

Updates to the Chicago Board Options Exchange Membership Meetings

Spotlight on: CBOE Moves Towards New Business Model

At its meeting on September 14, 2005, the CBOE Board of Directors approved the recommendations of the CBOE Business Model Task Force to begin the process of converting CBOE to a for-profit corporation.

The Business Model Task Force, appointed in January 2005, was charged with exploring how CBOE could best redefine its business model to take full advantage of a rapidly-changing marketplace. New business models, such as those resulting from the CME, ISE and CBOT IPOs, and the announced NYSE/Archipelago combination, have dramatically altered the competitive landscape.

CBOE will begin the transition process in January 2006. Initial steps will include:

- Streamlining the 2006 operating budget, based on a for-profit model.
- Examining the Exchange's committee structure, particularly the composition of the Advisory Committees, to determine if they reflect the committee structures of for-profit enterprises.
- Addressing the exercise rights held by Full CBOT Members.

CBOE members should also be aware that:

- The transition to a for-profit model will be a lengthy and complex process.
- Many legal documents will need to be prepared, filed and approved by the SEC.
- The services of Goldman Sachs have been retained to advise and guide CBOE through the transition process.
- CBOE's emphasis, at all stages of development of the new model, will be on adding value for our members and owners.
- Ultimately, the SEC and the CBOE owners are required to approve the final structure before a business model transformation can be implemented.

The intent of the move to a for-profit model is to give CBOE the flexibility to quickly respond to the challenges and opportunities presented in a highly-competitive marketplace. The new business model will provide strategic agility not inherent in our current structure. As developments occur, members will be kept apprised.

CBOE Launches Several Innovative Products

Jumbo-DJX Index Options

CBOE launched Jumbo-DJX index options, based on the Dow Jones Industrial AverageSM (DJIA[®]), on October 11, 2005. The Jumbo-DJX options (DXL) are 1/10th the value of the Dow Jones Industrial Average, with a multiplier of \$100, but ten times larger than the DJX options contract currently traded at CBOE. DXL options are cash-settled, with European-style exercise.

CBOE now offers a full suite of products based on the Dow Jones Industrial Average and other Dow Jones Indexes. In addition to DJX options, traded at CBOE since 1997, CBOE also offers options on the DIAMONDS® (DIA®) exchange-traded fund, which is approximately 1/100th the value of the DJIA.

CBOE also offers options on the Dow Jones Transportation Average (DTX), Dow Jones Utility Average (DUX), Dow Jones Equity REIT Index (DJR), Dow 10 Index (MUT) and Dow Jones Internet Commerce Index (ECM).

Please visit www.cboe.com/Products for additional contract specifications.

Mini-SPX Index Options

CBOE will launch a new options contract, Mini-SPX options, based on the Standard & Poor's 500 Index, beginning October 25, 2005. Mini-SPX options (XSP) will be 1/10th the value of the S&P 500® Index, and will trade on CBOE's Hybrid Trading System, which includes Remote Market Makers. Trading XSP options on CBOE's Hybrid Trading System will offer investors a smaller-sized S&P 500 contract with the combined advantages of electronic trading and the open-outcry market on a single platform.

Mini-SPX options will be based on 1/10th the value of the S&P 500 Stock Index, and will be cash-settled and European exercise. Mini-SPX options will be offered in addition to the S&P 500 Index (SPXSM) options which are full-value, cash-settled, with European-style exercise, and options on SPDRs (SPY), which are American-style exercise that settle into shares of the SPDRs Exchange-Traded Fund, which represents about 1/10th the value of the S&P 500 Index.

CBOE also offers two index options based on the S&P 100 Index; the OEX® is a cash-settled, American-style exercise contract, and the XEO®, which is cash-settled, with European-style exercise. Options on the iSharesSM S&P 100® Index Fund (OEF), an exchange-traded fund, which is American-style exercise, are also offered at CBOE.

