



In 2003, CBOE redefined
how options are traded.
Here's how we did it.

Chicago Board Options Exchange Annual Report 2003



CBOE*direct*® HyTS™

On June 12, 2003, the Chicago Board Options Exchange® (CBOE®) introduced CBOE*direct* HyTS, a revolutionary hybrid trading system. CBOE is the first exchange to truly marry the speed and efficiency of screen-based trading with the liquidity and price discovery of a competitive, open outcry marketplace.

By launching CBOE*direct* HyTS, CBOE has created a unique trading model, unlike that of any other options exchange.

The robust technology encompassed in CBOE*direct* HyTS combines the best features of screen-based trading and floor-based markets. By crafting a multi-faceted trading environment that combines the key elements of each, CBOE now offers customers and market makers a groundbreaking “best of both worlds” options marketplace.

ALL 5.00 OPEN/CUST UNCVRD A QFO

Strike: 25.00 C/P: CALL Price: 5.00 Price Type: WITH/Stop
 Acct Name: QFO Duration: DAY Exchange: CBOE SubExc:
 CMTA: Give Up: Send Clear Last

SELL 1,
OF

3 NBBO CBOE AMEX ISE PCX PHLX GO

BIDSIZE	BID	ASK	ASKSIZE	EXPIR_DATE	STRIKES	BIDSIZE	BID	ASK	ASKSIZE
7	30.05	30.06	31						
1110	5.00	5.10	400	18 OCT 2003	25.00	0	0.00	0.05	25
112	2.70	2.70	400	18 OCT 2003	27.50	460	0.10	0.15	3127
1	0.75	0.80	9681	18 OCT 2003	30.00	1449	0.65	0.70	520
5	0.10	0.15	5007	18 OCT 2003	32.50	585	2.50	2.55	132
0	0.00	0.05	836	18 OCT 2003	35.00	785	4.90	5.00	485
0	0.00	0.05	775	18 OCT 2003	37.50	625	7.40	7.50	675
1708	5.10	5.30	1505	22 NOV 2003	25.00	1363	0.10	0.15	1958
1692	2.90	3.00	727	22 NOV 2003	27.50	551	0.35	0.40	1836
310	1.20	1.25	482	22 NOV 2003	30.00	500	1.10	1.15	855
2068	0.30	0.35	130	22 NOV 2003	32.50	685	2.70	2.80	1493
678	0.05	0.10	1552	22 NOV 2003	35.00	1439	4.90	5.10	1452
0	0.00	0.05	995	22 NOV 2003	37.50	544	7.40	7.50	874

Expiry Date	Strike Price	Call/Put	Status	Bid Size	Bid
				1302	17.60
60 OCT-03	10.00	Call	OUTSTANDING	50	8.60
70 NOV-03	37.50	Call	OUTSTANDING	50	8.50
60 OCT-03	37.50	Call	FILLED	50	8.60
70 NOV-03	37.50	Call	FILLED	1189	5.40
60 OCT-03	85.00	Call	FILLED	1189	5.40
50 OCT-03	85.00	Call	FILLED	50	8.50
40 OCT-03	37.50	Call	FILLED	60	10.20



CBOE HyTS TERMINAL

CBOE partnered with Belzberg Technologies, Inc. to co-brand the CBOE Hybrid Trading System (HyTS) Terminal, a universal access, multifunctional, trading solution workstation. The HyTS Terminal serves as an order management tool, and provides CBOE customers with immediate point-and-click access to CBOE markets.

Increased Efficiency and Speed

CBOEdirect HyTS offers powerful new features which provide customers with efficiency, speed and market quality unparalleled in the options industry.

Individual Market Makers' Streaming Quotes

CBOEdirect HyTS allows in-crowd market makers to input real-time, streaming quotes into CBOEdirect, the system's trade engine. CBOE disseminates the resulting, composite best bid and offer, including the total size available at the best price. Customers benefit from tight, guaranteed markets that can be immediately accessed electronically.

The ability for market makers to stream live quotes, to post "quotes with size" and to more quickly execute orders allows CBOE market makers to better showcase the quality of markets found at CBOE.

Point-and-Click Execution for Customers

The HyTS Terminal is a universal access, multifunctional workstation that provides electronic access and order routing to U.S. options exchanges, as well as complete access to market data, real-time quotes and order management—all on a single screen. Terminal users may also obtain similar functionality for futures and stock exchanges. Additionally, the CBOE HyTS Terminal serves as a portal into the CBOE Hybrid Trading System.

CBOE MAKES MARKETS

CBOE's trading floor houses the most traders and the greatest pool of liquidity of any options exchange. Within this highly-liquid marketplace, opportunities for price improvement are plentiful.

Potential for Price Improvement

CBOE believes in the inherent value of the face-to-face, open outcry marketplace and also recognizes the beneficial features of electronic trading. The Hybrid Trading System, CBOE*direct* HyTS, is more than just the sum of its parts. The system offers customers synergistic benefits by uniting the advantages of both types of marketplaces. With nearly 1,400 well-capitalized market makers, CBOE features more options traders in one place than any other exchange. This vast pool of expertise and liquidity creates deep markets where abundant opportunities for price discovery allow for price improvement.

