



Memorandum No. 2211-07
RC No. SR-Phlx-2007-68
SR-Phlx-2007-65

MEMORANDUM

TO: Members and Member Organizations
Participants and Participant Organizations

FROM: Legal Department

DATE: August 31, 2007

RE: World Currency Options - Proposed Rule Changes

The Exchange has recently filed two proposed rule changes with the Securities and Exchange Commission dealing with U.S. dollar-settled foreign currency options (“World Currency Options” or “WCOs”).

First, the Phlx has filed SR-Phlx-2007-68, a proposed rule change to accommodate the listing and trading of WCOs with certain individually tailored features. These WCOs, known as “Flex Currency Options,” would trade pursuant to amendments proposed to be made to Rule 1079, FLEX¹ Index and Equity Options, and to Options Floor Procedure Advice F-28, Trading FLEX Index and Equity Options. The text of amended Rules 1079 and Options Floor Procedure Advice F-28, is set forth below. The entire proposed rule change is available on the Exchange’s website.

Second, the Exchange has filed SR-Phlx-2007-65 to update the Exchange’s fees applicable to WCOs in order to attract business and streamline the Exchange’s fee schedule. The Exchange proposed to eliminate the \$0.04 per contract comparison charge for transactions in WCOs applicable to customers. The Exchange also proposed to adopt a separate fee schedule for WCOs and to make technical changes to the current Summary of Index Option and U.S. Dollar-Settled Foreign Currency Option Charges fee schedule to update the fee schedule accordingly. The proposed rule change was to take effect upon filing. A copy of the Exchange’s current Summary of Index Option and U.S. Dollar-Settled Foreign Currency Option Charges and the Exchange’s proposed Summary of U.S. Dollar-Settled Foreign Currency Option Charges are attached to this memorandum.

¹ FLEX is a trademark of the Chicago Board Options Exchange, Inc.

Please contact Carla Behnfeldt, Legal Department, at (215) 496-5208, with any questions regarding SR-Phlx-2007-68, the proposed rule change regarding the introduction of FLEX currency options. Contact Bill Briggs, Executive Vice President, at (215) 496-5199 with any questions regarding the amendments to the Exchange's fee schedule.

New language is underlined; deletions are bracketed.

Rule 1079. FLEX Index, [and] Equity and Currency Options

A Requesting Member shall obtain quotes and execute trades in certain non-listed FLEX options at the specialist post of the non-FLEX option on the Exchange. The term "FLEX option" means a FLEX option contract that is traded subject to this Rule. Although FLEX options are generally subject to the rules in this section, to the extent that the provisions of this Rule are inconsistent with other applicable Exchange rules, this Rule takes precedence with respect to FLEX options.

(a) Characteristics:

(1) Underlying [security] interest --

(A) any index upon which options currently trade on the Exchange. The applicable index multiplier shall be the same multiplier, in the case of U.S. dollar-denominated FLEX index options, that applies to non-FLEX index options on the same underlying index; [or]

(B) any security which is options-eligible pursuant to Rule 1009; or

(C) any foreign currency which is options-eligible pursuant to Rule 1009 and which underlies non-FLEX U.S. dollar-settled foreign currency options.

(2) [No Change]

(3) Exercise price --

(A) with respect to FLEX index options, may be specified in terms of a specific index value number, a percentage of the index value calculated as of the open or close of trading on the Exchange on the trade date, or a method for fixing such number; [or]

(B) with respect to FLEX equity options, may be specified in terms of a specific dollar amount rounded to the nearest \$.10 or a percentage of the underlying security rounded to the nearest minimum increment; or

(C) with respect to FLEX currency options other than Japanese yen options, may be specified in terms of a specific dollar amount rounded to the nearest ten thousandth of a dollar (expressed without reference to the first two decimal places), and with respect to FLEX currency options on the Japanese yen, may be specified in terms of a specific dollar amount rounded to the nearest one millionth of a dollar (expressed without reference to the first four decimal places).