Members may visit www.cboe.com/miniSPX for additional contract specifications on the new product.

"Weeklys"

CBOE has created and will launch a new type of option, "Weeklys,SM" on October 28, 2005. Weeklys will have a life of one week, listing on a Friday, and expiring the following Friday, thus providing an efficient way to trade options specifically around certain news or events—such as economic data or earnings announcements.

Weeklys option contracts based on the S&P 500 Index (SPX) and on the S&P 100 Index (OEX) will open on Friday, October 28, and will expire the following Friday, November 4. New series will be listed each Friday, expiring the following Friday, except that no Weeklys will be listed that would expire during expiration week for standard options.

In general, Weeklys will have the same contract specifications as standard options, except for the expiration date and time to expiration. Initially, no more than five strike prices will be listed per class, per expiration (two in-, one at-, and two out-of-the-money strike prices), and no new series will be added between listing and expiration.

For more information on Weeklys, please visit www.cboe.com/Weeklys.

"Gas At The Pump" Futures

The CBOE Futures Exchange (CFE) will launch an innovative new product, "Gas At The PumpSM" futures, on October 28, 2005, pending regulatory approval. "Gas At The Pump" futures (GAPP) are designed to track the retail price for regular gasoline that consumers pay at the pump.

CFE will launch six different “Gas At The Pump” contracts: one based on the average U.S. price for gasoline resulting from a survey of approximately 800 stations across the country, and five others based on the average price of their respective geographic regions, known as Petroleum Administration for Defense Districts, within the United States. The contracts will be settled monthly based on the survey of retail gasoline outlets conducted by the Energy Information Administration (EIA), an independent statistical and analytical agency within the U.S. Department of Energy.

“Gas At The Pump” futures will be traded electronically, via CBOE*direct*®, and will be cleared through the triple-A rated Options Clearing Corporation (OCC). At expiration, GAPP futures contracts will be cash-settled, based on the final settlement price determined by the surveys conducted by the EIA.

Initial contract months for GAPP futures will be December, January, March and June. In general, there will be two near-term contract months plus two additional contract months on the March quarterly cycle. Price quotations will reflect the expected U.S. cost, in dollars and cents, per gallon of gas. For more details and contract specifications, visit <http://cfe.cboe.com/Gas> or contact Patrick Fay, CFE Managing Director, at 312.786.7925.

CBOE NASDAQ-100 BuyWrite Index

On September 9, 2005, CBOE and The Nasdaq Stock Market,SM Inc. (NASDAQ) announced that they signed an agreement for CBOE to calculate and disseminate the CBOE NASDAQ-100 BuyWrite Index (BXNSM). The new index is calculated using options on the NASDAQ-100 Index® (NDX).

The new CBOE NASDAQ-100 BuyWrite Index is a benchmark index that measures the performance of a theoretical portfolio that sells NDX call options against a portfolio of the stocks included in the NASDAQ-100 Index.

The CBOE NASDAQ-100 BuyWrite Index is jointly owned by CBOE and by NASDAQ. CBOE is now calculating and disseminating the BXN price at the end of each trading day. Historical daily values for the BXN are available dating back to December 30, 1994. For more data and information about BXN and its use as a portfolio management tool, please visit www.cboe.com/BXN.

CBOE Hybrid Gets Several Major Enhancements

Several major enhancements to the CBOE Hybrid Trading System have been or will be implemented shortly. These include:

Automated Improvement Mechanism (AIM)

- A paired order mechanism for facilitation and solicitation with orders of 49 or less guaranteed price-improvement from the NBBO.
- A 3–5 second auction is conducted for potential price improvement.
- Status: The software has already been fully implemented. Rules have been noticed by the SEC. Activation will occur upon SEC rule approval.

