



CBOE Regulatory Circular RG07-79

DATE: July 25, 2007

TO: Members and Member Firms

FROM: CBOE Research and Product Development

SUBJECT: New Product Launch on July 31, 2007:
Basket Credit Event Binary Options

OVERVIEW

On July 31, 2007, CBOE plans to commence trading Basket Credit Event Binary Options ("Basket CEBOs"). Below are some features of the proposed Basket CEBOs:

- Basket CEBOs pay out a cash settlement amount upon the confirmation of a Credit Event in one, some or all of the Basket Components. Each Basket Component pays a predetermined settlement value, based on the recovery rate specified for that component, to the option holder upon the confirmation of a Credit Event (e.g., bankruptcy or failure-to-pay) in a Basket Component (i.e., debt issuer or guarantor) and \$0 if there is no Credit Event prior to the Last Trading Day.
- Basket CEBOs will continue to trade after a Credit Event has been confirmed, unless there are no remaining Basket Components. Holders, as of the close of the confirmation date of the Credit Event, will receive the payout based on that Credit Event.
- Bankruptcy and Failure-to-Pay Default, as described in the CREDIT EVENTS section of this circular, will be the applicable Credit Events for Basket CEBOs.
- The Last Trading Day for Basket CEBOs, if there is no Credit Event, will be the 3rd Friday of the month. If a Credit Event has been confirmed prior to that date in every Basket Component or if a Redemption Event has been confirmed in the last Basket Component prior to that day, the series will cease trading at the time of the confirmation and the Last Trading Day will be changed to the confirmation date.
- The Expiration Date for Basket CEBOs if there is no Credit Event will be the 4th business day after the Last Trading Day. If a Credit Event has been confirmed before that day in every Basket Component or if a Redemption Event has been confirmed in the

last Basket Component prior to that day, the Expiration Date will be accelerated to the 2nd business day immediately following the last confirmation date.

- Up to 41 quarterly expiration months (10.25 years) may be listed at any time.
- Basket CEBOs will have unique class symbols for each calendar year. Standard Call Month codes will be used for Basket CEBOs and "Z" will be used for the "dummy" \$1 strike code.
- Basket CEBOs will be *P.M.-settled*.
- Basket CEBOs will trade from 8:30 a.m. – 3:00 p.m. (CT).

CURRENT CLASS LISTINGS

Following are the classes and contract months for series of Basket CEBOs currently listed for trading:

Product Name	Expiration Month and Option Symbols	
	Sep 2008	Sep 2012
Auto Sector Basket CEBO	AFY	AFZ
Home Builder Basket CEBO	BBR	BBS
High Yield Composite Basket CEBO	HAU	HEU

- At the end of this circular, CBOE sets forth a listing of the specific components contained within each basket identified above, and other relevant information.

CREDIT EVENTS

To the extent they are provided in the terms of the Relevant Obligations (described below) of the Basket Components within a Basket CEBO, the following are the applicable Credit Events for the above-listed classes:

- A Failure-to-Pay Default on its Reference Obligation (e.g., Company ABC 8.5% July 2013 bond) or on any other debt security obligations of the Reference Entity other than non-recourse indebtedness (the set of these obligations and the Reference Obligation are referred as the "Relevant Obligations"); provided that the minimum failure-to-pay amount, individually or in the aggregate, shall be the greater of \$750,000 or the amount specified in accordance with the terms of the Relevant Obligation(s).
- Bankruptcy as defined in the terms of the Relevant Obligation(s).

INFORMATION SOURCES

CBOE will confirm Credit Events and Special Contingencies based on at least two of the following sources of publicly available information: (1) Wall Street Journal, Bloomberg Service, Reuters, Dow Jones News Wire, Financial Times, New York Times; and/or (2) information submitted to or filed with the courts, the SEC, an exchange or association, the OCC, or another regulatory agency or similar authority.