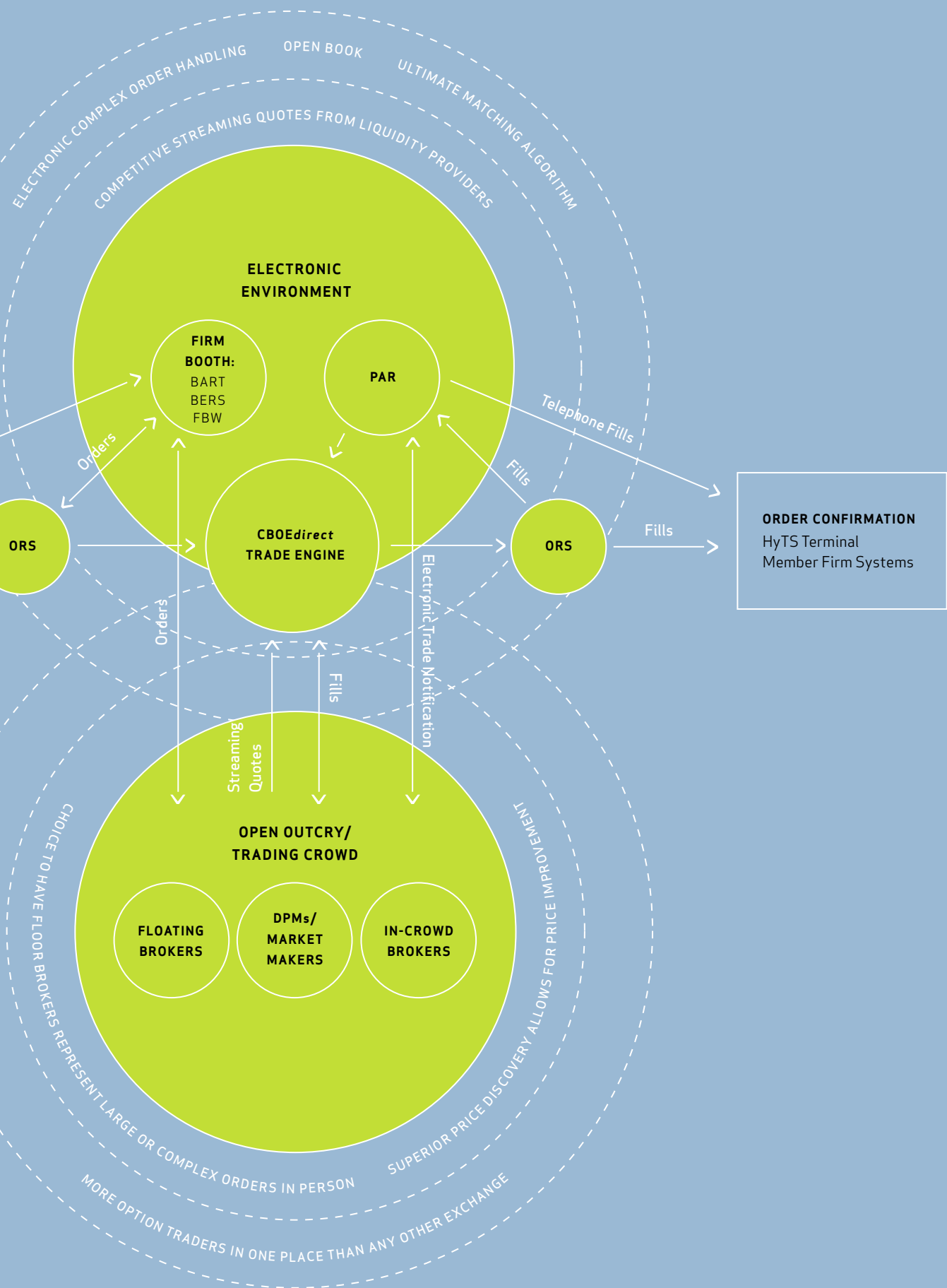
Open Access to the Limit Order Book

Because individual market makers now have electronic quoting capability, CBOE, for the first time, allows for the "opening of the Limit Order Book" to customer, firm and Broker/Dealer orders. Orders entered in the Book are afforded priority according to price and are eligible for electronic matching. Customer priority is retained.



KEY

BART—Booth Automated Routing Terminal
BERS—Booth Entry Routing System
DPM—Designated Primary Market Maker
FBW—Floor Broker Workstation
ORS—Order Routing System
PAR—Public Automated Routing System







CBOE TRADING FLOOR

CBOE's market makers compete aggressively, producing tight, deep markets.

Enhanced Access to CBOE's Markets

An open auction market combined with the benefits of electronic trading provides customers with easy access to CBOE's deep, transparent markets. Floor brokers can walk into a trading crowd and request markets on their customers' behalf.

Ultimate Matching Algorithm

The CBOE *direct* HyTS ultimate matching algorithm retains the priority to public customer orders that CBOE has always afforded. Additionally, participation rights are awarded to other market participants based on a formula that rewards deep liquidity, as well as competitive pricing.



Order Type	Qty	CBEX	CBEM	Time
Buy	100	100	100	10:00
Buy	200	200	200	10:01
Buy	300	300	300	10:02
Buy	400	400	400	10:03
Buy	500	500	500	10:04
Buy	600	600	600	10:05
Buy	700	700	700	10:06
Buy	800	800	800	10:07
Buy	900	900	900	10:08
Buy	1000	1000	1000	10:09

Fiscal Year Events and Highlights

JULY 1, 2002–JUNE 30, 2003

JULY 19, 2002

CBOE launches Large Order Utility (LOU) to allow customers to instantaneously secure CBOE's disseminated quote for large size orders that were not eligible for electronic execution.