Complex Order Book/Complex Order Auction (COB/COA)

- Complex orders resting in the COB will automatically execute when legs line up or when touched by other strategy orders or strategy quotes. Firms can choose whether to route orders directly to COB or the Public Automated Routing (PAR) system first.
- COB rollout to all classes was completed 10/3/05.
- With COA, incoming marketable and near-marketable spreads will initiate a 1–2 second auction for price improvement.
- COA software has already been fully implemented. Rules have been sent to SEC. Activation will occur upon SEC rule approval.

Hybrid Agency Liaison (HAL)

- When CBOE is not the National Best Bid or Offer, marketable orders will be flashed at the NBBO. If members do not step up to the NBBO, the order will be auto-linked and automatically sent through the Linkage System.
- Implementation is planned for completion by late November. Activation will occur upon SEC rule approval.

Hybrid Opening Enhancements (HOPE)

- Enhancements to current opening procedures designed to shorten the amount of time required to open a class and reduce the potential for out of range opening prices.
- Implementation was completed 10/7/05. This procedure includes an optional NBBO check for opening rotation that will be activated upon direction from market performance and procedures committees.

PAR Auto-Link Enhancements (AL)

- Until HAL is activated, NBBO rejects that route to PARs will automatically be sent to the away exchange through Linkage after 5 seconds unless the PAR broker manually addresses the order.
- The software has already been fully implemented. Activation has occurred in 25 trading crowds. The balance should be completed in October, subject to establishment of linkage clearing accounts by DPMs.

For further information on these enhancements, members may contact Anthony Montesano, Vice President, Trading Operations, at 312.786.7365 or (<mailto:montesan@cboe.com>); Carol Zylus at 312.786.7174 or (<mailto:zylusc@cboe.com>).

Resources Available for More Information on Hybrid Trading and Programs

Members with questions on various aspects of the Hybrid Trading System may contact the following individuals by phone or through the e-mail links listed:

- Rules Relating to Hybrid 1.0 or 2.0, including rules and regulations for e-DPMs and RMMs: Angelo Evangelou, Managing Senior Attorney, at 312.786.7464 or (<mailto:evangelou@cboe.com>)
- Getting connected to trade on Hybrid, either on or away from the trading floor: Curt Schumacher, Vice President and Chief Technology Officer, 312.786.7564 or (<mailto:curt@cboe.com>)
- General business issues such as Hybrid functionality, order routing and trading policies/procedures: Anthony Montesano, Vice President, Trading Operations, at 312.786.7365 or (<mailto:montesan@cboe.com>); Carol Zylus at 312.786.7174 or (<mailto:zylusc@cboe.com>)
- Access issues for the RMM, e-DPM and Remote Access for Floor Traders Programs: Dan Hustad, Vice President of Market Quality Assurance, at 312.786.7715 or (<mailto:hustadd@cboe.com>); Angela Redell, Director, Market Quality Assurance, at 312.786.7559 or (<mailto:redella@cboe.com>).
- To arrange for a demonstration of the CBOE HyTS[®] Terminal, which provides electronic access and order routing to U.S. options exchanges, as well as complete access to market data, streaming quotes, and order management—all on a single screen: Andrew Lowenthal, Director, Business Development, at 312.786.7180 or (<mailto:lowenthl@cboe.com>).

Additional information is available at <https://www.cboe.org/Hybrid>.

Court Rules Regarding Options on ETFs

On September 1, 2005, the U.S. District Court, Southern District of New York, dismissed claims that options that settle into exchange-traded funds (ETFs) were subject to a property right. This ruling only dealt with options on ETFs, and does not apply to options on cash-settled indexes, which were not under consideration by the court.

The court lifted a temporary restraining order that had prevented ISE or any other exchange from listing or trading options on DIA without a license and denied Dow Jones' request for a preliminary injunction against such activities. In a related matter, brought by the Standard and Poor's division of McGraw-Hill, seeking to enjoin ISE from listing or trading options on S&P Depositary Receipts (SPDR®), the judge dismissed the complaint upon a finding that S&P did not have a protectible interest in those ETF options. These two cases were consolidated by the court and heard as one case.

