). Some key features of the new FLEX Hybrid Trading System are the following:

- Method of Operation: Transactions can take place through either an open-outcry RFQ process similar to the existing FLEX RFQ System or a new, Internet- and API-based electronic trading platform. Currently, the FLEX RFQ System does not provide for a book, and quotes and orders expire at the conclusion of the RFQ process. By contrast, the new System may allow FLEX Orders to be entered and trade via an electronic book (the "Book"). The Exchange would determine on a class-by-class basis whether to make a Book available.⁵
- Access: CBOE members seeking to use the new System must apply to and be approved by the Exchange. Approved members are collectively referred to as "FLEX Traders." In addition, non-members that meet certain conditions may be offered "sponsored access" to the new System.
- Market-Maker Participation: As with the existing FLEX rules, there are two types of FLEX Market-Makers: FLEX Appointed Market-Makers and FLEX Qualified Market-Makers. The responsibilities and obligations of FLEX Market-Makers on the new System, and changes to the corresponding rules of the existing FLEX RFQ System, are discussed further below.

⁵ See Rule 24B.5(b)(1).

Detailed Summary of Proposed Rule Change

A. Proposed FLEX Hybrid Trading System Rules (Chapter XXIVB)

The rules governing the existing FLEX RFQ System are contained, and will continue to be maintained, in Chapter XXIVA of the Exchange rules. The proposed rules governing the new FLEX Hybrid Trading System are found in proposed Chapter XXIVB. The Exchange currently intends to maintain and operate both systems and will determine which system to use on a class-by-class basis. These determinations will be announced to the membership via regulatory circular. This rule further explains that Chapters I through XIX and XXIV of the Exchange rules apply to the new System, except as otherwise indicated. If the rules in Chapter XXIVB are inconsistent with other Exchange rules, the rules in Chapter XXIVB take precedence in relation to the trading of FLEX Options on the new System.

1. Definitions (Proposed Rule 24B.1)

Proposed Rule 24B.1, Definitions, corresponds with existing Rule 24A.1 but contains several new definitions necessary to accommodate the new System. For example, the term "FLEX Hybrid Trading System" means the Exchange's trading platform that allows FLEX Traders to submit RFQs, FLEX Quotes, and FLEX Orders. A "FLEX Quote" is a bid or offer entered by a FLEX Market-Maker or an order to purchase or sell entered by a FLEX Trader, in either case in response to an RFQ. A "FLEX Order" is a bid or offer entered by a FLEX Market-Maker or an order to purchase or sell entered by a FLEX Trader, in either case into the Book.

Proposed Rule 24B.1 also defines several terms relating to the RFQ process. The "Submitting Member" is the FLEX Trader who initiates the RFQ or who enters a FLEX Order into the Book. The "RFQ Response Period" is the period during which FLEX Traders

may provide FLEX Quotes in response to an RFQ. The "RFQ Reaction Period" is the period during which the Submitting Member determines whether to accept or reject the RFQ Market.⁶ The "RFQ Market" consists of the FLEX Quotes entered in response to an RFQ and FLEX Orders resting in the Book. An "RFQ Order" is an order to buy or an order to sell entered by the Submitting Member during the RFQ Reaction Period.

Proposed Rule 24B.1 also identifies certain trade conditions that can be placed on an RFQ Order or FLEX Order, such as fill-or-kill, all-or-none, minimum fill, "lots of," and hedge. FLEX Orders except for fill-or-kill orders would be designated by the System as day orders and, if unexecuted, would be canceled at the close of each trade day. An RFQ may include a hedge or "Intent to Cross" trade condition, discussed more fully below. Hedge and Intent to Cross trade conditions will be disclosed on the System.

2. Terms of FLEX Options (Proposed Rule 24B.4)

Proposed Rule 24B.4, Terms of FLEX Options, is similar to existing Rule 24A.4. Both rules set forth the variable terms of FLEX Options (such as the underlying security or index, put or call type, exercise style, expiration date, and exercise price). Other terms are not variable and are the same as those that apply to Non-FLEX Options. Both rules set forth the information required from a member who initiates an RFQ, such as the type and form of quote sought, any trade conditions, and the length of the RFQ Response Period.⁷

Proposed Rule 24B.4 lists additional contract and transaction specifications for RFQs, FLEX Quotes, FLEX Orders, and RFQ Orders. These specifications pertain in part to

⁶ See proposed Rule 24B.1(u) (as modified by Amendment No. 3).

⁷ The length of the RFQ Response Period is defined by the Submitting Member but must fall within the time ranges established by the appropriate Procedure Committee on a class-by-class basis. The period cannot be less than three seconds. See proposed Rule 24B.4(a)(3)(iii).

maximum expiration terms and second to minimum value size requirements. The maximum expiration terms are the same as in the existing FLEX rules.⁸ The minimum value size specifications are substantially similar to those in Rule 24A.4, though additional language has been added to clarify the minimum value size requirements for FLEX Orders entered in the Book. There are additional special terms for FLEX Index Options⁹ and FLEX Equity Options,¹⁰ which correspond to provisions in existing Rule 24A.4.

3. FLEX Trading Procedures and Principles (Proposed Rule 24B.5)

On the new System, there will be no trading rotations in FLEX Options, either at the open or the close.¹¹ Instead, trading will result from RFQs submitted through the System or in open outcry, or from transactions on the Book.

(a) Electronic RFQ Process

Upon receipt of an RFQ in proper form, the System will cause the terms and specifications of the RFQ to be communicated to all FLEX Traders. Any FLEX Trader, including the Submitting Member, may then enter a FLEX Quote during the RFQ Response Period. Any FLEX Quote or FLEX Order may be entered, modified, or withdrawn at any

⁸ For FLEX Equity Options, the maximum term is generally three years, although the Submitting Member may request up to five years. For FLEX Index Options, the maximum term is generally five years, although a Submitting Member may request up to ten years. See existing Rule 24A.4(a)(4); proposed Rule 24B.4(a)(5).

⁹ See proposed Rule 24B.4(b).

¹⁰ See proposed Rule 24B.4(c). For example, settlement of a FLEX Equity Option shall be by physical delivery of the underlying security.