JULY 23, 2002

The CBOE Volatility Index® (VIX®) closes at 50.48, marking the first time VIX has closed above 50 since November 11, 1987.

JULY 31, 2002

New records set for monthly volume in options on the S&P 500® Index (SPX™)—3,859,734 contracts and options on the Dow Jones Industrial Average™ (DJX)—1,485,582 contracts.

SEPTEMBER 30, 2002

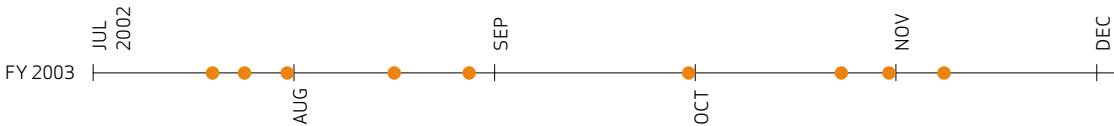
Volume in options on DIAMONDS® (DIA) increases by 37%. Introduced on May 20, 2002, options on DIA is one of the most successful new product launches in CBOE history.

NOVEMBER 8, 2002

OneChicago, LLC, a joint venture exchange between CBOE, CBOT and CME, launches trading of securities futures.

DECEMBER 31, 2002

For the calendar year, CBOE trades a total of 267,616,496 contracts, making 2002 the fourth busiest year in CBOE history.



AUGUST 15, 2002

CBOE membership votes overwhelmingly in favor of adopting governance amendments intended to increase the role of public directors on the Exchange's Board of Directors.

AUGUST 26, 2002

In a partnership with Chicago Public Schools, CBOE "adopts" John B. Drake Elementary School. CBOE members and staff, as part of the Working In The Schools (WITS) Program, tutor students throughout the school year.

OCTOBER 21, 2002

CBOE and Chicago Public Schools (CPS) hold a joint press conference to announce CPS' new "Futures Exchange" corporate partnership program.



OCTOBER 31, 2002

New record for monthly volume in options on QQQ set with a total of 2,508,407 contracts traded.

APRIL 26, 2003

CBOE marks its 30th anniversary and the launch of listed options. To commemorate the occasion, Mayor Richard M. Daley visited the Exchange on April 22, 2003 and rang the opening bell during a special ceremony.



FEBRUARY 27, 2003

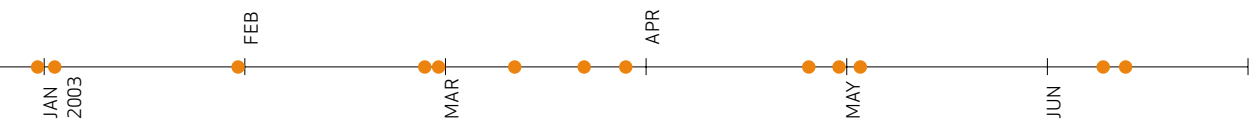
The CBOE Hybrid Trading System (HyTS) Terminal, a universal access, multifunctional, trading solution workstation, is introduced.

FEBRUARY 28, 2003

For the third consecutive month, CBOE has the largest total volume of all U.S. options exchanges in options on QQQ.

APRIL 30, 2003

The end of April marks one consecutive year in which index options' total monthly volume exceeds the previous year's levels.



JANUARY 2, 2003

Thirty Chicago high school students spend a week at CBOE as part of the annual Diversity Representation, Education and Mentoring (DREAM) program. The DREAM program, now in its fifth year, is an ongoing effort at CBOE to expose minority youth to the financial industry.

JANUARY 31, 2003

CBOE, along with the other U.S. options exchanges, participates in the launch of an intermarket linkage system.

MARCH 11, 2003

The 20th anniversary of index options trading at CBOE is celebrated. Standard & Poor's® executives rang the opening bell in recognition of the milestone.



MARCH 21, 2003

CBOE experiences one of the busiest trading days in its history as 2,003,524 contracts trade.

MARCH 27, 2003

CBOE S&P 500® BuyWrite Index (BXM™) is licensed to Rampart Investment Management, Inc. for a new investment vehicle to be based on the BXM.

MAY 2, 2003

Myron Scholes, 1997 Nobel Laureate in Economics for development of the Black-Scholes options pricing model, tours the CBOE trading floor and is honored at a 30th anniversary luncheon.



JUNE 9, 2003

CBOE activates application with the Commodity Futures Trading Commission to become a registered futures exchange.

JUNE 12, 2003

CBOE launches its new hybrid trading system, CBOE*direct* HyTS.

Each chapter in CBOE's remarkable history is chronicled by the Exchange's ability to innovate and elevate the standard for industry leadership. CBOE *direct* HyTS is in keeping with that long-standing tradition.



William J. Brodsky



Mark F. Duffy



Edward J. Joyce

Letter from the Office of the Chairman

Mounting competitive pressures, a prolonged bear market in equities and shaken investor confidence combined to make Fiscal Year 2003 extremely demanding for the Chicago Board Options Exchange (CBOE) and its members. In the midst of this very challenging year, CBOE celebrated 30 years of options trading and retained its position as the world's largest options exchange based on total volume. In addition, CBOE launched a major strategic and technological initiative designed to extend the Exchange's leadership position into the future.