SUCCESSION ADJUSTMENTS

Each Basket Component for which the Exchange has confirmed a Succession Event may be replaced by one or more Basket Components (“Successor Basket Components”) consisting of the Successor Basket Component(s) that have succeeded the original Basket Component as a result of a Succession Event based on the applicable share of each Successor Basket Component.

- A “Successor Basket Component” and a “Succession Event” will be defined in accordance with the terms of the Relevant Obligations of the Basket Component that is subject to adjustment for succession. In determining the applicable share, an equal share will be allocated to each Successor Basket Component that has succeeded the original Basket Component as issuer or guarantor of at least one Relevant Obligation and at least 25% of the principal amount of the original Basket Component’s outstanding debt obligations other than non-recourse indebtedness. If no Successor Basket Component satisfies the “at least 25%” requirement and the original Basket Component does not survive following the Succession Event, an equal share will be allocated to the Successor Basket Component(s) that succeeded to the largest percentage of the original Basket Component’s outstanding debt obligations other than non-recourse indebtedness.
- In the event of an adjustment for succession, the Exchange will specify the Reference Obligation, recovery rate and the basket weight of each Successor Basket Component. The newly specified weight(s) will equal the weight of the predecessor Basket Component replaced by the Successor Basket Component(s). The recovery rates of Successor Basket Components may differ from the specified recovery rate of the predecessor Basket Component and the recovery rates of two or more Successor Basket Components could differ from one another.
- In respect of each Basket CEBO contract that was subject to adjustment for succession, all other terms and conditions of each Basket CEBO containing a Successor Basket Component will be the same as the original Basket CEBO unless the Exchange determines, in its sole discretion, that a modification is necessary and appropriate for the protection of investors and the public interest, including but not limited to the maintenance of fair and orderly markets, consistency of interpretation and practice, and the efficiency of settlement procedures.

For additional information regarding Basket CEBO adjustments, please refer to Rule 29.4.

BASKET CEBO PRODUCT DESCRIPTION

Description:

Basket CEBOs are cash-settled call options based on a Basket of Reference Entities (“Basket Components”). The options automatically pay out a cash settlement amount upon the confirmation of a Credit Event in one, some or all of the Basket Components, as specified by the Exchange at listing. The cash settlement amount could be different for different Basket Components. From time to time, CBOE may create new baskets that contain several of the same Basket Components contained in existing Basket CEBOs, which would be listed as a new options class. Existing Basket CEBOs will continue to trade until expiration.

For each Basket CEBO class, the Exchange will specify:

- (a) the Notional Face Value of the Basket (e.g., \$100,000),
- (b) the Basket Components,
- (c) the weight of each Basket Component, which represents the fraction of the Notional Face Value of the Basket allocated to each Basket Component. (For example, if the Notional Face Value of the Basket is \$100,000, and there are 10 equally weighted Basket Components, each Basket Component has a Notional Face Value of \$10,000),
- (d) the recovery rate of each Basket Component,
- (e) the specified debt security that defines the Reference Obligation of each Basket Component (e.g., Corporation XYZ 8.375% July 2033 bond), and
- (f) the applicable Credit Event(s).

Basket Components will remain fixed from the time of listing to the expiration date of the option, except that Basket Components could be replaced by Successor Basket Components following a Succession Event and would be removed from the Basket CEBO after a Credit Event or Redemption Event is confirmed by the Exchange.

Relevant Securities:

The specified debt security that defines the Reference Obligation of each Basket Component and all its other debt security obligations.

Strike Price:

Not applicable. A dummy strike price of 1.00 will be in the OPRA strike price field. The strike code for Basket CEBOs will be "Z".

Only Call Options will trade:

You may receive data (Month/Strike) information for puts. In that event, **please disregard** the information.

Exercise Settlement Value:

The automatic payout for a Basket CEBO will be equal to the cash settlement amount divided by the contract multiplier specified by the Exchange. For example, if a Credit Event is confirmed in a Basket Component with a cash settlement amount is \$6,000, the Exercise Settlement Value will be \$6.00 (equivalent to \$7.00 minus the dummy strike value of \$1.00).

Unit/Multiplier:

1,000 per contract.