¹¹ See proposed Rule 24B.3.

point during the RFQ Response Period.¹² The System will dynamically calculate and disseminate to all FLEX Traders the RFQ Market.¹³

Following the RFQ Response Period, the Submitting Member may trade against the RFQ Market during the RFQ Reaction Period. The length of this period will be established by the appropriate Procedure Committee on a class-by-class basis and will not be more than five minutes.¹⁴ Failure of the Submitting Member to trade against the RFQ Market before expiration of the RFQ Reaction Period would equate to a rejection. During the RFQ Reaction Period: (1) FLEX Traders can continue to enter, modify, or withdraw FLEX Quotes and FLEX Orders; (2) FLEX Orders that are entered or modified during the RFQ Response and Reaction Periods will be treated the same as FLEX Quotes for purposes of the priority allocation; and (3) the System will dynamically calculate and disseminate to all FLEX Traders the RFQ Market given the current FLEX Quotes and resting FLEX Orders.¹⁵

The Submitting Member may decline to trade against the RFQ Market by canceling the RFQ or letting it expire. If the Submitting Member chooses to trade but has not indicated an Intent to Cross, he or she may enter an RFQ Order to trade with one side of the RFQ Market (but not both). The Submitting Member's RFQ Order will be eligible to trade with FLEX Quotes and FLEX Orders at a single price that will leave bids and offers which cannot

¹² However, a FLEX Appointed Market-Maker must meet certain FLEX Quote maintenance obligations. See proposed Rule 24B.5(a)(1)(ii)(B).

¹³ See proposed Rule 24B.5(a)(1)(ii)(C) (as modified by Amendment No. 2).

¹⁴ The Exchange originally proposed to cap the RFQ Reaction Period at 30 seconds. In Amendment No. 2, the Exchange proposed to increase the maximum period to five minutes "to address feedback received from members and potential users that the RFQ Reaction Period should be lengthened to provide Submitting Members with additional time to assess an RFQ Market, determine whether to accept or reject it, and process a response accordingly."

¹⁵ See proposed Rule 24B.5(a)(1)(iii)(B)(II) (as modified by Amendment No. 2).

trade with each other (the "BBO clearing price"). In determining the priority of FLEX Quotes and FLEX Orders, the System gives priority to those priced better than the BBO clearing price, then to FLEX Quotes and FLEX Orders at the BBO clearing price. Priority among FLEX Quotes and FLEX Orders at the BBO clearing price is as follows: (1) any FLEX Quotes that are subject to a FLEX Appointed Market-Maker participation entitlement; (2) FLEX Orders resting in the Book, based on the Book priority algorithm; (3) FLEX Quotes for the account of public customers and non-member broker-dealers based on time priority; and (4) all other FLEX Quotes based on time priority.

If the RFQ Market is locked or crossed, priority among FLEX Quotes and FLEX Orders at the BBO clearing price and on the same side as the RFQ Order is as follows: (1) FLEX Orders in the Book, based on the Book priority algorithm; (2) if applicable, an RFQ Order for the account of a public customer or non-member broker-dealer, then any FLEX Quote that is subject to a FLEX Appointed Market-Maker participation entitlement; (3) FLEX Quotes for the account of public customers and non-member broker-dealers, based on time priority; (4) if applicable, an RFQ Order for the account of a member, then any FLEX Quote that is subject to a FLEX Appointed Market-Maker participation entitlement; and (5) all other FLEX Quotes, based on time priority. The System will enter any remaining balance of the incoming RFQ Order in the Book (if available), unless the Submitting Member has indicated that the balance of the RFQ Order is to be automatically canceled if it is not traded.

If the Submitting Member has indicated an "Intent to Cross" in its RFQ request, the Submitting Member may receive a crossing participation entitlement if one has been established in that class by the appropriate Procedure Committee, and if the RFQ Order entered by the Submitting Member during the RFQ Reaction Period matches or improves the

BBO clearing price. The RFQ Order will be eligible to trade with FLEX Quotes and FLEX Orders at the BBO clearing price giving priority to the FLEX Quotes and FLEX Orders priced better than the BBO clearing price, then to FLEX Quotes and FLEX Orders at the BBO clearing price. Priority among multiple FLEX Quotes and FLEX Orders at the BBO clearing price is as follows: (1) FLEX Orders in the Book, based on the Book priority algorithm; (2) FLEX Quotes for the account of public customers and non-member broker-dealers, based on time priority; (3) the crossing participation entitlement; (4) any FLEX Quotes that are subject to a FLEX Appointed Market-Maker participation entitlement;¹⁶ and (5) then all other FLEX Quotes, based on time priority.

If a Book is available in that class, the System would enter any remaining balance of the incoming RFQ Order in the Book and treat it the same as other FLEX Orders. If there is no Book available, the System will expose any remaining balance of the incoming RFQ Order so other FLEX Traders can trade against it. After the remaining balance of the RFQ Order has been exposed for at least the Crossing Exposure Period,¹⁷ the Submitting Member may enter a contra-side order to trade all or any portion of the remaining balance.¹⁸

If the Submitting Member rejects the RFQ Market or to the extent the RFQ Market size exceeds the Submitting Member's size, the System automatically would execute any remaining FLEX Quotes and FLEX Orders that are marketable against each other at the BBO

¹⁶ The crossing participation entitlement and the FLEX Appointed Market-Maker entitlement together may not exceed a certain percentage of the original order. See proposed Rule 24B.5(d)(2)(i)(A)-(B).

¹⁷ The length of this Crossing Exposure Period shall be determined by the appropriate Procedure Committee on a class-by-class basis and shall not be less than three seconds. See proposed Rule 24B.5(a)(1)(iii)(D)(IV).

¹⁸ The Submitting Member must, however, enter a contra-side order when necessary to satisfy applicable minimum value size requirements. See id.

clearing price. Then, if a Book is available, any remaining balance of any FLEX Quote would be automatically entered into the Book unless the FLEX Trader who entered it had indicated that the FLEX Quote is to be automatically canceled if not traded. If no Book is available, any remaining balance of the FLEX Quotes will be automatically canceled at the conclusion of the RFQ Reaction Period.¹⁹

(b) Open-Outcry RFQ Process

To initiate a FLEX transaction using the open-outcry RFQ process under proposed Rule 24B.5, a Submitting Member would submit an RFQ to a FLEX Official. The Submitting Member would then immediately announce the terms and specifications of the RFQ to the crowd. FLEX Traders present in the crowd may respond orally with FLEX Quotes during the RFQ Response Period. A FLEX Trader could enter, modify, or withdraw its FLEX Quote at any point during the RFQ Response Period. At the expiration of the RFQ Response Period, the Submitting Member would identify the BBO (considering responsive FLEX Quotes and, if applicable, FLEX Orders resting in the Book) and announce the BBO to the crowd.