CBOE remained the leading exchange in overall options volume in FY 2003, garnering a 33% market share. Nearly 270 million contracts were traded, with an average daily volume of 1,071,305 contracts. Total equity options volume in FY 2003 was 159.3 million contracts. Despite a decrease of 2% when compared to FY 2002, the volume in FY 2003 represented the fourth highest fiscal year total in the Exchange's history.

Impressive growth in CBOE's options on benchmark indexes drove exchange volume in FY 2003, including: S&P 500[®] Index options (SPX), up 45%; S&P 100[®] Index options (OEX[®]), up 51%; options on the Dow Jones Industrial AverageSM (DJX), up 31%; Russell 2000 Index[®] options (RUT), up 71%; and options on the Nasdaq-100[®] Index Tracking Stock (QQQ), up 21%.

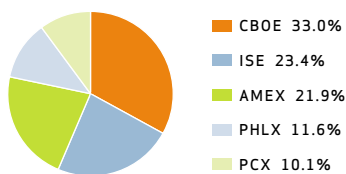
Total index options volume was 110.6 million contracts traded, an increase of 43% over FY 2002. From May 2002 through June 2003, index options volume at CBOE posted consecutive gains each month over the same month's year-ago level.

CBOE remains committed to innovations and strategies that will foster the future growth of the Exchange. The most significant of those in 2003, as we've noted in the previous pages, was the launch of CBOE*direct* HyTS, our new hybrid trading system.

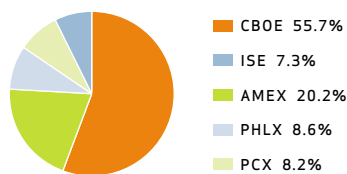
CBOE*direct* HyTS was designed to capitalize on CBOE's greatest assets—the largest pool of market-making professionals in the options industry and the deep, liquid markets found in

TOTAL OPTIONS MARKET SHARE

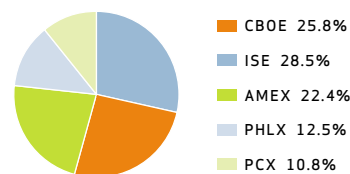
FISCAL YEAR 2003

**INDEX OPTIONS MARKET SHARE**

FISCAL YEAR 2003

**EQUITY OPTIONS MARKET SHARE**

FISCAL YEAR 2003



our trading crowds. Those assets, combined with the Exchange's ongoing commitment to enhance the trading process through technological innovation, led to the creation of this new business model.

CBOE *direct* HyTS provides market makers with cutting-edge technology to display their markets in order to compete more aggressively with both screen- and floor-based competitors. We believe that CBOE *direct* HyTS, with its unique marriage of traders and technology, has the capability to revolutionize the industry and change the way options are traded.

The conversion to Hybrid is ongoing as individual classes continue to be phased-in throughout the remainder of 2003. By year-end, the top classes, which account for approximately 90% of the national volume in equity options, will be traded on the Hybrid.

The emergence of CBOE *direct* HyTS onto the competitive landscape significantly alters the options marketplace. Additionally, because CBOE both built and owns the highly-flexible technology used to power CBOE *direct* HyTS, it can be easily adapted to future customer needs.

It is fitting, in our 30th anniversary year, for CBOE to punctuate its great tradition of leadership in customer service and technological innovation with the unveiling of CBOE *direct* HyTS, the trading model of tomorrow. Through the continued dedication and skilled efforts of our members and staff, we look forward to an even more productive and successful future.