Dow Jones & Co. and S&P/McGraw-Hill have appealed. It is anticipated that a decision on the appeal will be made in the next five to eight months. We are monitoring these actions closely. CBOE remains vigilantly committed to protecting our intellectual property, our leasing agreements and our contract rights.

CBOE Members may access the full text of the September 1 court ruling by clicking "ETF Options Decision" within the "Spotlight" section at <https://www.cboe.com/members>.

CBOE Members and Staff Generously Support Hurricane Relief Efforts

The overwhelming generosity of our members and staff was evident during CBOE's recent drive to raise funds to support hurricane relief efforts. Donations totaled \$287,350.69.

At the request of several members during our drive, CBOE accepted contributions for several charitable organizations working on Hurricane Katrina Relief Efforts. Those organizations are: the American Red Cross, the Salvation Army, the Bush Clinton Katrina Fund, Catholic Charities and the United Way.

In addition, the CBOE Board of Directors approved a CBOE contribution in the amount of \$300,000.

It is in times of difficulty and tragedy that true generosity and compassion are most needed, and we commend everyone for their efforts.

For information on the CBOE Hurricane Relief Efforts, please contact Christy Hahn, Civic and Governmental Affairs Manager, at 312.786.7066 or (<mailto:hahnc@cboe.com>).

Fundraising Drive to Support Pakistan Earthquake Relief Efforts

As a result of the devastating Pakistan earthquake, millions of people are in need of necessities such as food and shelter. To help support the recovery efforts, CBOE will be conducting a fundraising drive to support the Islamic Circle of North America (ICNA).

On October 27, CBOE will be collecting funds in the lobby of the Exchange to support relief efforts. Individuals may also contribute by writing a check to ICNA Relief and sending it to Christy Hahn, Civic and Governmental Affairs Manager, CBOE, 400 S. LaSalle St., Chicago, Illinois 60605. To learn more about ICNA, please visit www.ICNA.org or contact Ms. Hahn at 312.786.7066 or (<mailto:hahnc@cboe.com>).

Washington Update*Commodity Futures Trading Commission Reauthorization*

The Senate Banking Committee held a hearing September 8, 2005 titled "Examining the Commodities Futures Modernization Act of 2000 and Recent Market Developments." The U.S. Securities Markets Coalition testified at the hearing, representing all six options exchanges and the Options Clearing Corporation. The Coalition testified regarding margin requirements for single stock futures (SSF), and the importance of parity for both SSF products and options. The U.S. Senate Banking Committee has requested the Presidential Working Group (PWG), which consists of the Treasury Department, the Federal Reserve Board, the Securities and Exchange Commission and the Commodity Futures Trading Commission, report back with specific recommendations on reauthorization. The PWG is expected to release a report shortly, and we anticipate a favorable outcome for options.

Congressional Visits

CBOE, along with the CME and CBOT, sponsored a U.S. Senate Banking Committee staff educational trip to Chicago. Staff met with CBOE PAC Board members, had a trading floor tour and attended an educational session on options.

Congressman Collin Peterson (D-MN), ranking member of the House Agriculture Committee, and Congressman Kenny Hulsholf (R-MO) visited the Exchange, met with PAC Board members, and toured the trading floor. Senator Jeff Bingaman (D-NM), member of the Senate Finance Committee, also visited the Exchange this past month. Other recent visitors to the Exchange include: Congressmen Danny Davis (D-IL), Patrick McHenry (R-NC), Vito Fossella (R-NY); Congresswoman Shelley Berkley (D-NV); and Senator Jim DeMint (R-SC).