If the Submitting Member does not indicate an Intent to Cross or act as principal with respect to any part of the trade, the Submitting Member may submit an agency RFQ Order to trade against the RFQ Market. If the Submitting Member rejects the BBO or is given a BBO for less than the entire size requested, the FLEX Traders in the crowd other than the Submitting Member would have an opportunity to match or improve the BBO during a BBO Improvement Interval. At the expiration of any BBO Improvement Interval, the Submitting Member must promptly accept or reject the BBO.

¹⁹ See proposed Rule 24B.5(a)(1)(F).

If the Submitting Member indicates an Intent to Cross or act as principal with respect to any part of the trade, acceptance of the displayed BBO would be automatically delayed until the expiration of the BBO Improvement Interval. Prior to the BBO Improvement Interval, the Submitting Member must announce to the crowd the price at which it expects to trade. In these circumstances, the Submitting Member may participate with all other FLEX Traders present in the crowd in attempting to improve or match the BBO during the BBO Improvement Interval. At the expiration of the BBO Improvement Interval, the Submitting Member could trade against the BBO or reject it.

If the Submitting Member rejects the BBO after an RFQ Response Period or BBO Improvement Interval, or the BBO size exceeds the FLEX transaction size indicated in the RFQ, FLEX Traders present in the crowd could accept the unfilled balance of the BBO. Such acceptance must occur by public outcry immediately following the Submitting Member's rejection of the BBO or any BBO Improvement Interval, or the Submitting Member's trade that does not exhaust the full size of the BBO.

The highest bid (lowest offer) would have priority. Among bids (offers) at the same price, priority generally is as follows: (1) the crossing participation entitlement, if the Submitting Member has indicated an Intent to Cross and an entitlement is available in that class; (2) any FLEX Quote subject to a FLEX Appointed Market-Maker participation entitlement; (3) all other FLEX Quotes, in the sequence in which they are entered;²⁰ and (4) FLEX Orders resting in the Book, based on the Book priority algorithm. However, if a

²⁰ If two or more best bids (offers) are submitted in open outcry at the same time and same price or if the Submitting Member cannot reasonably determine the sequence in which they were made, priority would be apportioned equally among those open-outcry bids (offers). See proposed Rule 24B.5(a)(2)(v)(A)(III) (as modified by Amendment No. 2).

member is relying on the "G" exception to Section 11(a) of the Act,²¹ the member's bid (offer) must yield to any bid (offer) at the same price on the Book and all other bids (offers) that have priority over the Book. If a Submitting Member is asserting a crossing participation entitlement on behalf of a proprietary account of a member relying on the "G" exception and a FLEX Appointed Market-Maker is also asserting a participation entitlement, the Submitting Member's crossing participation entitlement combined with any guaranteed participation for FLEX Appointed Market-Makers shall not exceed 40% of the original order.

The proposed open-outcry RFQ process is similar to the existing process, with a few distinctions. Under the new System, the Submitting Member is responsible for announcing the terms and specifications of the RFQ to the crowd, receiving responsive FLEX Quotes, and at the conclusion of the RFQ Response Period announcing the BBO to the crowd. Under the existing process, the FLEX Post Official communicates the RFQ to the crowd over facilities maintained by the Exchange, responsive FLEX Quotes may be entered at the post, and the BBO is visibly displayed at the post and over the network.²² The proposed priority algorithm takes into consideration the Book, which does not exist currently, and provides that two bids submitted in open outcry at the same time and same price will be apportioned equally, as compared to the existing practice of affording priority to FLEX Appointed or Qualified Market-Makers.²³

²¹ 15 U.S.C. 78k(a)(1)(G).

²² Compare proposed Rules 24B.5(a)(2)(i)(B), (ii)(A), and (ii)(B) to existing Rule 24A.5(a)(ii), (b)(i), and (b)(iii).

²³ Compare proposed Rules 24B.5(a)(2)(v) and (d) to existing Rules 24A.5(e) and (f).

(c) The FLEX Book and FLEX Orders

The Exchange may determine to make a FLEX Book available on a class-by-class basis. If a Book has been enabled, a Submitting Member may enter a FLEX Order if it satisfies the applicable minimum value size requirements and the FLEX Order is in compliance with Section 11(a) of the Act. A FLEX Order submitted on behalf of the proprietary account of a member relying on the "G" exception to Section 11(a) may be entered only to hit the Book and may not rest in the Book.²⁴

FLEX Orders in the Book are ranked and matched based on price/time priority. However, if a FLEX Appointed Market-Maker is quoting at the best bid (offer) and a FLEX Appointed Market-Maker participation entitlement has been established, then priority at the same price is as follows: (1) any FLEX Orders for the account of public customer ranked ahead of the FLEX Appointed Market-Maker; (2) any FLEX Orders subject to a FLEX Appointed Market-Maker entitlement; and (3) all other FLEX Orders, based on time priority.²⁵

A Submitting Member may not execute as principal against a FLEX Order on the Book that it represents as agent unless: (1) the Submitting Member has been bidding or offering for at least the Crossing Exposure Period before receiving the agency FLEX Order that is executable against such bid or offer;²⁶ or (2) the agency FLEX Order is first subject to an RFQ and the agency FLEX Order (or any remaining balance not executed during the RFQ Reaction Period) is exposed on the System for at least the Crossing Exposure Period.²⁷ A

²⁴ See proposed Rule 24B.5(b)(2)(ii).

²⁵ See proposed Rule 24B.5(b)(2)(iii).

²⁶ See proposed Rule 24B.5(b)(3)(i)(B).

²⁷ See proposed Rule 24B.5(b)(3)(i)(A) (as modified by Amendment No. 2).

Submitting Member may not execute a solicited order against a FLEX Order that the Submitting Member is representing as agent unless the agency FLEX Order is first subject to any RFQ and the agency FLEX Order (or any remaining balance not executed during the RFQ Reaction Period) is exposed on the System for at least the Crossing Exposure Period.²⁸ The Crossing Exposure Period referenced in the above provisions will be established by the appropriate Procedure Committee on a class-by-class basis and will not be less than three seconds.²⁹

(d) Creation of Binding Contracts

Proposed Rule 24B.5(c) provides that acceptance of any bid or offer creates a binding contract under Rule 6.48. This provision is the same as in existing Rule 24A.5(d) and applies to both RFQ and Book transactions.