(4) Quote format --

(A) in the case of FLEX index options and equity options, a bid and/or offer in the form of a decimal price (e.g. .10 or .25), pursuant to Rule 1034, a specific dollar amount, or a percentage of the underlying equivalent value, in the case of FLEX index options, or security, in the case of FLEX equity options, rounded to the nearest minimum increment; or

(B) in the case of FLEX currency options, in the form of dollars per unit of underlying foreign currency. FLEX currency options shall be quoted and traded in minimum increments of \$.0001 (expressed as .01) for option contracts on the British pound, \$.0001 (expressed as .01) for option contracts on the Swiss franc, \$.0001 (expressed as .01) for option contracts on the Canadian dollar, .0001 (expressed as .01) for option contracts on the Australian dollar, \$.0001 (expressed as .01) for option contracts on the Euro, \$.000001 (expressed as .01) for option contracts on the Japanese yen.

(5) Exercise style --American or European in the case of FLEX index options and FLEX equity options, and European only in the case of FLEX U. S. dollar-settled foreign currency options;

(6) Expiration date --

(A) any month, business day and year within five years for FLEX index options and within two years for FLEX currency options, except that (i) a FLEX option may not expire on any day that falls on or within two business days prior or subsequent to an expiration day for a non-FLEX option on the same underlying index (except quarterly expiring index options) or underlying currency, (ii) the expiration date for FLEX currency options may not fall on a date on which the Federal Reserve Bank of New York is not scheduled to publish a Noon Buying Rate, and

(iii) all FLEX currency options will expire at 10:15 a.m. eastern time on their designated expiration date; or

(B) - (C) No Change.

(7) No Change.

(8) Minimum size --

(A) **Opening** --If there is no open interest in the particular series when an RFQ is submitted, the minimum size of an RFQ is:

(i) \$10 million underlying equivalent value, respecting FLEX market index options, and \$5 million underlying equivalent value respecting FLEX industry index options; [and]

(ii) the lesser of 250 contracts or the number of contracts having \$1 million of underlying equivalent value, with respect to FLEX equity options; and

(iii) 50 contracts in the case of FLEX currency options.

(B) **Opened** --If there is open interest, the minimum size of an RFQ is:

(i) respecting FLEX index options, \$1 million underlying equivalent value, or the remaining size on a closing transaction, whichever is less; [or]

(ii) respecting FLEX equity options, 100 contracts in the case of an opening transaction, or 25 contracts or the remaining size in the case of a closing transaction, whichever is less; or

(iii) respecting FLEX currency options, 25 contracts, or the remaining size on a closing transaction, whichever is less.

(C) **Responsive** --The minimum value size for a responsive quote, other than an assigned ROT or assigned Specialist, is (includes non-assigned ROTs and a non-assigned Specialist):

(i) respecting FLEX index options, \$1 million underlying equivalent value respecting index options, or the remaining size on a closing transaction, whichever is less. However, an assigned ROT and assigned Specialist are required to respond with at least \$10 million underlying equivalent value respecting FLEX market index options, and \$5 million underlying equivalent value respecting

FLEX industry index options, or the size amount requested in the RFQ, whichever is less; [or]

(ii) respecting FLEX equity options, 25 contracts, or the remaining size on a closing transaction, whichever is less. However, an assigned ROT and assigned Specialist are required to respond with at least 250 contracts, or the size amount requested in the RFQ, whichever is less; or

(iii) respecting FLEX currency options, 50 contracts, or the remaining size on a closing transaction, whichever is less. However, an assigned ROT and assigned Specialist are required to respond with at least 250 contracts, or the size amount requested in the RFQ, whichever is less.

(D) No Change.

