

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁰

Florence E. Harmon,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-56970; File No. SR-CBOE-2007-99]

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of Proposed Rule Change, as Modified by Amendment Nos. 1 and 2 Thereto, Relating to a Delta Hedging Exemption From Equity Options Position Limits

December 14, 2007.

On August 21, 2007, the Chicago Board Options Exchange, Incorporated (“CBOE” or “Exchange”) 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 to create a delta hedging exemption from equity options position limits. On October 4, 2007, the Exchange filed Amendment No. 1 to the proposed rule change. The Commission published the proposed rule change, as amended by Amendment No. 1, for comment in the *Federal Register* on October 15, 2007.³ On October 24, 2007, the Exchange filed Amendment No. 2 to the proposed rule change.⁴ The Commission received no comments on the proposed rule change. This order approves the proposed rule change as modified by Amendment Nos. 1 and 2.

Under the proposal, the Exchange would provide an exemption from equity options⁵ position and exercise limits⁶ for positions held by CBOE

members and certain non-member affiliates⁷ that are “delta neutral”⁸ under a “permitted pricing model.”⁹ The options contract equivalent of the net delta¹⁰ of a hedged options position still would be subject to the position limits in Rule 4.11 (subject to the availability of any other position limit exemptions).¹¹ A member that intends to employ, or whose non-member affiliate intends to employ, this exemption would be required to provide a written certification to CBOE stating that the member and/or its affiliate will use a permitted pricing model.¹² In addition, members that carry an account that includes an equity option position for a non-member affiliate would be required to obtain a written statement from the non-member affiliate confirming that the affiliate: (1) Is relying on this exemption; (2) will use only a permitted pricing model for purposes of calculating the net delta of its option positions for purposes of this exemption; (3) will promptly notify the member if it ceases to rely on this

⁷ The Commission notes that only those non-member affiliates identified in the definition of “permitted pricing model” would be eligible to rely on the delta hedging exemption. See *infra* note 9.

⁸ The term “delta neutral” would be defined in proposed Rule 4.11.04(c)(A) as referring to an equity option position that is hedged, in accordance with a permitted pricing model, by a position in the underlying security or one or more instruments relating to the underlying security, for the purpose of offsetting the risk that the value of the option position will change with incremental changes in the price of the security underlying the option position.

⁹ “Permitted pricing model” for purposes of this exemption would be a pricing model used by: (1) A member or its non-member affiliate, using a pricing model maintained and operated by the Options Clearing Corporation; (2) a member or its non-member affiliate subject to consolidated supervision by the Commission pursuant to Appendix E of Rule 15c3-1 under the Act (*i.e.*, a consolidated supervised entity or “CSE”); (3) a financial holding company (“FHC”) or a company treated as an FHC under the Bank Holding Company Act of 1956, or its affiliate subject to consolidated holding company group supervision; (4) a Commission registered OTC derivatives dealer; and (5) a national bank under the National Bank Act. See proposed Rule 4.11.04(c)(C).

¹⁰ “Net delta” would be defined to mean, at any time, the number of shares (either long or short) required to offset the risk that the value of an equity option position will change with incremental changes in the price of the security underlying the option position. See proposed Rule 4.11.04(c)(B).

“Options contract equivalent of the net delta” would be defined to mean the net delta divided by the number of shares underlying the options contract. See proposed Rule 4.11.04(c)(B).

¹¹ See proposed Rule 4.11.04(c)(B). The Commission notes that Rule 4.11.04 provides for multiple, independent hedge exemptions. Of course, to the extent that a position is used to hedge for the purpose of one exemption from position limit requirements, such as the delta hedge exemption, such position cannot be used to take advantage of another exemption from position limit requirements.