Sincerely,

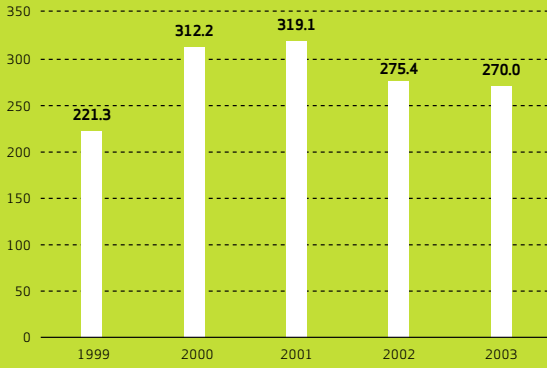
William J. Brodsky
Chairman and CEO

Mark F. Duffy
Vice Chairman

Edward J. Joyce
President and COO

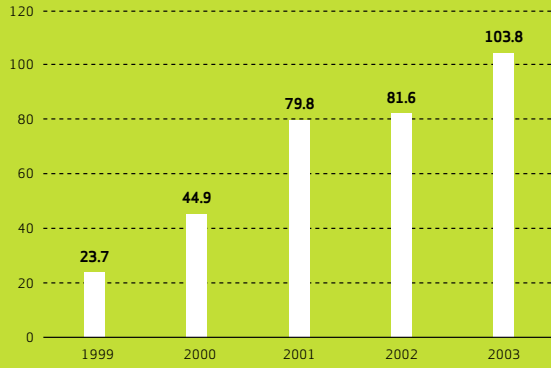
CBOE TOTAL VOLUME

IN MILLIONS, BY FISCAL YEAR



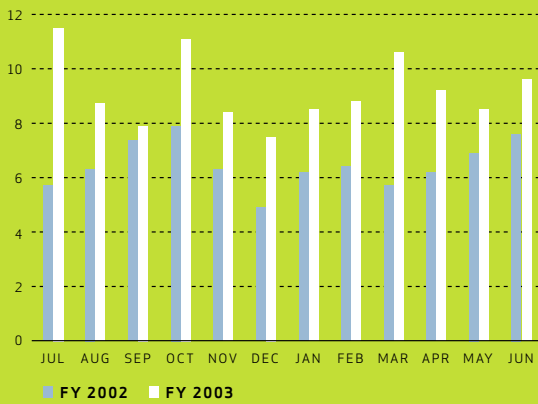
CBOE OPEN INTEREST

IN MILLIONS, BY FISCAL YEAR



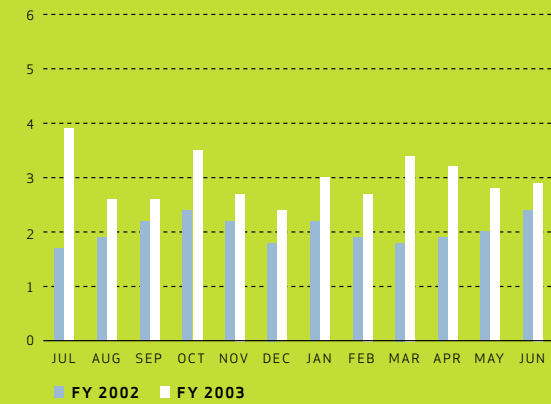
CBOE TOTAL INDEX VOLUME

IN MILLIONS, BY FISCAL YEAR



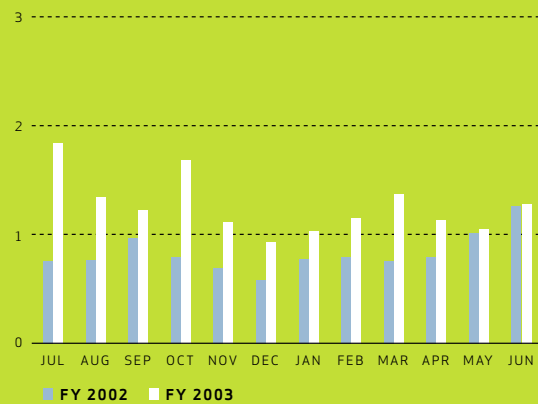
S&P 500 (SPX) VOLUME

IN MILLIONS, BY FISCAL YEAR



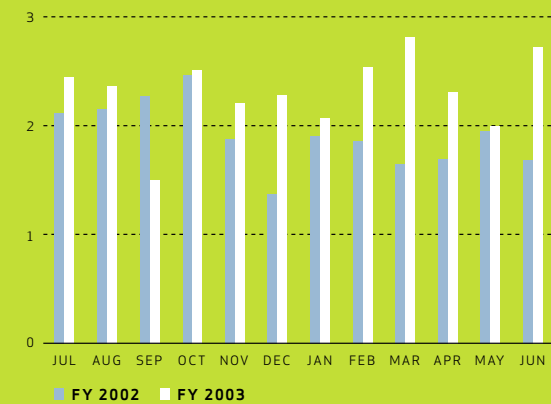
S&P 100 (OEX) VOLUME

IN MILLIONS, BY FISCAL YEAR



NASDAQ-100 INDEX TRACKING STOCK (QQQ) VOLUME

IN MILLIONS, BY FISCAL YEAR



CONSOLIDATED STATEMENTS OF INCOME AND RETAINED EARNINGS

Chicago Board Options Exchange, Incorporated and Subsidiaries
For the Years Ended June 30, 2003 and 2002 (in thousands)

	2003	2002
Revenues:		
Transaction fees	\$ 104,827	\$ 89,436
Other member fees	26,642	24,641
Options Price Reporting Authority Income	15,614	18,884
Regulatory fees	10,800	11,231
Interest	368	459
Equity in income of CSE	1,867	141
Other	3,674	4,031
Total Revenues	163,792	148,823
Expenses:		
Employee costs	64,094	63,920
Depreciation and amortization	29,252	29,709
Data processing	17,771	17,492
Outside services	11,794	13,458
Royalty fees	11,028	8,989
Travel and promotional expenses	4,853	5,428
Facilities costs	4,240	4,351
Equity in loss of OneChicago	4,165	1,483
Other	2,583	2,195
Communications	621	727
Severance expense		4,499
Total Expenses	150,401	152,251
Income (Loss) Before Income Taxes	13,391	(3,428)
Provision (Benefit) for Income Taxes:		
Current	5,201	(3,102)
Deferred	798	5,294
Total Provision for Income Taxes	5,999	2,192
Net Income (Loss)	7,392	(5,620)
Retained Earnings at Beginning of Year	103,670	109,290
Retained Earnings at End of Year	\$ 111,062	\$ 103,670

CONSOLIDATED BALANCE SHEETS

Chicago Board Options Exchange, Incorporated and Subsidiaries
June 30, 2003 and 2002 (in thousands)