(9) Settlement

(A) respecting FLEX index options, the settlement value may be specified as the index value reported at the: (i) close (P.M.-settled); (ii) opening (A.M.-settled) of trading on the Exchange, or (iii) as an average over a specified period of time, within parameters established by the Exchange. American style index options exercised prior to the expiration date can only settle based on the closing value on the exercise date. FLEX index options may be designated for settlement in U.S. dollars, British pounds, Canadian dollars, Japanese yen or Swiss francs; [or]

(B) respecting FLEX equity options, exercise settlement shall be by physical delivery of the underlying security pursuant to Rule 1044; or

(C) The settlement value for FLEX options on the Australian dollar, the Euro and the British pound shall be the day's announced Noon Buying Rate, as determined by the Federal Reserve Bank of New York on the expiration date. If the Noon Buying Rate is not announced by 5:00 p.m. (Eastern time ("ET")), the closing settlement value will be the most recently announced Noon Buying Rate, unless the Exchange determines to apply an alternative closing settlement value as a result of extraordinary circumstances. The closing settlement value for FLEX options on the Canadian dollar, the Swiss franc and the Japanese yen shall be an amount equal to one divided by the day's announced Noon Buying Rate, as determined by the Federal Reserve Bank of New York on the expiration date, rounded to the nearest .0001 (except in the case of the Japanese yen where the amount shall be rounded to the nearest .000001). If the Noon Buying Rate is not announced by 5:00 p.m. (Eastern time ("ET")), the closing settlement value will be based upon the most recently announced Noon Buying Rate, unless the Exchange

determines to apply an alternative closing settlement value as a result of extraordinary circumstances. FLEX currency options will cease trading at 9:45 a.m. eastern time on their designated expiration date.

(10) No Change.

(b) Procedure for Quoting and Trading FLEX Options. FLEX options will not be continuously quoted and series are not pre-established. The Exchange's Automated Options Market ("AUTOM") System will not be available for FLEX options. The variable terms of FLEX options shall be established through the process described in this Rule. All transactions must be in compliance with Section 11 of the Securities Exchange Act of 1934 and the rules promulgated thereunder, which may include yielding priority to customer orders.

(1) **Requesting Quotations.** The Requesting Member may initiate a Request-for-Quote by first announcing all of the following contract terms to the trading crowd of the non-FLEX option and then submitting an RFQ ticket to that specialist post: (1) underlying index, [or] security or foreign currency, (2) type, size and crossing intention (3) in the case of FLEX index options and FLEX equity options, exercise style, (4) expiration date, (5) exercise price, and, respecting index options, [(6)] the settlement value and [(7)] the currency. Thereafter, on receipt of an RFQ in proper form, the assigned Specialist or Requesting Member shall cause the terms of the RFQ to be disseminated as an administrative text message through the Options Price Reporting Authority ("OPRA").

(2) - (4) No Change.

(5) **Trading.** A trade in FLEX options cannot be executed until the end of the response time or BBO Improvement Interval. Once the response time or Improvement Interval ends, the Requesting Member is given the first opportunity to trade on the market, by voicing a bid/offer in the trading crowd. The Requesting Member has no obligation to accept any bid or offer for a FLEX option. If the Requesting Member rejects the BBO or the BBO size exceeds the entire size requested, another member may promptly accept such BBO or the unfilled balance of the BBO.

(A) No Change.

(B) FLEX Book --The Specialist in the listed non-FLEX equity, [or] index or U.S. dollar-settled foreign currency option, whether or not assigned in FLEX options, must accept FLEX orders on the FLEX book after completion of the RFQ process. Only customer day limit orders may be placed on the FLEX index, [or FLEX] equity or U.S. dollar-settled foreign currency option book. Booked orders expire at the end of each trading day. The limit price and size must be written on the RFQ ticket

and submitted for dissemination. In order to trade with the book, an executing member must quote the market and announce the trade.

(C) No Change.

(6) - (9) No Change.

(c) No Change.

(d) Position Limits.

(1) No Change.

(2) FLEX equity options shall not be subject to a separate FLEX position limit. Positions in FLEX equity options shall not be taken into account when calculating position limits for non-FLEX equity options, or FLEX or non-FLEX index options.