(e) Guarantees

For FLEX Equity Options, the Exchange's appropriate Procedure Committee may determine on a class-by-class basis to establish a crossing participation entitlement for facilitations and/or solicitations with respect to open-outcry and/or electronic trades. The entitlement percentage may not exceed 40% of the original order.³⁰ If the Submitting Member matches or improves the BBO or BBO clearing price, as applicable, the Submitting Member would have priority to execute the contra-side of the order up to the crossing participation entitlement percentage. The appropriate Procedure Committee similarly may determine on a class-by-class basis to establish a crossing participation entitlement for FLEX Index Options, which may not exceed 40% of the trade. With respect to FLEX Index

²⁸ See proposed Rule 24B.5(b)(3)(ii) (as modified by Amendment No. 2).

²⁹ See proposed Rule 24B.5(b)(3)(iii) (added by Amendment No. 2).

³⁰ See proposed Rule 24B.5(d)(2)(i)(A).

Options, if the Submitting Member matches or improves the BBO or BBO clearing price, as applicable, the Submitting Member would have priority to execute the contra-side of the order up to the largest of: (1) the crossing entitlement percentage; (2) a proportional share of the trade; (3) \$1 million underlying equivalent value; or (4) the remaining underlying equivalent value on a closing transactions valued at less than \$1 million.³¹

In the past, the establishment of FLEX Appointed Market-Maker entitlements were the subject of separate rule filings.³² In lieu of submitting separate rule filings, the Exchange has now proposed to include specific parameters within the rule text, similar to its rules respecting crossing participation entitlements and market-maker participation entitlements for Non-FLEX Options.³³ Henceforth, the appropriate Procedure Committee may establish a participation entitlement for FLEX Appointed Market-Makers on a class-by-class basis with respect to open-outcry RFQs, electronic RFQs, and/or Book transactions. Any such entitlement shall: (1) be divided equally by the number of FLEX Appointed Market-Makers quoting at the BBO or BBO clearing price, as applicable; (2) collectively be no more than: (a) 50% of the remaining order when one other FLEX Market-Maker is quoting at the same price, (b) 40% when two other FLEX Market-Makers are quoting at the same price, and (c) 30% when three or more FLEX Market-Makers are quoting at the same price; and (3) when combined with any Submitting Member's crossing participation entitlement, shall not exceed

³¹ See proposed Rule 24B.5(d)(2)(i)(B). In the FLEX RFQ System rules, the crossing participation entitlement for transactions in FLEX Index Options is currently 20%, and there are similar provisions for FLEX Index Options that could permit an entitlement of greater than 40% in certain cases. See existing Rule 24A.5(e)(iii)(B).

³² See Rule 24A.5(e)(iv); Securities Exchange Act Release No. 45934 (May 15, 2002), 67 FR 36276 (May 23, 2002) (SR-CBOE-2002-09).

³³ See, e.g., Rule 8.87, Participation Entitlement of DPMs and e-DPMs (providing for a DPM/e-DPM participation entitlement after all public customer orders are satisfied).

40% of the size of the original order.³⁴ Pronouncements regarding the applicable participation entitlements must be announced to the membership via regulatory circular.

(f) Solicited Orders

A Submitting Member trading in open outcry may not cross an order that he or she is holding with an order that he or she solicited from a FLEX Market-Maker who is then in the trading crowd, except in accordance with CBOE Rule 6.55, Multiple Representation Prohibited. A Submitting Member utilizing the electronic System may not cross an order that he or she is holding with: (1) a solicited order for a FLEX Market-Maker's individual or joint account; or (2) a solicited order initiated by the FLEX Market-Maker for an account in which the FLEX Market-Maker has an interest, unless the FLEX Market-Maker refrains from participating on the same trade.³⁵

(g) FLEX Standard Minimum Increments

The applicable increments for FLEX Index Options will be identical to the increments in the existing FLEX rules, which permit decimal bids and offers in the designated currency that meet or exceed certain minimum parameters.³⁶ For example, the minimum increment in U.S. dollars is \$0.01 (or such other minimum as the appropriate Procedure Committee may set from time to time to ensure fair and orderly markets). The applicable increments for FLEX Equity Options will be determined by the appropriate Procedure Committee on a class-by-class basis, but may not be smaller than \$0.01. This represents a change from the existing FLEX rules, under which the trading increments applicable to FLEX Equity Options

³⁴ See proposed Rule 24B.5(d)(2)(ii).

³⁵ See proposed Rule 24B.5(d)(2)(i)(C).

³⁶ See existing Rule 24A.5(g) (which is proposed to be renumbered as Rule 24A.5(f)); proposed Rule 24B.5(e).

are the same as those applicable to Non-FLEX Equity Options (i.e., \$0.10 for simple bids and offers in series quoted at or above \$3 a contract, \$0.05 for simple bids and offers in series quoted below \$3 a contract, and \$0.01 for series quoted in the penny pilot program³⁷).

4. FLEX Market-Maker Appointments and Obligations (Proposed Rule 24B.9)

Under the rules for the new System, the Exchange will appoint two or more FLEX Qualified Market-Makers to each FLEX Index Option class and settlement currency, and two or more FLEX Qualified Market-Makers to each FLEX Equity Option class. In making such appointments and in taking other action with respect to FLEX Qualified Market-Makers, the Exchange shall take into account the factors enumerated in, and shall refer to the requirements of, existing CBOE Rule 8.3, Appointment of Market-Makers. As a condition to receiving and maintaining a FLEX Qualified Market-Maker appointment in a FLEX Index Option (FLEX Equity Option), the FLEX Qualified Market-Maker must maintain an appointment in one or more Non-FLEX Index Option classes (Non-FLEX Equity Option classes). The Non-FLEX Option class need not include the FLEX Option class's underlying index or security.

Notwithstanding the above, the appropriate Market Performance Committee may determine to solicit applications and appoint: (1) one or more FLEX Appointed Market-Makers in addition to appointing FLEX Qualified Market-Makers to such classes; or (2) two or more FLEX Appointed Market-Makers in lieu of appointed FLEX Qualified Market-Makers. Thus, under this revised structure applicable to both platforms, a FLEX Option class could be structured as a FLEX Qualified Market-Maker-only crowd with at least two

³⁷ See CBOE Rule 6.42.

participants, a mixed FLEX Qualified/Appointed Market-Maker crowd with at least three participants, or a FLEX Appointed Market-Maker-only crowd with at least two participants.

