

I. Description of the Proposal

The purpose of the proposed rule change is to expand the applicability of CBOE Rule 8.51, its firm quote ("firm quote") or ten-up ("ten-up") rule, to include two-part equity option orders in which the component series are on opposite sides of the market and in a one-to-one ratio. The CBOE believes this change will enhance the ability of public customers to execute defined risk strategies, such as spreads and straddles, at the disseminated market quotes.⁵

CBOE Rule 8.51 places the responsibility on the trading crowd to ensure that non-broker-dealer customer orders are sold or bought, up to ten contracts, at the quoted offer or bid, respectively. This "firm quote" or "ten-up" requirement is meant to provide confidence that the displayed quotes may be relied upon by the investing public and to ensure that public customer orders will be executed at those quotes, or better.

From its inception the ten-up rule was intended to apply to, and has been interpreted to apply only to, single part orders, *i.e.*, either a buy order or a sell order for a particular option series. The Exchange has determined, however, that public customers would be served better if the interpretation were expanded to include a requirement to provide a ten-up market in two-part equity option orders in which the components of the order are on opposite sides of the market and in a one-to-one ratio to each other. The expansion in the interpretation of this rule would make it possible for public customers to execute both sides of a defined risk strategy, for up to ten contracts on each side, such as a spread or a straddle, at the disseminated prices. The exchange believes the rule change should help it compete more effectively for public customer order flow and trading activity.

The Exchange does not believe this rule change would be burdensome to market-makers because, under the current interpretation, the market-makers would be required to satisfy the ten-up requirement as to each leg of a spread or straddle if each was placed as a separate order. This rule change would merely ensure that these two components may be done at the same time, as one order, and at the same prevailing market quotes. The Exchange

believes, however, that it is inappropriate, under any circumstance, to extend the firm-quote treatment to multipart orders with all parts on the same side of the market as this would effectively impose the burden on options market-makers of making markets in the underlying security. For example, a position in a long call and a short put is economically equivalent to being long the underlying stock; and thus, requiring a trading crowd to provide firm quote treatment to an order for this position would essentially be requiring the option market-makers to act as market-makers in the underlying security.⁶

II. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 6(b)(5).⁷ In particular, the Commission believes the proposal is consistent with the Section 6(b)(5) requirement that the rules of an exchange be designed to promote just and equitable principles of trade and not to permit unfair discrimination between customers, issuers, brokers, and dealers.

The Commission believes that the CBOE's proposal to modify its current ten-up rule should expand the benefits to public customers associated with ten-up markets. In general, the ten-up rule results in faster executions of public customer orders and improves the quality of the Exchanges' options markets and market maker performance. Specifically, the proposal will extend the ten-up rule to each leg of certain two-part equity options. Accordingly, small public customers will be assured order execution for both parts of the order at the same time and at the best bid or offer to a minimum depth of ten contracts. Accordingly, the proposal should result in better executions for these types of non-broker dealer customer orders.

The Commission also believes the proposal will provide greater depth to the option markets without imposing any undue burdens upon market makers. Because market makers are already required to satisfy the ten-up requirement as to each leg of two part equity option orders as if each was

placed as a separate order, the Commission does not believe the proposal will impose any additional unnecessary burdens or capital risks upon market makers.

The Commission also notes that the proposal will only apply to two-part equity option orders in which the components are on opposite sides of the market and in a one-to-one ratio. The Commission believes these conditions are reasonable measures that should help ensure that the proposal will not allow the simultaneous execution of certain types of orders that otherwise might effectively raise the firm quote requirements above the current ten contracts limit, which could create disparate firm quote treatment for "one" versus "two" part orders.

The Commission finds good cause for approving Amendment No. 1 to the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. Amendment No. 1 adopts Interpretation and Policy .06 to Rule 8.51, which reflects in summary form the policy described in the Regulatory Circular. Because the Regulatory Circular was included as part of the filing, the substance and policy of which were discussed in the notice, the Commission does not believe that Amendment No. 1 raises any new or substantive issues. Therefore, the Commission believes it is consistent with Sections 6(b)(5) and 19(b)(2) of the Act to approve Amendment No. 1 to the proposal on an accelerated basis.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. 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 at the Commission's Public Reference Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. SR-CBOE-94-

Amendment No. 1 proposes to add Interpretation and Policy .06 to CBOE Rule 8.51.

⁵ In its filing, the CBOE included a draft regulatory circular to be issued to members describing the change in policy applicable to the ten-up guarantee under CBOE Rule 8.51.

⁶ Under existing Rule 8.51, the firm quote size minimum will continue to not apply whenever a "fast market" is declared under Rule 6.6, and may be suspended for any class or series on a case by case basis as determined by the Market Performance Committee.

⁷ 15 U.S.C. 78f(b)(5) (1982).