However, each member or member organization (other than a Specialist or ROT) that maintains a position on the same side of the market in excess of the standard limit under Rule 1001 for non-FLEX equity options of the same class on behalf of its own account or for the account of a customer shall report information on the FLEX equity option position, positions in any related instrument, the purpose or strategy for the position and the collateral used by the account. This report shall be in the form and manner prescribed by the Exchange. In addition, whenever the Exchange determines that a higher margin requirement is necessary in light of the risks associated with a FLEX equity option position in excess of the standard limit for non-FLEX equity options of the same class, the Exchange may consider imposing additional margin upon the account maintaining such under-hedged position, pursuant to its authority under Exchange Rule 722(i)(8). Additionally, it should be noted that the clearing firm carrying the account will be subject to capital charges under SEC Rule 15c3-1 to the extent of any margin deficiency resulting from the higher margin requirement.

(3) Positions in FLEX currency options will be aggregated with positions in non-FLEX U.S. dollar-settled foreign currency option contracts as well as physical delivery foreign currency option contracts for purposes of determining compliance with the position limits established by Rule 1001. Like non-FLEX U.S. dollar-settled foreign currency contracts, (i) one British pound FLEX option contract shall count as one third of a contract, (ii) one Euro FLEX option contract shall count as one sixth of a contract, (iii) one Australian dollar FLEX option contract shall count as one fifth of a contract, (iv) one Canadian dollar FLEX option contract shall count as one fifth of a contract, (v) one Swiss Franc FLEX option contract shall count as one sixth

of a contract, and (vi) one Japanese yen FLEX option contract shall count as one sixth of a contract.

(e) Exercise Limits. In determining compliance with Rules 1002 and 1002A, exercise limits for FLEX options shall be equivalent to position limits established in this Rule. Positions in FLEX options shall not be taken into account when calculating exercise limits for non-FLEX options, except as provided in paragraph (d) above. The minimum exercise size shall be the lesser of \$1 million underlying equivalent value for FLEX index options, and 25 contracts for FLEX equity and currency options, or the remaining size of the position.

(f) FLEX equity and currency options shall be subject to the exercise-by-exception procedure of Rule 805 of the Options Clearing Corporation.

F-28 Trading FLEX Index and Equity Options

A Requesting Member shall obtain quotes and execute trades in non-listed FLEX options at the specialist post of the non-FLEX option on the Exchange, pursuant to Rule 1079. FLEX options will not be continuously quoted and series are not pre-established. The variable terms of FLEX options shall be established through the process described in the Rule. All transactions must be in compliance with Section 11 of the Securities and Exchange Act of 1934 and the Rule promulgated thereunder, which may include yielding priority to customer orders.

(1) Requesting Quotations. The Requesting Member may initiate a Request-for-Quote (RFQ) by first announcing all of the following contract terms to the trading crowd of the non-FLEX option and then submitting an RFQ ticket to the trading crowd of the non-FLEX option and then submitting an RFQ ticket to that specialist post:

(1) underlying index, [or] security or foreign currency,

(2) - (7) No Change.

Thereafter, on receipt of an RFQ in proper form, the Requesting Member shall cause the terms of the RFQ to be disseminated as an administrative text message through the Options Price Reporting Authority ("OPRA").

(2) - (4) No Change.

(5) Trading. A trade in FLEX options cannot be executed until the end of the response time or BBO Improvement Interval. Once the response time or Improvement Interval ends, the Requesting Member is given the first opportunity to trade on the market, by voicing a bid/offer in the trading crowd. The Requesting Member has no obligation to

accept any bid or offer for a FLEX option. If the Requesting Member rejects the BBO or the BBO size exceeds the entire size requested, another member may promptly accept such BBO or the unfilled balance of the BBO.

(A) RFQ Remains Open --Once the BBO is established and no trade has occurred, the RFQ remains open during that trading day, such that a member may re-quote the market with the respect to the open RFQ, as opposed to submitting an additional RFQ. An assigned ROT or assigned Specialist who responded to the open RFQ during the response time or BBO Improvement Interval may immediately join the re-quoted market, thus matching for parity purposes. The Requesting Member is not given the first opportunity to trade on the re-quoted market, nor is the re-quoting member. If a trade occurs, that RFQ is no longer open and a new RFQ is required.