Cash Settlement Amount:

If the Exchange confirms a Credit Event in an Basket Component occurred prior to 10:59 p.m. (CT) on the Last Trading Day, the cash settlement amount will be equal to the Notional Face Value of the Basket Component times one minus its Recovery Rate (its "loss rate"). For example, if the Notional Face Value of the Basket Component is \$10,000, and the Exchange specifies a recovery rate of 40% (or 0.40) for the particular Basket Component in which a Credit Event is confirmed, the cash settlement amount is $\$6,000 = \$10,000 * (1 - 0.40)$.

Minimum Price Increment:

\$0.05 per unit (\$50 per contract).

Contract Months:

Unless a Credit Event in all Basket Components has been confirmed, the Last Trading Day in the series will be the 3rd Friday of the expiration month in the March, June, September or December expiration month (however, if that day is not a business day, the Last Trading Day in the series will be on the preceding business day).

Special Contingencies:

Special procedures will apply if one or more of the following events occur on or before the Last Trading Day:

- (1) A Succession Event, which will be defined in accordance with the terms of the Relevant Obligation(s).

Adjustment for Succession: Once the Exchange has confirmed a Succession Event in an Basket Component, that component may be replaced by one or more Basket Components ("Successor Basket Components") that have succeeded the original Basket Component as a result of a Succession Event based on the applicable share of each Successor Basket Component, as determined in accordance with Rule 29.4

For each Successor Basket Component, the Exchange will specify the Reference Obligation (e.g., XYW 8.375% December 2033 bond), recovery rate and the Basket weight of each Successor Basket Component. The sum of the weights of the Successor Basket Components will equal the weight of the Basket Component replaced by the Successor Basket Components. The recovery rates of Successor Basket Components

may differ from the specified recovery rate of the predecessor Basket Component and the recovery rates of two or more Successor Basket Components could differ from one another.

(2) A Redemption Event, which will be defined in accordance with the terms of the Relevant Obligation(s) and will include the redemption or maturity of the Reference Obligation and of all other Relevant Obligations. If the Reference Obligation is redeemed or matures but other Relevant Obligation(s) remain, a new Reference Obligation will be specified from among the remaining Relevant Obligation(s) and the substitution will not be deemed a Redemption Event.

Adjustment for Redemption: Once the Exchange has confirmed a Redemption Event in a Basket Component, that Basket Component will be removed from the Basket CEBO.

Confirmation of Credit Event and Special Contingencies:

The Exchange will confirm Credit Events and Special Contingencies based on at least two of the following sources of publicly available information: (1) announcements published by newswire services or information services companies, the names of which will be announced to the membership via Regulatory Circular; and/or (2) information submitted to or filed with the courts, the SEC, an exchange or association, the OCC, or another regulatory agency or similar authority. Every determination made by the Exchange shall be within its sole discretion and shall be conclusive and binding on all investors and not subject to review. CBOE identifies the specific information sources on page 3 of this circular.

The confirmation period will begin when the Basket CEBO contract is listed and will extend to 3:00 p.m. (CT) on the Expiration Date.

Settlement:

Basket CEBOs settle in cash. If the Exchange confirms a Credit Event in a Basket Component prior to 10:59 p.m. (CT) on the Last Trading Day, the cash settlement amount will be equal to the Notional Face Value of the Basket Component times one minus its Recovery Rate (its "loss rate"). If no Credit Event is confirmed in a Basket Component, the cash settlement value will be \$0.

Last Trading Day:

The 3rd Friday of the expiration month (or, if that day is not a business day, the preceding business day); provided, however, if a Credit Event is confirmed prior to that day, the series will cease trading at the time of confirmation of the Credit Event and the Last Trading Day would be accelerated to the confirmation date.

Expiration Date:

The 4th business day after the 3rd Friday of the expiration month (or, if that day is not a business day, the 4th business day after the preceding business day); provided, however, if a Credit Event is confirmed by the Exchange to members and the OCC, the Expiration Date will be accelerated to the 2nd business day immediately following the confirmation date.