¹² See proposed Rule 4.11.04(c)(E)(1) and (E)(3)(i)

exemption; (4) authorizes the member, upon request, to provide to the Exchange or the Options Clearing Corporation such information regarding positions of the non-member affiliate as part of the Exchange’s confirmation or verification of the accuracy of the net delta calculation under this exemption; and (5) if the non-member affiliate is using the Options Clearing Corporation model, has duly executed and delivered to the Exchange such documents as the Exchange may require as a condition to reliance on this exemption.¹³

Furthermore, any member would be required to report, in accordance with Rule 4.13, all equity options positions (including those that are delta neutral) that are reportable under that rule, and also would be required to report on its own behalf or on behalf of a designated aggregation unit¹⁴ the net delta and options contract equivalent of the net delta of such positions for each account that holds an equity option position subject to the delta hedging exemption in excess of the levels specified in Rule 4.11.¹⁵ Each member relying on the exemption would be required to retain, and undertake reasonable efforts to ensure that its non-member affiliates relying on the exemption retain, a list of the options, securities, and other instruments underlying each option position net delta calculation reported to the Exchange; and to produce such information to the Exchange upon request.¹⁶ In addition, the options positions of a non-member relying on the exemption would be required to be carried by a member with which it is affiliated.¹⁷

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange.¹⁸ In particular, the Commission believes that the proposed rule change is consistent with section

¹³ See proposed Rule 4.11.04(c)(E)(3)(ii).

¹⁴ See proposed Rule 4.11.04(c)(D), which provides, under certain conditions, that the net delta of an options position held by an entity entitled to rely on the exemption could be calculated without regard to positions in or relating to the security underlying the option position held by an affiliated entity or another trading unit within the same entity, provided that, among other things, no control relationship exists between such affiliates or trading units and the entity has designated in writing in advance the affiliates or trading units that are to be considered separate and distinct from each other.

¹⁵ See proposed Rule 4.11.04(c)(F).

¹⁶ See proposed Rule 4.11.04(c)(G).

¹⁷ See proposed Rule 4.11.04(c)(E)(2).

¹⁸ In approving this rule, the Commission notes that it has considered the proposed rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁰ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 56631 (October 9, 2007), 72 FR 58341.

⁴ In Amendment No. 2, CBOE made a technical revision to the proposal. This is a technical amendment and is not subject to notice and comment. In Amendment No. 2, CBOE noted that the effective date of the proposal will be February 1, 2008, or such later date as may be necessary to ensure completion of the required technology changes by the Options Clearing Corporation and the Securities Industry Automation Corporation.

⁵ Equity options for purposes of this proposed rule change includes stock options and options on exchange-traded funds.

⁶ CBOE Rule 4.12 establishes exercise limits for an option at the same level as the option’s position limit under Rule 4.11. Therefore, no changes are proposed to Rule 4.12.

6(b)(5) of the Act,¹⁹ which requires, among other things, that CBOE rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The Commission has previously stated its support for recognizing options positions hedged on a delta neutral basis as properly exempted from position limits.²⁰

It is therefore ordered, pursuant to section 19(b)(2) of the Act,²¹ that the proposed rule change (SR-CBOE-2007-99), as modified by Amendment Nos. 1 and 2, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²²

Florence E. Harmon,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-56960; File No. SR-ISE-2007-118]

Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change as Modified by Amendment No. 1 Thereto Relating to Fee Changes

December 13, 2007.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on December 11, 2007, the International Securities Exchange, LLC (“ISE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items

have been substantially prepared by the Exchange. The Exchange has designated this proposal as one establishing or changing a due, fee, or other charge imposed by ISE under Section 19(b)(3)(A)(ii) of the Act³ and Rule 19b-4(f)(2) thereunder,⁴ which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

ISE proposes to amend its Schedule of Fees to reflect the addition of six new Premium Products.⁵ The text of the proposed rule change is available at the Commission’s Public Reference Room, at the Exchange, and on its Web site at <http://www.ise.com>.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change, and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange is proposing to amend its Schedule of Fees to reflect the addition of options on the following new products: the ProShares UltraShort QQQ Fund® (“QID”), ProShares Ultra QQQ Fund® (“QLD”),⁶ ProShares

UltraShort S&P500® Fund (“SDS”), ProShares Ultra S&P500® Fund (“SSO”),⁷ ProShares UltraShort Russell2000 Fund (“TWM”) and ProShares Ultra Russell2000 Fund (“UWM”).⁸ The Exchange represents that QID, QLD, SDS, SSO, TWM and UWM are eligible for options trading because they constitute “Exchange-Traded Fund Shares,” as defined by ISE Rule 502(h).