(B) FLEX Book --The Specialist in the listed non-FLEX equity, [or] index or U.S. dollar-settled foreign currency option, whether or not assigned in FLEX options, must accept FLEX orders on the FLEX book after completion of the RFQ process. Only customer day limit orders may be placed on the FLEX index, [or FLEX] equity or U.S. dollar-settled foreign currency option book. Booked orders expire at the end of each trading day. The limit price and size must be written on the RFQ trade ticket and submitted for dissemination. In order to trade with the book, an executing member must quote the market and announce the trade.

(C) Acceptance of a bid/offer creates a binding contract under Exchange rule.

(6) Crossing. Whenever a Requesting Member intends to cross, after the BBO is determined, with or without a BBO Improvement Interval, the Requesting Member, having announced an intention to cross, must bid and offer at or better than the BBO.

(A) No Change.

(B) No Change.

(C) No Change.

For additional provisions governing FLEX options, see Rule 1079.

New text underlined; deleted text bracketed

SUMMARY OF INDEX OPTION [AND U.S. DOLLAR-SETTLED FOREIGN CURRENCY OPTION*] CHARGES (p. 1/1)

OPTION COMPARISON CHARGE (applicable to all trades – except specialist trades)

Registered Option Trader	\$.03 per contract
Firm (Proprietary and Customer Executions) ¹⁰ +	\$.04 per contract

OPTION TRANSACTION CHARGE

Customer Executions	\$.40 per contract [***]
Firm/Proprietary** ¹¹ +	\$.20 per contract
Firm/Proprietary Facilitation+	\$.20 per contract
Registered Option Trader	\$.21 per contract
Specialist	\$.24 per contract

OPTION FLOOR BROKERAGE ASSESSMENT

Monthly Net Floor Brokerage Income	Assessment
\$0 to \$200,000	5% for all amounts up to and including \$200,000
Any amount over \$200,000	No additional charge

Monthly Cap: \$10,000

CANCELLATION FEE

\$1.10 per order for each cancelled AUTOM-delivered order in excess of the number of orders executed on the Exchange by a member organization in a given month. The cancellation fee is not assessed in a month in which fewer than 500 AUTOM-delivered orders are cancelled.

REAL-TIME RISK MANAGEMENT FEE

\$.0025 per contract for firms/members receiving information on a real-time basis

See Appendix A for additional fees.

+ Subject to a maximum fee of \$60,000, except for certain license fees which are assessed per contract side – see \$60,000 “Firm Related” Equity Option and Index Option Cap.

[* U.S. dollar-settled foreign currency options include XDB, XDE, XDN, XDS, XDA and XDC.]

***Non-clearing firm members’ proprietary transactions are eligible for the “firm” rate based upon submission of a PHLX rebate request form with supportive documentation within thirty (30) days of invoice date.*

[*** Subject to a maximum charge of \$4,000 per trade per side for U.S. dollar-settled foreign currency transactions.]

¹⁰ For the purpose of this Summary of Index Option [and FXI Option] Charges, the Firm / Proprietary comparison or transaction charge applies to member organizations for orders for the proprietary account of any member or non-member broker-dealer that derives more than 35% of its annual, gross revenues from commissions and principal transactions with customers. Member organizations will be required to verify this amount to the Exchange by certifying that they have reached this threshold and by submitting a copy of their annual report, which was prepared in accordance with Generally Accepted Accounting Principles (“GAAP”). In the event that a firm has not been in business for one year, the most recent quarterly reports, prepared in accordance with GAAP, will be accepted.

¹¹ See footnote 10.

