



Date: May 27, 2005

To: The Membership

From: Office of the Chairman

Re: Options on Diamonds (DIA)

For the past several days, the Exchange has been monitoring an attempt by the International Securities Exchange ("ISE") to list options on the ETFs on the Dow Jones Industrial Average ("DIAMONDS") without a license. As most of you are aware, CBOE has an exclusive license agreement with Dow Jones & Co., the publisher and owner of the Dow Jones Industrial Average, to trade DIA options since May of 2002. The ISE's claim, similar to the one it is making with respect to options on SPDRs, is that it cannot be required to obtain a license in connection with trading DIA options. We disagree with this claim, and wanted to take this opportunity to inform you of the situation and what CBOE is doing to address it.

- On Monday, May 23<sup>rd</sup>, CBOE first learned of ISE's attempt to certify (that is, register with the Options Clearing Corporation for listing) options on DIA.
- CBOE initiated contact with Dow Jones & Co. to inform them of this, and Dow Jones immediately began legal action.
- Dow Jones obtained a temporary restraining order (TRO) precluding ISE from listing or trading options on DIA until the matter could be heard in court. That hearing is scheduled for Friday, May 27<sup>th</sup>, at 9:15 AM ET.
- To keep the ISE from listing the product while the litigation proceeds, Dow Jones will have to convince the court to extend the TRO. If the court does not extend the TRO, ISE could conceivably begin trading options on DIA as soon as after the hearing on Friday. However, the legal issues would continue to be adjudicated.
- Given the imminent possibility that ISE could commence trading, the Office of the Chairman has been in communication with representatives of the index community and the DIA crowd to determine our competitive response. Exchange staff is now making preparations, in accordance with instructions received from the OOC and relevant index committees, to deal with matters that may arise from multiple listing, including linkage, fees and payment for order flow.

As was announced on May 13, 2005, the Exchange had been planning to introduce a new, non-DPM form of Hybrid in DIA options following July expiration. CBOE has filed rules with the Securities and Exchange Commission ("SEC") to allow for this platform, and those rules have been published for comment. The comment period expires on June 7<sup>th</sup>, 2005, and SEC approval is expected sometime thereafter.

Given that CBOE was already planning on taking this step, and preparations were already being made, the Exchange sees no need to divert from that course. Rather, the timeline has been accelerated, and the plan is now to launch DIA options on this new hybrid platform as soon as

possible following SEC approval. Exchange staff has been in contact with DIA crowd members to prepare them for Hybrid, and the requisite operational tasks have been or are in the process of being completed. There will be no DPM assigned to the DIA options at this time, and the Index Floor Procedures Committee will oversee the application of the system. As is the case with our current hybrid technology, we expect this platform to be highly competitive.

We will keep the Membership informed of events as they progress. You may be assured that CBOE continues to vigorously defend its rights to our intellectual property and proprietary products, and that we will continue to do so in the future. If you have any questions, please direct them to Bill Brodsky, Ed Joyce or Ed Tilly.