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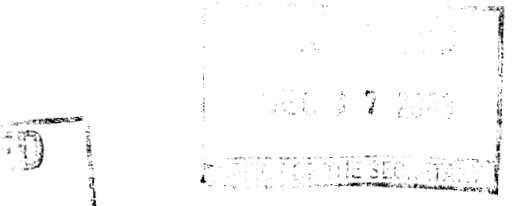

July 21, 2003

Ms. Annette Nazareth
Director
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

4-469

Dear Annette:

It **was** good meeting with you and Lori. **As** we discussed, I am enclosing a letter prepared by our outside counsel, Schiff Hardin & Waite, describing the substantial legal precedent which establishes that a license from the owner of a stock index is needed in order for an exchange to be able to trade derivatives based on that index. The letter clearly distinguishes the holding in *Golden Nugget* from those cases involving attempts by exchanges to trade indexed derivatives without licenses from the owners of the indexes. I hope this helps to further clarify these issues.

Joanne Moffic-Silver, Michael Meyer, and I would be glad to further discuss these issues with you, if you would find it helpful.

Sincerely,

Bill

WJB/sls
Enclosure

cc: Robert Colby, Esquire
Elizabeth King, Esquire

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July 17, 2003

Joanne Moffic-Silver, Esq.
General Counsel
Chicago Board Options Exchange, Inc.
400 South LaSalle Street
Chicago, Illinois 60605

Dear Joanne:

You asked me to consider whether the 1987 U.S. Court of Appeals decision in Golden Nugget v. American Stock Exchange[1] is inconsistent with earlier court decisions to the effect that an exchange needs a license from the owner of a stock index in order to trade derivatives based on that index. Golden Nugget held that an exchange trading options on Golden Nugget common stock may without a license use the "Golden Nugget" name as a means of identifying the issuer of the option's underlying stock, As explained below, I believe the decision in Golden Nugget is entirely consistent with those earlier decisions, and should not be read as allowing an exchange to use a stock index in connection with trading in index options unless it has a license to do so from the owner of the index.

In Golden Nugget, the Court addressed whether the trading of options on Golden Nugget common stock on the American Stock Exchange without the consent of the issuer constituted a misappropriation of the issuer's property, infringed on its trade name or constituted unfair competition. After determining that the federal Securities Exchange Act of 1934 did not preempt the application of state law in these respects (federal preemption had been the basis of the District Court's dismissal of the case), the Court of Appeals held that the issuer had no identifiable property right that was misappropriated by the Amex, and that it is not a violation of a company's trademark for another party to accurately and not deceptively identify a product by reference to the trademark. For the same reasons, and because the Court found nothing dishonest or unfair in the Amex's conduct, the Court did nut find Amex had engaged in the tort of unfair competition as a result of its trading Golden Nugget options without the issuer's consent.

In reaching this conclusion, the Court in Golden Nugget took pains to distinguish the issues in the case before it from issues addressed in prior cases concerning attempts by exchanges to trade indexed derivatives without licenses from the owners of the indexes. Those cases are Board of Trade v. Dow Jones & Co.[2] and Standard & Poor's Corp. v. Commodity Exchange, Inc.[3]

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[1] 828 F.2d 585 (9th Cir. 1987)
[2] 98 Ill 2d 109, 456 N.E.2d 84 (1983), aff'g 108 Ill. App.3d 681 (1st Dist 1982)

In the Board of Trade case, having failed in its effort to secure a license from Dow Jones permitting it to use the Dow Jones Industrial Average as the basis of a new futures contract to be traded in its market, CBOT submitted a proposal to the CFTC to trade a futures contract that would be based on the DJIA, but would be designated as the "CBT Index", presumably to avoid infringing on Dow Jones' trademarks. The CFTC approved the CBOT filing by designating CBOT as a contract market for the CBT Index contract.

While its application for contract market designation was pending at the CFTC, CBOT filed a declaratory judgment action in the Illinois state court seeking a declaration that trading a futures contract based on the DJIA would not violate the proprietary rights of Dow Jones in its index. Dow Jones took the position that trading such a contract would amount to the misappropriation of its rights to the DJIA. The trial court found that Dow Jones had a proprietary right in its index and that a wrongful use of that index would be actionable, but that the CBOT's proposed use of the DJIA was not a misappropriation of Dow Jones' property so long as CBOT used a disclaimer disavowing that its contract had any association with Dow Jones. .The Illinois Appellate Court disagreed, and reversed the finding of the lower court on the basis that CBOT's proposed use of Dow Jones expertise in developing and maintaining an index intended to correlate with the general pattern of stock market activity and its attempt to associate the CBT Index with the "aura of reliability, respectability, or expertise" associated with a Dow Jones index, constituted a misappropriation "not of Dow Jones' name, but of the property right of Dow Jones in its averages and the good will and public respect attendant to them.'" The Illinois Supreme Court affirmed the judgment of the Appellate Court on essentially the same misappropriation grounds.