	2003	2002
Assets		
Current Assets:		
Cash and cash equivalents	\$ 20,558	\$ 6,861
Accounts receivable	18,473	17,207
Income taxes receivable	1,519	4,361
Prepaid medical benefits	1,777	1,028
Other prepaid expenses	4,464	4,406
Other current assets	912	673
Total Current Assets	47,703	34,536
Investments in Affiliates	14,976	13,861
Land	4,914	4,914
Property and Equipment:		
Building	57,609	57,609
Furniture and equipment	110,006	170,152
Less accumulated depreciation and amortization	(104,577)	(157,621)
Total Property and Equipment—Net	63,038	70,140
Other Assets:		
Goodwill	1,388	1,388
Software development work in progress	5,440	6,455
Data processing software and other assets (less accumulated amortization— 2003, \$31,854; 2002, \$28,334)	38,325	34,412
Total Other Assets—Net	45,153	42,255
Total	\$ 175,784	\$ 165,706

See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS (CONTINUED)

For the Years Ended June 30, 2003 and 2002 (in thousands)	2003	2002
Liabilities and Members' Equity		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 15,173	\$ 14,436
Marketing fee payable	687	1,079
Unearned income	1,500	1,250
Membership transfer deposits	200	657
Total Current Liabilities	17,560	17,422
Long-term Liabilities:		
Unearned income	2,000	250
Deferred income taxes	24,228	23,430
Total Long-term Liabilities	26,228	23,680
Total Liabilities	43,788	41,102
Members' Equity		
Memberships	20,934	20,934
Retained earnings	111,062	103,670
Total Members' Equity	131,996	124,604
Total	\$ 175,784	\$ 165,706

CONSOLIDATED STATEMENTS OF CASH FLOWS

Chicago Board Options Exchange, Incorporated and Subsidiaries For the Years Ended June 30, 2003 and 2002 (in thousands)	2003	2002
Cash Flows from Operating Activities:		
Net Income (Loss)	\$ 7,392	\$ (5,620)
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	29,252	29,709
Long-term settlement obligations		(5,333)
Deferred income taxes	798	5,294
Equity in income of CSE	(1,867)	(141)
Equity in loss of OneChicago	4,165	1,483
Gain on disposition of property		(277)
Changes in assets and liabilities:		
Accounts receivable	(1,266)	5,005
Income taxes	2,842	(1,048)
Prepaid medical benefits	(749)	(101)
Other prepaid expenses	(58)	(220)
Other current assets	(239)	(119)
Accounts payable and accrued expenses	737	793
Marketing fee payable	(392)	(8,095)
Unearned income	2,000	1,396
Membership transfer deposits	(457)	657
Other deposits		(416)
Net Cash Flows from Operating Activities	42,158	22,967
Cash Flows from Investing Activities:		
Capital and other assets expenditures	(25,047)	(21,871)
OneChicago investment	(3,414)	(4,388)
Proceeds from disposition of property		413
Net Cash Flows from Investing Activities	(28,461)	(25,846)
Net Increase (Decrease) in Cash and Cash Equivalents	13,697	(2,879)
Cash and Cash Equivalents at Beginning of Year	6,861	9,740
Cash and Cash Equivalents at End of Year	\$ 20,558	\$ 6,861

Supplemental Disclosure of Cash Flow Information

Cash paid for income taxes	\$ 3,875	\$ 0
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See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Chicago Board Options Exchange, Incorporated and Subsidiaries
For the Years Ended June 30, 2003 and 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business – The Chicago Board Options Exchange (“the Exchange”) is a registered securities exchange, subject to oversight by the Securities and Exchange Commission. The Exchange’s principal business is providing a marketplace for trading equity and index options.

Basis of Presentation – The consolidated financial statements include the accounts and results of operations of Chicago Board Options Exchange, Incorporated, and its wholly owned subsidiaries, Chicago Options Exchange Building Corporation and, beginning in 2002, CBOE, LLC. Inter-company balances and transactions are eliminated.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts of assets and liabilities, disclosure of contingent assets and liabilities, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition – Transaction Fees revenue is considered earned upon the execution of the trade and is recognized on a trade date basis. Other Member Fees revenue is recognized during the period the service is provided. OPRA income is allocated based upon the market share of the OPRA members and is received quarterly. Estimates of OPRA’s quarterly revenue are made and accrued each month. Regulatory Fees are predominately received in the month of January and are amortized monthly to coincide with the services rendered during the fiscal year.

Cash and Cash Equivalents – Cash and cash equivalents include highly liquid investments with maturities of three months or less from the date of purchase.

Investments – All investments are classified as available-for-sale and are reported at cost which approximates their fair value in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 115, “Accounting for Certain Investments in Debt and Equity Securities.”

Accounts Receivable – Accounts receivable consist primarily of transaction, marketing and other fees receivable from The Options Clearing Corporation (“OCC”), and the Exchange’s share of distributable revenue receivable from The Options Price Reporting Authority (“OPRA”).

Investments in Affiliates – Investments in affiliates represent investments in OCC, OneChicago, (“ONE”) and The Cincinnati Stock Exchange (“CSE”). The investment in OCC (20% of its outstanding stock) is carried at cost because of the Exchange’s inability to exercise significant influence. The Exchange accounts for the investment in CSE (68% of its total certificates of proprietary membership) under the equity method due to the lack of effective control over the operating and financing activities of CSE. During 2002 the Exchange made an initial investment in ONE (approximately 40% of its outstanding stock). This investment is accounted for under the equity method.