Final Settlement Date:

The day following the Expiration Date.

Trading Hours:

8:30 a.m. – 3:00 p.m. (CT).

Trading Platform:

CBOEdirect

Position Limit:

50,000 contracts.

Margin:

As described in Rule 12.3(l).

ADDITIONAL INFORMATION

Please refer to Chapter XXIX of CBOE's rules Basket CEBOs:

- RG07-80: Basket Credit Event Binary Options - System Settings

You can also find additional information on our website located at: <http://www.cboe.com/credit>.

Any questions about this memorandum may be directed to the Help Desk at (312) 786-7086 or 786-8749.

Auto Sector Basket CEBOS (AFY, AFZ)

	Company Name	Equity Ticker	Reference Obligation	REF OB CUSIP	Equity Cusip	Notional Value	Assumed Recovery Rate	Cash Settlement Amount
1	ArvinMeritor Inc	ARM	ARM 8 1/8 09/15/15	043353AC5	043353101	\$14,285.71	0.40	\$8,571.43
2	Amern Axle & Mfg Inc	AXL	AXL 5 1/4 02/11/14	02406PAE0	024061103	\$14,285.71	0.40	\$8,571.43
3	Ford Mtr Co	F	F 6 1/2 08/01/18	345370BX7	319963104	\$14,285.71	0.40	\$8,571.43
4	Gen Mtrs Corp	GM	GM 7 1/8 07/15/13	370442BS3	382550101	\$14,285.71	0.40	\$8,571.43
5	Goodyear Tire & Rubr Co	GT	GT 9 07/01/15	382550AU5	413619107	\$14,285.71	0.40	\$8,571.43
6	TRW Automotive Inc	TRW	TRW 9 3/8 02/15/13	87264QAM2	873168108	\$14,285.71	0.40	\$8,571.43
7	Visteon Corp	VC	VC 7 03/10/14	92839UAC1	969457100	\$14,285.71	0.40	\$8,571.43
						\$100,000.00		\$60,000.00

Home Builder Sector Basket CEBOS (BBR, BBS)

Company Name	Equity Ticker	Reference Obligation	REF OB CUSIP	Equity Cusip	Notional Value	Assumed Recovery Rate	Cash Settlement Amount
1 KB Home	KBH	KBH 7.75 02/01/10	48666KAF6	526057104	\$12,500.00	0.40	\$7,500.00
2 K Hovnanian Entpers Inc	HOV	HOV 6.5 01/15/14	442488AQ8	451663108	\$12,500.00	0.40	\$7,500.00
3 Beazer Homes USA Inc	BZH	BZH 6.5 11/15/13	07556QAJ4	07556Q105	\$12,500.00	0.40	\$7,500.00
4 Std Pac Corp	SPF	SPF 7 08/15/15	85375CAT8	00206R102	\$12,500.00	0.40	\$7,500.00
5 Centex Corp	CTX	CTX 5.25 06/15/15	152312AQ7	126650100	\$12,500.00	0.40	\$7,500.00
6 Lennar Corp	LEN	LEN 5.95 03/01/13	526057AG9	532716107	\$12,500.00	0.40	\$7,500.00
7 Pulte Homes Inc	PHM	PHM 5.25 01/15/14	745867AQ4	V7780T103	\$12,500.00	0.40	\$7,500.00
8 Toll Bros Inc	TOL	TOL 6.875 11/15/12	88947EAA8	88732J108	\$12,500.00	0.40	\$7,500.00
					\$100,000.00		\$60,000.00

High Yield Composite Basket CEBOS (BBR, BBS)