A FLEX Appointed Market-Maker must provide a FLEX Quote in response to any open-outcry RFQ in a class of FLEX Options to which it is appointed and trades in open outcry.³⁸ In addition, a FLEX Appointed Market-Maker must provide FLEX Quotes in response to a designated percentage of electronic RFQs, such percentage to be determined by the appropriate Procedure Committee and not less than 80%.³⁹ Although a FLEX Qualified Market-Maker need not enter a FLEX Quote in response to an RFQ in a class of FLEX Options to which it is appointed,⁴⁰ the FLEX Qualified Market-Maker (like the FLEX Appointed Market-Maker) must submit a FLEX Quote if called upon by a FLEX Official, including when no FLEX Quotes are submitted in response to a specific RFQ.⁴¹

5. FLEX Officials (Proposed Rule 24B.14)

Existing FLEX Rule 24A.12 provides that a FLEX Post Official is responsible for: (1) reviewing the conformity of RFQs and FLEX Quotes to the terms and specifications contained in Rule 24A.4; (2) posting RFQs for dissemination; (3) determining the BBO; (4) ensuring that contracts are executed in conformance with the priority principles set forth in Rule 24A.5(e); (5) calling for Indicative FLEX Quotes in accordance with the requirements of Rule 24A.12(c); and (6) calling upon FLEX Qualified Market-Makers to provide FLEX Quotes in specific classes of FLEX Equity Options as provided in Rule 24A.9(c).⁴²

³⁸ See proposed Rule 24B.9(c)(i).

³⁹ See proposed Rule 24B.4(a)(5)(iv).

⁴⁰ See proposed Rule 24B.9(c).

⁴¹ See proposed Rule 24B.9(d).

⁴² See existing Rule 24A.12(b).

Proposed Rule 24B.14, FLEX Official, corresponds with existing Rule 24A.12 and describes the functions of a FLEX Official for the new System. The FLEX Official would continue to be responsible for reviewing the conformity of open-outcry RFQs to the applicable terms and specifications in proposed Rule 24B.4. However, because open-outcry FLEX Quotes will now be provided to the Submitting Member, the FLEX Official is no longer responsible for reviewing them for conformity to the applicable terms and specifications or for determining the BBO. In addition, a FLEX Official may nullify a FLEX transaction, whether electronic or open-outcry, if he or she determines that it does not conform to the terms of proposed Rules 24B.4 or 24B.5. As noted above, a FLEX Official may call upon FLEX Market-Makers, whether Qualified or Appointed to a given class, to provide FLEX Quotes in certain circumstances, as provided in proposed Rule 24B.9.

A FLEX Official may be an employee of the Exchange or an independent contractor. The Exchange may designate other qualified employees or independent contractors to assist the FLEX Official as the need arises.⁴³

6. Position and Exercise Limits

Proposed Rules 24B.7, Position Limits and Reporting Requirements, and 24B.8, Exercise Limits, are modeled after existing Rules 24A.7 and 24A.8. However, the Exchange is proposing to make certain revisions to existing Rules 24A.7 and 24A.8, and to include the same language in proposed Rules 24B.7 and 24B.8, relating to the applicable position and exercise limits for FLEX Index Options and the aggregation of certain FLEX and non-FLEX positions. The Exchange has proposed changes to Rule 24A.7 to conform the language of

⁴³ See proposed Rule 24B.14(a).

that rule to reflect changes that were recently approved by the Commission in a separate proposed rule change.⁴⁴

In addition, the proposal would amend Rule 24A.7 to establish new position limits for certain industry-based FLEX Index Option classes:

1. No more than four times the applicable position limits established pursuant to Rule 24.4A for FLEX Options on: (a) the Dow Jones Transportation Average or the Dow Jones Utility Average; or (b) an industry-based index that is not a "narrow-based security index," as defined under Section 3(a)(55)(B) of the Act.⁴⁵
2. For all other industry-based FLEX Index Option classes, no more than one times the applicable number of Non-FLEX Index Option contracts (whether long or short) of the put class and the call class on the same side of the market, as determined on the basis of the position limits established pursuant to Rule 24.4A, Position Limits for Industry Index Options.

The proposal also would amend Rule 24A.7 to provide that position limits for a micro narrow-based FLEX Index Option class shall not exceed one times the applicable number of Non-FLEX Index Option contracts (whether long or short) of the put class and the call class on the same side of the market, as determined on the basis of the position limits established pursuant to Rule 24.4B, Position Limits for Options on Micro Narrow-Based Indexes As Defined Under Rule 24.2(d). Finally, new language to Rule 24A.7 would provide that, except as otherwise provided, the position limit for a broad-based FLEX Index Option class

⁴⁴ See Securities Exchange Act Release No. 56350 (September 4 2007), 72 FR 51878 (September 11, 2007) (SR-CBOE-2007-79).

⁴⁵ 15 U.S.C. 78c(a)(55)(B).

may not exceed 200,000 contracts on the same side of the market. Proposed Rule 24B.7 replicates amended Rule 24A.7 in the rules applying to the new System.

Both rules would contain new language requiring that positions in FLEX Options must be aggregated with positions in Non-FLEX Options in certain circumstances:

- QIX Options: Commencing at the close of trading two business days prior to the last trading day of the calendar, positions in FLEX Index Options having an exercise settlement value determined by the level of the index at the close of trading on the last trading day before expiration shall be aggregated with positions in Quarterly Index (QIX) Options on the same index with the same expiration and shall be subject to the position limits set forth in Rule 24.4, 24.4A, or 24.4B, as applicable.
- Weekly Options: Commencing at the close of trading two business days prior to the last trading day of the week, positions in FLEX Options that are cash-settled⁴⁶ shall be aggregated with positions in Short Term Option Series on the same underlying index with the same means for determining exercise settlement value (e.g., opening or closing prices of the underlying index) with the same expiration and shall be subject to the position limits set forth in Rule 24.4, 24.4A, 24.4B or 29.5, as applicable.