Property and Equipment – Property and equipment are carried at cost. Depreciation on building, furniture and equipment is provided on the straight-line method. Estimated useful lives are 40 years for the building and five to ten years for furniture and equipment. Leasehold improvements are amortized over the lesser of their estimated useful lives or the remaining term of the applicable leases.

Data Processing Software – Data processing software is carried at cost and amortized over five to seven years using the straight-line method commencing with the date the software is put in service.

Goodwill – SFAS No. 142, “Goodwill and Other Intangible Assets,” requires that goodwill and separately identified intangible assets with indefinite lives no longer be amortized but reviewed annually (or more frequently if impairment indicators arise) for impairment. Separately identified intangible assets not deemed to have indefinite lives will continue to be amortized over their useful lives. Upon review by Exchange management, it was determined there has been no impairment of the intangible assets included in the financial statements. Goodwill is amortized over fifteen years for income tax purposes.

Income Taxes – Income taxes are determined using the liability method, under which deferred tax assets and liabilities are recorded based on differences between the financial accounting and tax bases of assets and liabilities.

Unearned Income – Unearned income represents amounts received by the Exchange for which the contracted services have not been provided.

Fair Value of Financial Instruments – SFAS No. 107, “Disclosures About Fair Value of Financial Instruments,” requires disclosure of the fair value of certain financial instruments. The carrying values of financial instruments included in assets and liabilities are reasonable estimates of their fair value.

Reclassifications – Certain prior year amounts have been reclassified to conform with the current year presentation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Recent Accounting Pronouncement – In November 2002, the FASB issued FASB Interpretation Number 45 (FIN), “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others,” effective June 30, 2003. FIN45 is an interpretation of FASB Statements No. 5, 57 and 107 and a rescission of FASB Interpretation No. 34. This interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The Exchange has determined the impact of adopting FIN45 to be immaterial.

In January 2003, the FASB issued FIN46, “Consolidation of Variable Interest Entities,” effective July 1, 2003. This interpretation of Accounting Research Bulletin No. 51, Consolidated Financial Statements, addresses consolidation by business enterprises of variable interest entities that meet one or all of certain preset characteristics. The Exchange has determined the impact of adopting FIN46 to be immaterial.

2. INVESTMENT IN THE CININNATI STOCK EXCHANGE

The investment in CSE is accounted for using the equity method. Condensed financial statements of the CSE as of and for the years ended June 30, 2003 and 2002 are as follows (in thousands):

	2003	2002
Balance Sheets		
Cash and cash equivalents	\$ 15,734	\$ 4,955
Securities available-for-sale	525	2,090
Other current assets	12,449	9,007
Long-term securities available-for-sale	11,508	8,540
Other long-term assets	4,862	5,661
Total assets	45,078	30,253
Current liabilities	26,888	14,543
Deferred income taxes	982	1,252
Members’ equity	17,208	14,458
Total liabilities and members’ equity	45,078	30,253
The Exchange’s share of members’ equity	\$ 12,175	\$ 10,308

	2003	2002
Statement of Operations		
Transaction revenue	\$ 4,160	\$ 2,971
Other revenue	14,885	5,011
Total revenues	19,045	7,982
Employee costs	2,342	2,622
Other expenses	13,948	5,152
Total expenses	16,290	7,774
Net income	2,755	208
The Exchange’s equity in net income	\$ 1,867	\$ 141

3. RELATED PARTIES

The Exchange’s equity in the net assets of OCC exceeded its cost by approximately \$8.3 million and \$8.6 million at June 30, 2003 and 2002, respectively. The Exchange collected transaction and other fees of \$129.0 million and \$123.4 million for the years ended June 30, 2003 and 2002, respectively, by drawing on accounts of the Exchange’s members held at OCC. For the years ended June 30, 2003 and 2002, respectively, the amount collected includes \$8.2 million and \$19.3 million of marketing fees (see note 8). The Exchange had a receivable due from OCC of \$11.9 million and \$11.1 million at June 30, 2003 and 2002, respectively.

The Exchange incurred reimbursable expenses on behalf of CSE, for expenses such as employee costs, computer equipment and office space of \$3.7 million and \$2.6 million for the years ended June 30, 2003 and 2002, respectively. The Exchange had a receivable from CSE of \$890 thousand and \$485 thousand at June 30, 2003 and 2002, respectively.

OPRA is a committee administered jointly by the five options exchanges and is authorized by the Securities and Exchange Commission to provide consolidated options information. This information is provided by the exchanges and is sold to outside news services and customers. OPRA’s operating income is distributed among the exchanges based on their relative volume of total transactions. Operating income distributed to the Exchange was \$15.6 million and \$18.9 million for the years ended June 30, 2003 and 2002, respectively. The Exchange had a receivable from OPRA of \$4.1 million and \$4.5 million at June 30, 2003 and 2002, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Exchange, the Chicago Mercantile Exchange and the Chicago Board of Trade are partners in ONE, a joint venture created to trade single stock futures. Certain ONE employees also have minority interests in the joint venture. ONE is a for-profit entity with its own management and board of directors, and is separately organized as a regulated exchange. The Exchange contributed \$3.4 million and \$4.4 million in capital to ONE during the years ended June 30, 2003 and 2002, respectively. The Exchange had a receivable due from ONE of \$1.0 million and \$391 thousand at June 30, 2003 and June 30, 2002, respectively.

