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Regulatory Circular RG05-74

To: DIA Trading Crowd Members

From: Trading Operations

Re: Linkage Plan Overview for DIA

The Linkage Plan (the Plan) will be implemented in DIAMONDS (DIA) when another option exchange lists DIA with CBOE. The corresponding CBOE linkage rules are 6.80 through 6.85. This memo is an overview for all CBOE members outlining the Plan requirements in a hybrid option class.

- Avoid Trade Throughs: CBOE Members should avoid initiating trade throughs of away exchange markets. If they do trade through a better market, members may be subject to liability by having to fill a Satisfaction order and may be required to adjust trade prices to the NBBO. Even if no S order is received, trade throughs will still be tabulated for regulatory review and possible disciplinary action. This Linkage Rule applies to all CBOE members.
- Avoid Locking or Crossing NBBO Markets: CBOE Members who create quotes that lock or cross another market should either move their market to unlock or uncross the NBBO, or if they are a market maker, they can also send a Principal order through linkage to trade with the away market. Failure to correct a locked or crossed market may result in disciplinary action. This Linkage Rule applies to all CBOE members.
- Unexecuted Linkage Orders: If inbound linkage orders are not fully traded electronically or from PAR within the allotted time period, the remaining balance will automatically reroute and trade with remaining volume in the hybrid quote, or the linkage order will be canceled (due to no quote size remaining).
- All floor brokers in multiply listed classes must set their PAR Profile to enable the NBBO Dialog window. This will allow each selected order to be viewed against the quotes from all markets, not just those at CBOE. Linkage functionality is only enabled for the PAR terminal operated by the OBO.
- Any eligible market maker can send a Principal order. To route P orders, market maker firms will provide CBOE members access to Linkage.
- Customer orders that are marketable against a better quote at another market will route to the DIA floor brokers' PAR, instead of the OBO. These orders should trade at the current NBBO price to avoid locking NBBO quotes or possible trade throughs.

Details on other aspects of linkage follow. For questions relating to the Linkage Plan, please contact Tim Watkins at (312) 786-7172, or Roger Mulcahy at (312) 786-7280. For regulatory questions related to linkage, please contact Margaret Williams at (312) 786-7834.

LINKAGE OVERVIEW in DIA:

- The Plan includes 3 order types for Linkage:
 - Principal-Acting-As-Agent (P/A) Order
A DPM, PAR Official, or OBO holding an unexecuted customer order can send a P/A linkage order representing the terms of that customer order to the NBBO market.
 - Principal (P) Order
Any eligible CBOE market maker can send a P linkage order for his own account to the NBBO market. This includes on-floor market makers, DPMs, eDPMs, RMMs, and LMMs.
 - Satisfaction (S) Order
Any market that trades through booked customer orders (in the displayed quote) may receive a Satisfaction order claiming liability on behalf of booked customer orders. The violating market is obligated to fill the S order. If no trade through occurred, or if a valid exception applies, the S order may be cancelled.
- The Plan establishes special minimum size guarantees and automatic execution requirements for incoming P/A and P orders. These guarantees require that the full linkage size must trade within 15 seconds or the receiving exchange's quote must fade from the NBBO price, with any remaining order balance canceled.
- CBOE autoex handling of inbound Linkage orders (in hybrid classes, including DIA):
 - Inbound Principal-Acting-As-Agent (P/A) and Inbound Principal (P) will both autoex against the hybrid quote up to the full size of the order, and any P/A or P order balance larger than the quote size will route to PAR for a 12-second period. If the P/A or P is not traded from PAR, it will reroute to trade with the hybrid quote. If no quote remains, the P/A or P order will be automatically canceled.
 - In certain scenarios a P/A or P order may not autoex against the hybrid quote, or the minimum Autoex Size does not trade. These orders will route to PAR, and the OBO will announce this condition to the trading crowd. The crowd should step up and at least fill this minimum amount at the original NBBO price.
 - Inbound Satisfaction (S) orders will route to PAR for 3 minutes, no autoex. Another exchange views CBOE as trading through their quote. CBOE members who traded through must fill the S order. Certain exemptions apply, allowing cancellation. Special rules exist for block trades.

General Linkage Plan Rules:

- Market Maker Eligibility - To participate in linkage, a market maker must be logged into Hybrid, must be making 2-sided quotes, and satisfy the Linkage 80/20 Test. A market maker cannot send P orders for more than 20% of his or her customer-traded contracts to an away market (must trade 80% or more at home exchange).
- If the originating exchange receives no response to a P/A or P order within 20 seconds, the originating member is entitled to trade through that NBBO price at the next best NBBO, without penalty, provided all markets at the better price have been addressed through linkage.
- Linkage fees for P/A and P orders may be set by each individual exchange. The receiving, or executing, exchange will charge a linkage fee if the order trades there.
- Principal Order Restrictions (P Class Gate): Autoex restrictions exist if multiple market makers from the same exchange route P orders for the same class to the same NBBO market at the same time. Once a P order is automatically executed, any subsequent P orders from that same exchange and the same option class can be rejected for the next 15 seconds. CBOE will address all inbound P orders for autoex handling after this 15-second reject period. (According to the Plan, any subsequent outbound P orders from CBOE can be routed for manual handling after this initial period and up to one minute. After one minute, the receiving market must resume autoex treatment for that class.)