Proposed Rule 24B.8 replicates existing Rule 24A.8 regarding exercise limits. Both rules generally provide that the exercise limit for a FLEX Index Option is equivalent to the position limit. Both rules also set forth certain minimum value size requirements for exercises of FLEX Equity Options and FLEX Index Options.

⁴⁶ FLEX Index Options and FLEX Credit Default Options are cash-settled. FLEX Equity Options are settled by physical delivery. See existing Rules 24A.4(b)(4) and (c)(3) and 29.19; see also proposed Rules 24B.4(b)(4) and (c)(3).

In an earlier proposed rule change, CBOE represented that, when it files a proposed rule change to list and trade a new Non-FLEX Index Option, it also would propose to list and trade the FLEX Index Options in the same filing and include proposed position and exercise limits.⁴⁷ Because the maximum FLEX Index Option position and exercise limits will now be explicitly set out in Rules 24A.7, 24A.8, 24B.7, and 24B.8, the Exchange seeks to eliminate this earlier commitment.

7. Financial Requirements

Under the proposal, a FLEX Index Market-Maker may not effect a FLEX Index Option transaction unless it has demonstrated to the satisfaction of the Exchange that the net liquidating equity maintained in the FLEX Appointed Market-Maker's individual or joint accounts with any one clearing member in which transactions in FLEX Index Options will be conducted is at least \$100,000.⁴⁸ In addition, a FLEX Index Appointed Market-Maker is required to maintain at least \$1 million net liquidating equity and/or \$1 million net capital, as applicable.⁴⁹ A FLEX Index Appointed Market-Maker or its clearing member must immediately inform the Exchange whenever the FLEX Index Appointed Market-Maker fails to be in compliance with any of the above requirements. FLEX Market-Makers and floor brokers must file letters of guarantee accepting financial responsibility for all FLEX

⁴⁷ See Securities Exchange Act Release No. 43108 (August 2, 2000), 65 FR 48770 (August 9, 2000) (SR-CBOE-00-26) (immediately effective proposal providing for the listing and trading of FLEX Options on all indices that underlie Non-FLEX Options listed and traded by the Exchange).

⁴⁸ See proposed Rule 24B.11.

⁴⁹ See proposed Rule 24B.12.

transactions they make.⁵⁰ These provisions parallel existing Rules 24A.13, 24A.14, and 24A.15 that apply to the FLEX RFQ System.

8. Other Rules for New System

Other rules in proposed Chapter XXIVB are the same as, or closely modeled after, the existing rules of the FLEX RFQ System. Proposed Rules 24B.2, Hours of Trading; 24B.3, Trading Rotations; 24B.10, Related Securities; 24B.15, Nonavailability of RAES; and 24B.16, Inapplicability of Split Price and Accommodation Liquidation Rules, are identical to Rules 24A.2, 24A.3, 24A.11, 24A.16, and 24A.17, respectively. Proposed Rules 24B.6, Discretionary Transactions, and 24B.13, Letter of Guarantee or Authorization are virtually identical to Rules 24A.6 and 24A.15, respectively, except for non-substantive grammatical changes. Proposed Rules 24B.11, FLEX Index Appointed Market-Maker Account Equity, and 24B.12, FLEX Index Appointed Market-Maker Financial Requirements, are virtually identical to Rules 24A.13 and 24A.14, respectively, except that revisions are being made to clarify that these rules apply only to FLEX Appointed Market-Makers in FLEX Index Options.⁵¹

⁵⁰ See proposed Rule 24B.13.

⁵¹ The special account equity and financial requirements under existing Rules 24A.13 and 24A.14 apply only to FLEX Appointed Market-Makers, who currently are appointed only to FLEX Index Option classes and currently are subject to certain heightened minimum value size requirements under Rule 24A.4(a)(4)(iv). Given the proposed changes to the FLEX Market-Maker appointments discussed above, which would allow for the appointment of a FLEX Equity Appointed Market-Maker, proposed Rules 24B.11 and 24B.12 make clear that these special account equity and financial requirements would apply only to FLEX Appointed Market-Makers in FLEX Index Options (who would continue to be subject to the heightened minimum value size requirements under proposed Rule 24B.4(a)(5)(iv)) and not FLEX Appointed Market-Makers in FLEX Equity Options (who would not be subject to heightened minimum value size requirements). The Exchange has proposed corresponding changes to existing Rules 24A.13 and 24A.14.

B. Changes to Existing FLEX Rules

The Exchange is proposing various changes to the existing FLEX rules to conform them to the corresponding new System rules. In addition, the term "Indicative FLEX Quote" in Rule 24A.1 and a related reference in Rule 24A.12 are being deleted. Indicative FLEX Quotes are non-binding indications of the market that were periodically supplied by FLEX Market-Makers and displayed on the FLEX communication network. This functionality is no longer utilized, so these references in Rules 24A.1 and 24A.12 are being deleted.

The Exchange is also proposing to increase the crossing participation entitlement percentage available on the FLEX RFQ System. Currently, the Submitting Member may obtain a crossing participation entitlement of 25% of the incoming order for a FLEX Equity Option or 20% of the incoming order for a FLEX Index Option.⁵² Under the proposal, the appropriate Procedure Committee could determine on a class-by-class basis whether to establish a crossing participation entitlement for facilitations and/or solicitations and the applicable crossing participation entitlement percentage, which may not exceed 40% of the incoming order.⁵³ These revisions would make the crossing participation entitlements equivalent on the FLEX RFQ System and the FLEX Hybrid Trading System.

C. Other Changes to CBOE Rules

The Exchange is proposing to allow sponsored access to the new System. Under proposed Rule 6.20A, a CBOE member ("Sponsoring Member") may provide a non-member ("Sponsored User") with electronic access to the System. The proposed rule outlines the requirements that Sponsored Users and Sponsoring Members are required to meet prior to

⁵² See Rule 24A.5(e)(iii)(A)-(B). Other existing provisions could allow the Submitting Member to receive in excess of 20% of an incoming order for a FLEX Index Option. See Rule 24A.5(e)(iii)(B).

⁵³ See proposed Rule 24A.5(e)(iii)(A)-(B).

engaging in a sponsorship arrangement. A Sponsored User may be a person, such as an institutional investor, who has entered into a sponsorship arrangement with a Sponsoring Member for purposes of entering orders on the System. This would include entering and responding to electronic RFQs and entering FLEX Orders into the Book. A Sponsored User may utilize the System only if authorized in advance by one or more Sponsoring Members in accordance with the provisions of proposed Rule 6.20A.