Financial Update

For the first eight months of 2005, CBOE reported a pre-tax profit of \$12.9 million, compared to a budgeted pre-tax profit of \$2.7 million. Strong volume and control over expenses allowed CBOE to post these positive results. Volume averaged 1,747,000 contracts per day during this time period, which is 24% more than the 1,408,300 contracts that CBOE averaged for the six months ended December 31, 2004. Working capital for the Exchange increased from \$42.4 million to \$54.5 million during this time period. During the first eight months, CBOE recorded new capital expenditures of \$15.0 million, mostly related to the implementation of our Hybrid Trading System, systems capacity upgrades, and our disaster recovery site. CBOE also received \$5.0 million from the National Stock Exchange (NSX) in January, representing the first installment of the sale of our interest in NSX and also disbursed \$6.0 million from our working capital for the purchase of CBOT exercise rights at the end of May.

CBOE Volume Update for September 2005 –**Total Volume Surges 56%; Average Daily Volume for Month Hits New All-Time High***Exchange Volume, September 2005:*

Total Volume

- 41,206,760 contracts
- +56% vs year-ago (September 04)

Average Daily Volume

- 1,962,227 contracts
- +56% vs year-ago (September 04)

Year-To-Date Volume

- 334,991,587 contracts
- +28% vs YTD 2004

Open Interest

- 177,598,354 contracts
- +24% vs year-ago (September 04)

September highlights at CBOE included:

- Options on SPDRs, which were first listed by five exchanges on January 10, 2005, set a new all-time CBOE monthly volume record in September with 1,692,228 contracts traded, surpassing the previous high of 1,645,478 contracts traded in August 2005.
- On Friday, September 16, trading volume in options on the S&P 500 Index (SPX) set a new single day record of 801,974 contracts traded.
- Also on Friday, September 16, total trading volume at CBOE was 3,043,405 contracts, which ranked as the second busiest trading day in CBOE history. Eight of the top ten highest single trading days in CBOE history occurred in 2005.
- Volume in index options was 17.0 million contracts traded, an increase of 64% over September 2004. The top five index options at CBOE during September were: S&P 500 Index (SPX); Nasdaq-100 Index Tracking Stock® (QQQ); Standard & Poor's Depository Receipts®/SPDRs (SPY); S&P 100 Index (OEX); and iShares® Russell 2000® Index Fund (IWM).
- Volume in stock option classes rose 50% over September 2004 as 24.2 million contracts were traded. The top five stock option classes at CBOE during September were: Altria Group, Inc. (MO); Apple Computer, Inc. (AAPL); Time Warner, Inc. (TWX); Google Inc. (GOOG); and General Motors Corporation (GM).
- During September, CBOE Futures Exchange (CFE) volume totaled 6,213 contracts traded. At the end of September, open interest stood at 12,490 contracts.

OneChicago Volume 81% Higher than September 2004

In September 2005, 538,267 security futures contracts traded at OneChicago, 81% higher than September 2004 volume. The average daily volume in September was 25,632 contracts. Year-to-date volume as of the end of September is up 151%. Each single stock futures contract is equivalent to 100 shares of the underlying stock or exchange-traded fund.

For additional information on products or services available at OneChicago, visit <http://www.onechicago.com> or call 312.424.8500. To learn more about single stock futures, members may also contact Mark Esposito, OneChicago Project Coordinator, at 312.424.8527 or (<mailto:SPO@OneChicago.com>).

E-mails to Members

CBOE members who prefer to receive the OPEN INTEREST newsletters via e-mail rather than by U.S. Mail should send their requests, including member name, firm name (if applicable) and desired e-mail address to (<mailto:members@cboe.com>), or contact the CBOE Membership Department directly at 312.786.7449.

Also available: MEMBER E-NEWS, a weekly update for CBOE members that is being distributed via e-mail only and posted on the CBOE Member website. Please be sure to submit your e-mail address to (<mailto:members@cboe.com>), or contact the Membership Department to begin receiving this weekly update.

Please feel free to contact us directly with feedback on any of the topics presented in this newsletter. We welcome your thoughts, ideas and suggestions.



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