SUMMARY OF U.S. DOLLAR-SETTLED FOREIGN CURRENCY OPTION* CHARGES

(p. 1/1)

OPTION COMPARISON CHARGE (applicable to all trades – except specialist trades)

<u>Registered Option Trader</u>	<u>\$.03 per contract</u>
<u>Firm (Proprietary [and Customer Executions])¹²</u>	<u>\$.04 per contract</u>
<u>Customer Executions</u>	<u>No Charge</u>

OPTION TRANSACTION CHARGE

<u>Customer Executions</u>	<u>\$.40 per contract ***</u>
<u>Firm/Proprietary**¹³</u>	<u>\$.20 per contract</u>
<u>Firm/Proprietary Facilitation</u>	<u>\$.20 per contract</u>
<u>Registered Option Trader</u>	<u>\$.21 per contract</u>
<u>Specialist</u>	<u>\$.24 per contract</u>

OPTION FLOOR BROKERAGE ASSESSMENT

<u>Monthly Net Floor Brokerage Income</u>	<u>Assessment</u>
<u>\$0 to \$200,000</u>	<u>5% for all amounts up to and including \$200,000</u>
<u>Any amount over \$200,000</u>	<u>No additional charge</u>

Monthly Cap: \$10,000

CANCELLATION FEE

\$1.10 per order for each cancelled AUTOM-delivered order in excess of the number of orders executed on the Exchange by a member organization in a given month. The cancellation fee is not assessed in a month in which fewer than 500 AUTOM-delivered orders are cancelled.

REAL-TIME RISK MANAGEMENT FEE

\$.0025 per contract for firms/members receiving information on a real-time basis

See Appendix A for additional fees.

* U.S. dollar-settled foreign currency options include XDB, XDE, XDN, XDS, XDA and XDC.

**Non-clearing firm members' proprietary transactions are eligible for the "firm" rate based upon submission of a PHLX rebate request form with supportive documentation within thirty (30) days of invoice date.

*** Subject to a maximum charge of \$4,000 per trade per side.

¹² For the purpose of this Summary of U.S. Dollar-Settled Foreign Currency Option Charges, the Firm / Proprietary comparison or transaction charge applies to member organizations for orders for the proprietary account of any member or non-member broker-dealer that derives more than 35% of its annual, gross revenues from commissions and principal transactions with customers. Member organizations will be required to verify this amount to the Exchange by certifying that they have reached this threshold and by submitting a copy of their annual report, which was prepared in accordance with Generally Accepted Accounting Principles ("GAAP"). In the event that a firm has not been in business for one year, the most recent quarterly reports, prepared in accordance with GAAP, will be accepted.

¹³ See footnote 12.

SUMMARY OF PHYSICAL DELIVERY CURRENCY OPTION CHARGES**

OPTION COMPARISON CHARGE (applicable to all trades – except specialist trades)

Firm (Proprietary and Customer Executions) and Registered Option Trader	\$.05 per contract
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OPTION TRANSACTION CHARGE*

Customer Executions	\$.28 per contract
Firm (Proprietary Executions)	\$.23 per contract
Registered Option Trader and Specialist	\$.14 per contract

OPTION FLOOR BROKERAGE ASSESSMENT

5% of net floor brokerage income.

FLOOR BROKERAGE TRANSACTION FEE

\$.05 per contract, for floor brokers executing transactions for their own member firm.

**Volume Discount for Physical Delivery Currency Options
Transaction Charge Activity**

*Volume discounts will be available based upon total Customer Executions and Firm Proprietary activity per billing period. The discount will apply to the number of contracts executed within the specified ranged (i.e., member XYZ executed 340,000 contracts for his Customer and Firm in a billing period. All contracts will be billed at the normal rates, however, rebates of \$.10 will be given for 140,000 contracts.)

Number of Contracts	Reduction
200,001 – 400,000	\$.10 per contract
400,001 or more	\$.20 per contract

See Appendix A for additional fees.

** U.S. dollar-settled foreign currency options are subject to a separate fee schedule. See Summary of [Index Option and] U.S. Dollar-Settled Foreign Currency Option Charges.