Company Name	Equity Ticker	Reference Obligation	REF OB CUSIP	Equity Cusip	Notional Weight	Recovery Rate	Cash Settlement Amount
1 Ford Mtr Co	F	F 6 1/2 08/01/18	345370BX7	345370860	\$2,000.00	0.40	\$1,200.00
2 Gen Mtrs Corp	GM	GM 7 1/8 07/15/13	370442BS3	370442105	\$2,000.00	0.40	\$1,200.00
3 Charter Comms Hldgs LLC	CHTR	CHTR 10 04/01/09	16117PAK6	16117M107	\$2,000.00	0.40	\$1,200.00
4 El Paso Corp	EP	EP 7 7/8 06/15/12	28336LAE9	28336L109	\$2,000.00	0.40	\$1,200.00
5 Williams Cos Inc	WMB	WMB 7 1/2 01/15/31	969457BB5	969457100	\$2,000.00	0.40	\$1,200.00
6 The AES Corp	AES	AES 7 3/4 03/01/14	00130HBC8	00130H105	\$2,000.00	0.40	\$1,200.00
7 Chesapeake Engy Corp	CHK	CHK 6 7/8 01/15/16	165167BE6	165167107	\$2,000.00	0.40	\$1,200.00
8 Lyondell Chem Co	LYO	LYO 10 1/2 06/01/13	552078AV9	552078107	\$2,000.00	0.40	\$1,200.00
9 CMS Engy Corp	CMS	CMS 6 7/8 12/15/15	125896AZ3	125896100	\$2,000.00	0.40	\$1,200.00
10 RH DONNELLEY Corp	RHD	RHD 8 7/8 01/15/16	74955WAG4	74955W307	\$2,000.00	0.40	\$1,200.00
11 NRG Energy Inc	XEL	NRG 7 1/4 02/01/14	629377AT9	98389B100	\$2,000.00	0.40	\$1,200.00
12 Level 3 Comms Inc	LVL	LVL 3 1/2 06/15/12	52729NBK5	52729N100	\$2,000.00	0.40	\$1,200.00
13 Dynegy Hldgs Inc	DYN	DYN 8 3/8 05/01/16	26816LAT9	26817G102	\$2,000.00	0.40	\$1,200.00
14 AMR Corp	AMR	AMR 9.1 05/01/16	001765AB2	001765106	\$2,000.00	0.40	\$1,200.00
15 Allied Waste North Amer Inc	AW	AM 7 3/8 06/01/16	026375AL9	019589308	\$2,000.00	0.40	\$1,200.00
16 EchoStar DBS Corp	DISH	DISH 6 5/8 10/01/14	27876GAX4	278762109	\$2,000.00	0.40	\$1,200.00
17 Tenet Healthcare Corp	THC	THC 7 3/8 02/01/13	88033GAY6	88033G100	\$2,000.00	0.40	\$1,200.00
18 Ctzns Comms Co	CZN	CZN 6 1/4 01/15/13	17453BAP6	17453B101	\$2,000.00	0.40	\$1,200.00
19 Royal Caribbean Cruises Ltd	RCL	RCL 6 7/8 12/01/13	780153AP7	V7780T103	\$2,000.00	0.40	\$1,200.00
20 L 3 Comms Corp	LLL	LLL 7 5/8 06/15/12	502413AJ6	502424104	\$2,000.00	0.40	\$1,200.00
21 Mirant North America LLC	MIR	MIR 7 3/8 12/31/13	60467XAC1	60467R100	\$2,000.00	0.40	\$1,200.00
22 Goodyear Tire & Rubr Co	GT	GT 9 07/01/15	382550AU5	382550101	\$2,000.00	0.40	\$1,200.00
23 Rite Aid Corp	RAD	RAD 7.7 02/15/27	767754AJ3	767754104	\$2,000.00	0.40	\$1,200.00
24 Abitibi Consol Inc	ABY	ABY 8 3/8 04/01/15	003669AJ7	003924107	\$2,000.00	0.40	\$1,200.00
25 Nortel Networks Corp	NTL	NT 4 1/4 09/01/08	656568AB8	656567401	\$2,000.00	0.40	\$1,200.00
26 Reynolds Amern Inc	RAI	RAI 7 5/8 06/01/16	761713AE6	761713106	\$2,000.00	0.40	\$1,200.00
27 Idearc Inc	IAR	IAR 8 11/15/16	451663AC2	451663108	\$2,000.00	0.40	\$1,200.00
28 KB Home	KBH	KBH 7 3/4 02/01/10	48666KAF6	48666K109	\$2,000.00	0.40	\$1,200.00
29 Advanced Micro Devices Inc	AMD	AMD 7 3/4 11/01/12	007903AJ6	007903107	\$2,000.00	0.40	\$1,200.00
Smurfit Stone Container							
30 Enterprises Inc	SSCC	SSCC 7 1/2 06/01/13	47508XAD7	832727101	\$2,000.00	0.40	\$1,200.00
Allegheny Engy Supp Co							
31 LLC	AYE	AYE 8 1/4 04/15/12	017363AE2	017361106	\$2,000.00	0.40	\$1,200.00
32 K Hovnanian Entpers Inc	HOV	HOV 6 1/2 01/15/14	442488AQ8	442487203	\$2,000.00	0.40	\$1,200.00
33 NOVA Chems Corp	NCX	NCX 0 11/15/13	66977WAH2	66977W109	\$2,000.00	0.40	\$1,200.00