All of the applicable fees covered by this filing are identical to fees charged by the Exchange for all other Premium Products. Specifically, the Exchange will charge an execution fee and a comparison fee for all transactions in options on QID, QLD, SDS, SSO, TWM and UWM.⁹ The amount of the

for trading, marketing, and promotion of options on QLD and QID or with making disclosures concerning options on QLD and QID under any applicable federal or state laws, rules or regulations. NASDAQ and ProShares do not sponsor, endorse, or promote such activity by ISE and are not affiliated in any manner with ISE.

⁷ “Standard & Poor’s®,” “S&P®,” “S&P 500®,” “Standard & Poor’s 500®,” “Standard & Poor’s Depository Receipts®,” and “SPDR®” are trademarks of The McGraw-Hill Companies, Inc. (“McGraw-Hill”), and have been licensed for use by ProShares in connection with the listing and trading of the SSO and the SDS on the American Stock Exchange. SSO and SDS are not sponsored, sold or endorsed by Standard & Poor’s (“S&P”), a division of McGraw-Hill, and S&P makes no representation regarding the advisability of investing in SSO and SDS. McGraw-Hill, S&P and ProShares have not licensed or authorized ISE to: (1) Engage in the creation, listing, provision of a market for trading, marketing, and promotion of options on SSO and SDS; or (2) to use and refer to any of their trademarks or service marks in connection with the listing, provision of a market for trading, marketing, and promotion of options on SSO and SDS or with making disclosures concerning options on SSO and SDS under any applicable federal or state laws, rules or regulations. McGraw-Hill, S&P and ProShares do not sponsor, endorse, or promote such activity by ISE and are not affiliated in any manner with ISE.

⁸ “Russell 2000® Index” is a trademark of Frank Russell Company (“Russell”) and has been licensed for use ProShares in connection with the listing and trading of the UWM and TWM on the American Stock Exchange. UWM and TWM are not sponsored, sold or endorsed by Russell, and Russell makes no representation regarding the advisability of investing in UWM and TWM. Russell and ProShares have not licensed or authorized ISE to: (1) Engage in the creation, listing, provision of a market for trading, marketing, and promotion of options on UWM and TWM; or (2) to use and refer to any of their trademarks or service marks in connection with the listing, provision of a market for trading, marketing, and promotion of options on UWM and TWM or with making disclosures concerning options on UWM and TWM under any applicable federal or state laws, rules or regulations. Russell and ProShares do not sponsor, endorse, or promote such activity by ISE and are not affiliated in any manner with ISE.

⁹ These fees will be charged only to Exchange members. Under a pilot program that is set to expire on July 31, 2008, these fees will also be charged to Linkage Orders (as defined in ISE Rule 1900). See Securities Exchange Act Release No. 56128 (July 24, 2007), 72 FR 42161 (August 1, 2007) (SR-ISE-2007-55).

¹⁹ 15 U.S.C. 78f(b)(5).

²⁰ See Securities Exchange Act Release No. 40594 (October 23, 1998), 63 FR 59362, 59380 (November 3, 1998) (File No. S7-30-97) (adopting rules relating to OTC derivatives dealers). The Commission notes that it recently approved a proposal by the National Association of Securities Dealers, Inc. (n/k/a Financial Industry Regulatory Authority, Inc.) to expand the class of entities permitted to use the delta hedging exemption from equity options position limits. See Securities Exchange Act Release No. 56916 (December 6, 2007), 72 FR 70627 (December 12, 2007) (SR-NASD-2007-044).

²¹ 15 U.S.C. 78s(b)(2).

²² 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(ii).

⁴ 17 CFR 240.19b-4(f)(2).

⁵ “Premium Products” is defined in the Schedule of Fees as options on the products enumerated therein.

⁶ “NASDAQ-100 Index” is a trademark of the NASDAQ Stock Markets, Inc. (“NASDAQ”) and has been licensed for use by ProShares in connection with the listing and trading of the QLD and the QID on the American Stock Exchange. QLD and QID are not sponsored, sold or endorsed by NASDAQ, and NASDAQ makes no representation regarding the advisability of investing in QLD and QID. NASDAQ and ProShares have not licensed or authorized ISE to: (1) Engage in the creation, listing, provision of a market for trading, marketing, and promotion of options on QLD and QID; or (2) to use and refer to any of their trademarks or service marks in connection with the listing, provision of a market