D. Amendment Nos. 2 and 3

In Amendment No. 2, the Exchange made the following changes to the proposal:

- In proposed Rule 24B.5(a)(1), modifying the procedures that apply during the electronic RFQ Reaction Period to: (i) permit FLEX Quotes and FLEX Orders to be entered, modified, or canceled during the RFQ Reaction Period; (ii) increase the maximum RFQ Reaction Period from the proposed 30 seconds to five minutes; (iii) provide that, if the Submitting Member enters a FLEX Quote during the RFQ Reaction Period, the Submitting Member must be bidding (offering) for at least the Crossing Exposure Period prior to entering an RFQ Order; and (iv) provide that the RFQ Market is dynamically updated during both the RFQ Response and RFQ Reaction Periods;
- Also in proposed Rule 24B.5(a)(2), modifying the open-outcry priority provisions to clarify the Exchange's original intent that, after the application of any participation entitlements, all other FLEX Quotes submitted in response to an open-outcry RFQ have priority based on the sequence in which those FLEX Quotes are made in open outcry and, to the extent two or more best bid (offer) FLEX Quotes are submitted in open outcry at the same time

and same price (or the Submitting Member cannot reasonably determine the sequence), priority will be apportioned equally;

- In proposed Rule 24B.5(b), modifying the Book crossing provisions to clarify the Exchange's original intent that an agency FLEX Order must first be subject to an RFQ and the agency FLEX Order (or any remaining balance not executed during the RFQ Reaction Period) must also be exposed on the System for at least the Crossing Exposure Period prior to entering a contra-side principal or solicitation order that is executable against the agency FLEX Order. Previously, the proposed rule text had simply indicated that the agency FLEX Order must first be subject to an RFQ;
- Updating the text of Rules 24A.7 and 24A.8, as well as proposed Rules 24B.7 and 24B.8, to reflect unrelated changes that have been approved in a separate rule filing⁵⁴ and to make certain non-substantive corrections;
- Inserting corresponding changes to the discussion sections of the Form 19b-4 and the Exhibit 1 Federal Register notice to reflect the above-noted changes;
- Providing information regarding its plans respecting dissemination of FLEX data via the Options Price Reporting Authority ("OPRA"). Specifically, with respect to price reporting, the Exchange currently plans to continue disseminating via OPRA information regarding executed FLEX transactions. However, the Exchange currently does not plan to disseminate via OPRA information respecting pending electronic and open-outcry RFQs or information on resting orders in the Book; and

⁵⁴ See Securities Exchange Act Release No. 56350 (September 4, 2007), 72 FR 51878 (September 11, 2007) (SR-CBOE-2007-79).

- Submitting as part of Exhibit 5 the text of the Sponsored User Agreement form that the Exchange proposes to use in connection with proposed Rule 6.20A.

In Amendment No. 3, the Exchange made the following changes to the proposal:

- Revising the text of Rule 24B.1(u), RFQ Reaction Period, to reflect that during this time a Submitting Member determines whether to accept or reject the RFQ Market, which consists of both FLEX Quotes and FLEX Orders; and
- Correcting the text of proposed Rule 24B.5(a)(2)(iii) that was submitted as part of Amendment No.2.

III. Discussion

After careful consideration, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.⁵⁵ In particular, the Commission finds that the proposal is consistent with Sections 6(b)(5) of the Act,⁵⁶ which requires that the rules of an exchange be designed, among other things, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market, and, in general, to protect investors and the public interest. The Commission also finds that the proposal is consistent with Section 11A(a)(1)(C) of the Act,⁵⁷ which sets forth Congress's findings that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure, among other things, economically efficient

⁵⁵ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

⁵⁶ 15 U.S.C. 78f(b)(5).

⁵⁷ 15 U.S.C. 78k-1(a)(1)(C).

execution of securities transactions; fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets; and the practicability of brokers executing investors' orders in the best market. The Commission generally believes that an exchange furthers these principles when developing products and trading functionality that compete with the over-the-counter markets. This order approves the amended proposal in its entirety, although only certain aspects of the proposed rule change are discussed below.

A. Execution Algorithm and Priority and Allocation Rules

1. Electronic trading

The Commission believes that the priority and allocation rules for electronic trading on the new System are reasonable and consistent with the Act. These rules generally provide for allocation pursuant to price/time priority, with some allowance for market-maker and crossing participation guarantees. The proposed guarantees appear reasonably designed to balance incentives for providing liquidity in the FLEX market (in the case of the market-maker entitlement) and for bringing trades to the Exchange (in the case of the crossing participation entitlement) with incentives for all other market participants to quote competitively.

The Commission also believes that the priority and allocation rules for electronic FLEX trading are consistent with Section 11(a) of the Act.⁵⁸ The Commission believes, however, that neither a Submitting Member who trades against an electronic RFQ Market nor any other FLEX Trader who itself submits an RFQ Quote electronically qualifies for the "effect-versus-

⁵⁸ 15 U.S.C. 78k(a). Section 11(a)(1) prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises discretion unless an exception applies.

execute" exception to Section 11(a).⁵⁹ Nevertheless, the Commission believes that other exceptions may apply. FLEX Market-Makers qualify for the market-maker exception. With respect to non-market-maker members, the new System appears reasonably designed to cause RFQ Quotes constituting the RFQ Market and the RFQ Order that trades against the RFQ Market to yield to non-member interest, consistent with the "G" exception.⁶⁰

2. Open-outcry trading on new System

The Commission believes that the priority and allocation rules for open-outcry trading on the new System are reasonable and consistent with the Act. These provisions are generally modeled on the priority and allocation rules of the existing FLEX RFQ System, which were previously found by the Commission to be consistent with the Act.⁶¹ There is one significant difference, however, the addition of an electronic Book. Generally, an order resting on the Book will be filled only after all FLEX Quotes submitted in open outcry, even if the order was booked before the RFQ began and any oral responses to the RFQ were submitted.⁶² The Commission generally believes that displayed limit orders of public customers must be able to compete freely and openly for executions on an equitable basis. However, with a highly customized product such as FLEX Options, there are likely to be few booked orders. Therefore, solely with respect to the FLEX Hybrid Trading System, the Commission believes at the present time that it is appropriate to approve CBOE's proposal to allow FLEX Quotes submitted in response to an open-outcry RFQ to have priority over same priced bids (offers)

⁵⁹ 17 CFR 240.11a2-2(T).