4. LEASES

The Exchange leases office space with lease terms of six months and five years. Rent expenses related to leases during FY03 and FY02 were \$735 thousand and \$1.8 million, respectively. Future minimum lease payments under these noncancelable operating leases are as follows at June 30, 2003 (in thousands):

2004	\$	758
2005		776
2006		736
2007		112
2008		66
Total	\$	2,448

5. EMPLOYEE BENEFITS

Eligible employees participate in the Chicago Board Options Exchange SMART Plan (the "SMART Plan"). The SMART Plan is a defined contribution plan, which is qualified under Internal Revenue Code Section 401(k). The Exchange contributed \$3.5 million and \$3.4 million to the SMART Plan for the years ended June 30, 2003 and 2002, respectively.

Eligible employees participate in the Supplemental Employee Retirement Plan (the "SERP Plan"). The SERP Plan is a defined contribution plan that is nonqualified by Internal Revenue Code regulations. The Exchange contributed \$788 thousand and \$579 thousand to the SERP Plan for the years ended June 30, 2003 and 2002, respectively.

The Exchange also has a Voluntary Employees' Beneficiary Association ("VEBA"). The VEBA is a trust, qualifying under Internal Revenue Code Section 501(c)(9), created to provide certain medical, dental, severance, and short-term disability benefits to employees of the Exchange. Contributions to the trust are based on reserve levels established by Section 419(a) of the Internal Revenue Code. During fiscal 2003 and 2002, the Exchange contributed \$2.7 million and \$1.8 million, respectively, to the trust.

6. COMMITMENTS

In September 2000, the Exchange reached an agreement in principle to settle a consolidated civil class action lawsuit filed against the Exchange and other U.S. options exchanges and certain market maker firms. The Exchange agreed to pay \$16.0 million in three equal installments on or before October 16, 2000, July 1, 2001, and July 1, 2002. All payments have been made, and are being held in escrow pending approval of the settlement agreement by the U.S. District Court for the Southern District of New York.

7. INCOME TAXES

A reconciliation of the statutory federal income tax rate to the effective income tax rate, for the years ended June 30, 2003 and 2002, is as follows:

	2003	2002
Statutory federal income tax rate	35.0%	34.0%
State income tax rate, net of federal income tax effect	4.7	4.7
Equity in income of CSE	0.0	(98.0)
Other permanent differences, net	5.1	(4.6)
Effective income tax rate	44.8%	(63.9%)

At June 30, 2003 and 2002, the net deferred income tax liability approximated (in thousands):

	2003	2002
Deferred tax assets	\$ 11,369	\$ 9,261
Deferred tax liabilities	35,597	32,691
Net deferred income tax liability	\$ 24,228	\$ 23,430

Deferred income taxes arise principally from temporary differences relating to the use of accelerated depreciation methods for income tax purposes, capitalization of software, licensing fees, funding of the VEBA trust, and beginning in 2002, undistributed earnings from the Exchange's investment in CSE.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Due to CBOE's refined strategy of possibly selling the CSE investment, management now believes that CBOE's expected realization of its investment in CSE will most likely be through the sale of its investment in CSE, which will trigger a capital gain at CBOE's normal tax rate. Therefore, beginning in 2002, CBOE has modified the deferred tax liability rate to match the changed disposition strategy.

8. MARKETING FEE

Even though the original Exchange-sponsored marketing fee was suspended effective August 1, 2001, the Exchange continued to facilitate the collection of payment for order flow funds from DPMs and distributed funds to order provider firms, as directed by the DPMs each month. Effective June 2, 2003, the Exchange re-instituted a new marketing fee program. As of June 30, 2003 and 2002 amounts held by CBOE on behalf of others included accounts receivable balances of \$687 thousand and \$1.1 million, respectively.

9. LITIGATION

A former member of the Exchange has requested compensation for losses it alleges to have incurred because the Exchange terminated that member's appointment as a designated primary market maker. The former member states that it has suffered substantial lost profits and that it lost the opportunity to sell its business at a multiple of those profits. The Exchange has informed the former member that specific Exchange rules preclude claims of this type from being made against the Exchange. The former member has initiated no lawsuit or other formal legal proceeding.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Members of the Chicago Board Options Exchange, Incorporated:

We have audited the accompanying consolidated balance sheets of the Chicago Board Options Exchange, Incorporated and subsidiaries (the "Exchange") as of June 30, 2003 and 2002, and the related consolidated statements of income and retained earnings and of cash flows for the years then ended. These financial statements are the responsibility of the Exchange's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of The Cincinnati Stock Exchange ("CSE") for the years ended June 30, 2003 and 2002, the Exchange's investment in which is accounted for by use of the equity method. The Exchange's equity of \$12.2 million and \$10.3 million in the CSE's net assets at June 30, 2003 and 2002, respectively, and of \$1.9 million and \$141 thousand in that Exchange's net income for the respective years then ended are included in the accompanying financial statements. The financial statements of CSE were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for CSE, is based solely on the report of such other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other auditors, such consolidated financial statements present fairly, in all material respects, the financial position of the Exchange and its subsidiaries at June 30, 2003 and 2002, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

DeBitta + Touche LLP

August 15, 2003

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