High Yield Composite Basket CEBOS (BBR, BBS)

Company Name	Equity Ticker	Reference Obligation	REF OB CUSIP	Equity Cusip	Notional Weight	Recovery Rate	Cash Settlement Amount
34 Sanmina SCI Corp	SANM	SANM 8 1/8 03/01/16	800907AK3	800907107	\$2,000.00	0.40	\$1,200.00
35 TRW Automotive Inc	TRW	TRW 9 3/8 02/15/13	87264QAM2	87264S106	\$2,000.00	0.40	\$1,200.00
36 Beazer Homes USA Inc	BZH	BZH 6 1/2 11/15/13	07556QAJ4	07556Q105	\$2,000.00	0.40	\$1,200.00
37 Fst Oil Corp	FST	FST 7 3/4 05/01/14	346091AU5	346091705	\$2,000.00	0.40	\$1,200.00
38 Smithfield Foods Inc	SFD	SFD 7 3/4 05/15/13	832248AH1	832248108	\$2,000.00	0.40	\$1,200.00
39 Flextronics Intl Ltd	FLEX	FLEX 6 1/2 05/15/13	33938EAJ6	Y2573F102	\$2,000.00	0.40	\$1,200.00
40 Tesoro Corp	TSO	TSO 6 1/4 11/01/12	881609AQ4	881609101	\$2,000.00	0.40	\$1,200.00
41 Amkor Tech Inc	AMKR	AMKR 7 3/4 05/15/13	031652AQ3	031652100	\$2,000.00	0.40	\$1,200.00
42 ArvinMeritor Inc	ARM	ARM 8 1/8 09/15/15	043353AC5	043353101	\$2,000.00	0.40	\$1,200.00
43 Eastman Kodak Co	EK	EK 7 1/4 11/15/13	277461BD0	277461109	\$2,000.00	0.40	\$1,200.00
44 Mosaic Co	MOS	MOS 7 3/8 08/01/18	449669CD0	61945A107	\$2,000.00	0.40	\$1,200.00
45 Dillards Inc	DDS	DDS 7.13 08/01/18	254067AH4	254067101	\$2,000.00	0.40	\$1,200.00
46 Massey Engy Co	MEE	MEE 6 7/8 12/15/13	576203AH6	576206106	\$2,000.00	0.40	\$1,200.00
47 Mediacom LLC	MCCC	MCCC 9 1/2 01/15/13	58445MAJ1	58446K105	\$2,000.00	0.40	\$1,200.00
48 Unisys Corp	UIS	UIS 8 1/2 10/15/15	909214BK3	909214108	\$2,000.00	0.40	\$1,200.00
49 Visteon Corp	VC	VC 7 03/10/14	92839UAC1	92839U107	\$2,000.00	0.40	\$1,200.00
50 Std Pac Corp	SPF	SPF 7 08/15/15	85375CAT8	00206R102	<u>\$2,000.00</u>	0.40	<u>\$1,200.00</u>
					\$100,000		\$60,000