



To: Members and Member Organizations

Regulatory Circular RG04-120

From: Regulatory Services Division
Legal Division

Date: November 24, 2004

Re: CBOE Rule Filing re Systematizing Orders & COATS

On November 23, 2004, CBOE filed a proposed rule change, SR-CBOE-2004-77, which proposes to amend CBOE rules relating to the systematizing of orders in connection with the requirement to implement a consolidated options audit trail system ("COATS"). CBOE filed this rule filing in compliance with a specific undertaking in the SEC Enforcement Order from 2000, which required CBOE and the other option exchanges to design and implement COATS in five phases in order to provide an accurate, time-sequenced record of electronic and other orders, quotations, and transactions. This rule filing relates to Phase V of COATS. A copy of the rule filing is available on CBOE's website at www.cboe.org/legal under the tab "Rule Filings Submitted to the SEC", or from CBOE's Legal Division.

Submission of Comments regarding the Rule Filing. As noted in the rule filing, members and other interested persons may submit written data, views, and arguments concerning the rule filing, including whether the proposed rule filing is consistent with the Securities Exchange Act, by any of the following methods:

Electronic comments:

- Use the SEC's Internet comment form at www.sec.gov/rules/sro.shtml; or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-CBOE-2004-77 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609.

General Requirement. In summary, and except as described below, the rule filing proposes that beginning on **January 10, 2005**, each order, cancellation of, or change to an order in any option class transmitted to CBOE should be "systematized", in a format approved by CBOE, either before it is sent to CBOE or upon receipt on the floor of CBOE. (See pages 3 and 7 of the rule filing.) An order is systematized if:

- (i) the order is sent electronically to CBOE; or
- (ii) the order that is sent to CBOE non-electronically (*e.g.*, telephone orders) is input electronically into CBOE's systems contemporaneously upon receipt on CBOE, and prior to representation of the order.

OEX, XEO and SPX. The rule filing also proposes that the requirement to systematize orders shall apply in the OEX, SPX and XEO option classes beginning on **March 28, 2005**. (See pages 4 and 9 of the rule filing.)

Marketable Orders. With respect to non-electronic, market and marketable orders sent to CBOE, the member responsible for systematizing the order shall input into CBOE's systems at least the following eight specific items with respect to the order prior to the representation of the order: (i) the option symbol; (ii) the expiration month; (iii) the expiration year; (iv) the strike price; (v) buy or sell; (vi) call or put; (vii) the number of contracts; and (viii) the Clearing Member. Any additional information with respect to the order shall be input into CBOE's systems contemporaneously upon receipt, which may occur after the representation and execution of the order. (See pages 3-4, and 7-9 of the rule filing.) As noted in the filing, CBOE intends to continue to evaluate whether some number of order terms less than the eight identified above would be sufficient to distinguish one order from another that a member may receive at or about the same time, and thus support eliminating the necessity to input some of these orders terms prior to representation. CBOE also will continue to evaluate whether there are more efficient means or devices to input the required order information.

Due Diligence Rule. The rule filing also proposes to amend Rule 6.73 - Responsibilities of Floor Brokers to make explicit that a broker's responsibility to immediately and continuously represent market and marketable orders is subject to the requirement set forth in this rule filing, namely, that each order must be systematized prior to representation.

Devices and Training. The manner of systematizing orders will be through the Floor Broker Workstation ("FBW"), BERS, or through proprietary systems approved by CBOE. Educational training sessions to further explain the COATS requirement to systematize orders in equity and index option classes will be held throughout December 2004, and scheduling information as to these sessions will be provided shortly. In addition, the Regulatory Division will begin shortly distributing reports to brokers showing current systemization rates.

If you have questions concerning the FBW or other devices to systematize orders, please contact Monica Wiedlin-Torres at 786-7368, or Jeff Short at 786-8410, or Maureen Smith at 786-7556. If you have any questions relating to the rule filing, please contact Patrick Sexton at 786-7467. Finally, if you have any regulatory related questions about this new requirement or reports showing current systemization rates, please contact Karen Charleston at 786-7724.