⁶⁰ See 15 U.S.C. 78k(a)(1)(G) (setting forth all requirements for the "G" exception).

⁶¹ See Securities Exchange Act Release No. 31920 (February 24, 1993), 58 FR 12280 (March 3, 1993) (SR-CBOE-92-17).

⁶² See proposed Rule 24B.5(a)(2)(v)(A).

on the Book.⁶³ The Commission also notes that an open-outcry FLEX Quote must yield to the Book and all other bids (offers) that have priority over the Book if the member entering the FLEX Quote is relying on the "G" exception to Section 11(a) of the Act.⁶⁴

3. Orders on the Book

If the Exchange enables an electronic Book in a FLEX Option class, any transaction involving a booked order must comply with Section 11(a) of the Act. If a FLEX Trader cannot avail itself of any other exception, it must rely on the "G" exception, which requires, among other things, that a member order yield to a non-member order at the same price, even if the member order has time priority. The new System has not been programmed to cause a member order on the Book to yield to a later-arriving non-member order at the same price, although proposed Rule 24B.5(b)(2)(ii) prohibits a member order that is relying on the "G" exemption from resting on the Book. The Commission believes that a member may rely on the "G" exception if it sends an order to the Book and then cancels it immediately if it is not executed in full.

4. Changes to Allocation Rules of FLEX RFQ System

CBOE has proposed certain changes to its allocation rules under the existing FLEX RFQ System. Under the proposal, a FLEX Appointed Market-Maker will have priority over a FLEX Qualified Market-Maker when the two submit orders at the same time and same price. The Commission believes that this is consistent with the Act in light of the greater quoting obligations of the FLEX Appointed Market-Maker. CBOE also is proposing to increase the percentages of an incoming order that can be reserved for a crossing guarantee

⁶³ If circumstances change and the FLEX Book becomes frequently used, the Commission may revisit this issue.

⁶⁴ See proposed Rule 24B.5(a)(2)(v)(B).

or FLEX Appointed Market-Maker participation entitlement.⁶⁵ These percentages appear reasonably designed to balance incentives for providing liquidity with incentives for all other market participants to quote competitively.

5. Best Execution

The proposed rules do not explicitly require an RFQ Trader to trade against an RFQ Market. The Commission reminds RFQ Traders that the duty of best execution requires them to assess the quality of competing markets to ensure that a customer order is directed to the market providing the most advantageous terms for the customer. If a Submitting Member declines to trade a customer order against an RFQ Market and subsequently facilitates the customer order at a price inferior to the RFQ Market, there would be a presumption that the Submitting Member did not fulfill its best execution obligation.

B. Market-Maker Benefits and Obligations

The Commission believes that the balance of benefits and obligations of FLEX Market-Makers under the rules for the new System is consistent with the Act. A FLEX Appointed Market-Maker must provide a FLEX Quote in response to any open-outcry RFQ in a class of FLEX Options to which it is appointed and trading in open outcry.⁶⁶ In addition, the FLEX Appointed Market-Maker must provide FLEX Quotes in response to a designated percentage of electronic RFQs, such percentage to be determined by the appropriate Procedure Committee and not less than 80%.⁶⁷ Although a FLEX Qualified Market-Maker need not enter a FLEX Quote in response to an RFQ in its assigned class,⁶⁸ the FLEX

⁶⁵ See proposed Rule 24A.5(e)(iii)-(iv).

⁶⁶ See proposed Rule 24B.9(c)(i).

⁶⁷ See proposed Rule 24B.4(a)(5)(iv).

⁶⁸ See proposed Rule 24B.9(c).

Qualified Market-Maker (like the FLEX Appointed Market-Maker) must submit a FLEX Quote if called upon by a FLEX Official, including when no FLEX Quotes are submitted in response to a specific RFQ.⁶⁹ FLEX Appointed Market-Makers may be awarded a participation entitlement, noted above. Both FLEX Market-Makers qualify for the market-maker exception to Section 11(a) of the Act.

C. Position and Exercise Limits

The Commission believes that the proposed position and exercise limits in FLEX Options are reasonable and consistent with the Act. They appear reasonably designed to prevent a member from establishing an imprudent position in FLEX Options. Moreover, the Commission believes that these rules are reasonably designed to prevent a FLEX Trader from using FLEX Options to evade the position limits applicable to comparable Non-FLEX Options. In view of the explicit standards for position and exercise limits set forth in Rules 24A.7, 24A.8, 24B.7, and 24B.8, the Commission believes it is reasonable to relieve the Exchange of the obligation to propose new position and exercise limits for FLEX Options whenever it lists and trades a comparable non-FLEX product.

D. Sponsored Access

The Commission believes that the proposed sponsored access provisions are reasonable and consistent with the Act. The Commission notes that these provisions are substantially similar to those of another exchange, which previously were approved by the Commission.⁷⁰

The Exchange has proposed to offer sponsored access only to the new FLEX Hybrid Trading

⁶⁹ See proposed Rule 24B.9(d).

⁷⁰ See NYSE Arca Equities Rule 7.29; Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (SR-PCX-00-25) (approving proposal to establish Archipelago Exchange as the equities trading facility of the Pacific Exchange).

System, not to open-outcry FLEX trading or to other Exchange trading facilities. If the Exchange in the future would seek to offer sponsored access to its other trading facilities, it would have to file a proposed rule change pursuant to Section 19(b) of the Act.

E. Acceleration

The Commission finds good cause for approving the proposal, as modified by Amendment Nos. 2 and 3, prior to the thirtieth day after the date of publication of notice of the amended proposal in the Federal Register. Amendment Nos. 2 and 3 made only minor changes to the overall proposal, which was subject to a notice-and-comment period. Because no comments were received, the Commission believes that good cause exists to grant accelerated approval and thereby allow the Exchange to implement the proposal without further delay.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment Nos. 2 and 3, including whether it is consistent with the Act.

Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>);
- or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-CBOE-2006-99 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-CBOE-2006-99. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>).

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-CBOE-2006-99 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁷¹ that the proposed rule change (SR-CBOE-2006-99), as amended, is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁷²

Florence E. Harmon
Deputy Secretary

⁷¹ 15 U.S.C. 78s(b)(2).

⁷² 17 CFR 200.30-3(a)(12).