In affirming the right of Dow Jones to prevent the unlicensed use of its index In connection with futures trading, the Illinois Supreme Court directly addressed the connection between fostering creativity and protecting the right of those who create not to have the fruits of their efforts misappropriated. In this respect, the Court observed, "Whether protection against appropriation is necessary to foster creativity depends in part upon the expectation of that sector of the business community which deals with the particular intangible. If the creator of an intangible product expects to be able to control the licensing or distribution of the intangible in order to profit from his effort, and similarly those who would purchase the product expect and are willing to pay €or the use of the intangible, a better argument can be made in favor of granting protection."[5] Experience during the years since the Board of Trade case was decided has confirmed that both creators of indexes and their licensors often share a common belief that the value of an index may best be realized through exclusive licensing arrangements.

The Illinois Supreme Court also observed that finding Dow Jones "... has a proprietary interest in its indexes and averages which vests it with the exclusive right to license their use for trading in stock

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[3] 683 F.2d 704 (2d Cir 1982), aff'g 538 F Supp. 1063 (S D N Y. 1982)
[4] 108 Ill App 2d 681 at 695
[5] 98 Ill 2d 109 at 120

index futures would not preclude [CBOT] and others from marketing stock index futures contracts. The extent of defendant's [Dow Jones'] monopoly would be limited, for as defendant points out, there are an infinite number of stock market indexes which could be devised."[6]

The Comex case involved similar facts. There, too, Comex failed in its effort to secure a license from S&P that would have permitted it to use the S&P 500 Index and related trademarks for a futures contract to be traded on that exchange. As CBOT had done when it was unable to secure a license from Dow Jones, Comex filed an application with the CFTC to be designated as a contract market for futures contracts based on a "Comex 500" index, described as an index that "essentially duplicates" the S&P 500. Comex advertised its proposed new index future by referring to the S&P 500 Index without disclaiming any relationship with or sponsorship by S&P. In response, S&P filed suit against Comex seeking a preliminary injunction against the use of its index as a misappropriation of its property, and against the use of its trademarks on the ground that this would prbduce'confusion as to the source of the 500 index proposed to be used by Comex and S&P's affiliation therewith. The U.S. District Court for the Southern District of New York granted a preliminary injunction on both trademark and misappropriation grounds, and the Court of Appeals affirmed the District Court's action, In affirming, the Court of Appeals made it clear that its decision could stand on misappropriation grounds alone by acknowledging that even if the prominent use of disclaimers might reduce S&P's chance of success on trademark grounds, "the broad preliminary injunction is adequately supported by S&P's misappropriation claim against Comex."[7]

By contrast to the Board of Trade and Cornex cases, Golden Nugget involved only the use of a trade name to describe an option, and not the use of any of Golden Nugget's property. Although Golden Nugget attempted to assert a misappropriation claim in reliance on Board of Trade and Comex, the court in Golden Nugget distinguished those cases because they each involved a person who "... had a proprietary interest in its own product [i.e., the index] that was being used to the commercial advantage of the appropriator and to the disadvantage of its owner. This case is different. Quite simply, appellant's misappropriation claim fails because it had no property interest that could be misappropriated."[8]

In other words, Golden Nugget stands for the proposition that the mere use of a trade name to accurately identify a product neither constitutes the misappropriation of property of the owner of the trade name nor an infringement of the owner's trademark rights. Accordingly, Golden Nugget has no bearing on the right of the owner of property associated with a stock index to prevent the misappropriation of its property by an exchange seeking to trade instruments based on the index without a license from the owner.

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[6] Id. at 121
[7] 683 F.2d 704 at 710
[8] 828 F.2d 586 at 591

The same two part analysis focusing on the use of the trademark and the separate use of the data embodied in the index is reflected in the recent case of The McGraw Hill Companies, Inc. v. Vanguard Index Trust'. That case involved Vanguard's attempt to use the S&P 500 Index in connection with a new exchange-traded fund, relying on a license it was previously granted to use the Index in connection with mutual funds generally. In that case both parties acknowledged that a license to use the Index was required, and they disagreed only as to whether Vanguard already had been granted such a license. Consistent with this, the court in McGraw Hill did not even consider whether Vanguard could sponsor an ETF indexed to the S&P 500 without any license from McGraw Hill at all. Instead, throughout its opinion the court referred to the need for Vanguard to have a license to use "the S&P 500 data" represented by the index as well as a separate license to use trademark rights associated with the index. In this respect, the McGraw Hill decision is entirely consistent with the holding in Golden Nugget, which, as noted above, is limited to permitting the unlicensed use of trademarks for descriptive purposes only, and does not support the unlicensed use of an index associated with trading in an indexed securities product.

In conclusion, I believe the Board of Trade, Comex, Golden Nugget and McGraw Hill cases all reflect the same recognition that when an exchange trades an index option or other index derivative, it does not just make use of the name associated with the index for mere descriptive purposes, but it also makes use of the expertise, reputation and goodwill of the owner of the index in marketing the indexed product, and it and its clearing house make use of the data that constitutes the index in calculating settlement values and taking other action in support of the trading of the indexed product. There is nothing in the Golden Nugget opinion or in any of these other opinions that would allow an exchange to use an index for these purposes without a license from the owner of the index.

Very truly yours,

Michael L. Meyer

MLM/dcg

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[9] 139 F. Supp. 2d 544 (S.D.N.Y.. 2001)