

## **Regulatory Circular RG00-122**

DATE: August 10, 2000  
TO: Members and Member Organizations  
FROM: Division of Regulatory Services  
SUBJECT: Margin Requirements for Options  
on the Mini-NDX Index ("MNX")  
EXCHANGE James J. Adams (312) 786-7718  
CONTACTS: Rich Lewandowski (312) 786-7183

Options on the Mini-NDX Index ("MNX") are slated for listing and trading on the Chicago Board Options Exchange ("CBOE") on August 14, 2000. The CBOE MNX index is based on 1/10 the value of the NASDAQ 100 Index®. MNX is a modified capitalization-weighted index composed of 100 of the largest non-financial securities listed on the NASDAQ Stock Market. The index was created in 1985 with a base value set to 250 on February 1 of that year. After reaching a level of nearly 800 on December 31, 1993, the index level was halved on January 3, 1994. MNX options are cash settled and European style exercise.

This circular explains the margin requirements applicable to transactions in MNX options.

### **MARGIN**

In accordance with CBOE Rule 12.3(c)(4), a long option position expiring in 9 months or less must be paid for in full. For long option positions with more than 9 months until expiration, margin of at least 75% of purchase cost(current market value) must be deposited(maintained). Investors should first consult their brokerage firm regarding the firm's policy on margining long options.

The MNX index is considered broad-based. Therefore, option writers are subject to the broad-based index option category margin requirements in CBOE Rule 12.3(c)(5)(A). The margin requirement for a short put or call on a broad-based index is 100% of the current market value of the contract plus 15% of the underlying index value, less the out-of-the-money dollar amount, if any, subject to a minimum for calls of 100% of the option market value plus 10% of the underlying index value, and a minimum for puts of 100% of the option market value plus 10% of the option's aggregate exercise price.

In a margin account, no margin is required for a MNX call option carried in a short position which is covered by a long position in equivalent units of a "underlying stock basket" as defined in CBOE Rule 12.3(a)(7). Correspondingly, no margin is required for a MNX put option carried in a short position which is offset by a short position in equivalent units of a underlying stock basket. In computing margin on the underlying stock basket, the current market value used shall not be greater than the exercise price in the case of a short MNX call. In the case of a short MNX put, in computing margin on the underlying stock basket, margin shall be the amount required by CBOE Rule 12.3(b)(2), plus any amount by which the exercise price of the put exceeds the current market value of the qualified stock basket.

Where a short option contract is covered by an "escrow agreement" meeting the requirements of CBOE Rule 12.3(d)(2), no margin is required on the short put or call.

Spreads and straddles are permitted for options covering the same number of shares of the same underlying index. Members should be aware that due to their exercise feature, it is possible for European-style options to trade at a discount to their intrinsic values. It is possible that the spread margin held by the carrying broker could become insufficient to cover the assignment obligation on the short option if the customer is unable to exercise the long option and it is trading at a discount to its intrinsic value.

For spreads and straddles, 10 MNX contracts can offset 1 NDX contract. Spread and straddle margin treatment must be determined for each individual MNX series involved versus a proportionate NDX position.

#### Spread Example:

Long 5 MNX DEC (2000) 335 calls @ 7  
 Long 5 MNX DEC (2000) 345 calls @ 2  
 Short 1 NDX DEC (2000) 3400 calls @ 18

To calculate the margin requirement,  
 the short NDX call can be viewed as  
 equivalent to 10 contracts with an exercise  
 price of 340.

Long 5 MNX DEC (2000) 335 calls  
 Long 5 MNX DEC (2000) 345 calls  
 Short 10 \*\*\* DEC (2000) 340 calls

#### Margin Requirement Calculation:

Spread #1:

Long 335 calls (5) vs. Short 340 calls (5) -- (no requirement, long exercise price does not exceed short exercise price)

Spread #2:

Long 345 calls (5) vs. Short 340 calls (5) --  $(345 - 340) \times 5 \times 100 = \$2,500$

The total margin requirement for these spread positions is \$2,500. For the same underlying index, the margin requirement for each spread is the amount (aggregate) by which the long call(short put) exercise price exceeds the short call(long put) exercise price. The long side must expire with or after the short side. Any credit generated when establishing all three positions can be applied to the total margin requirement. Any debit must be paid for in full.

Straddle Example:

Short 5 MNX DEC (2000) 350 calls @ 5  
 Short 5 MNX DEC (2000) 340 calls @ 2  
 Short 1 NDX DEC (2000) 3500 call @ 9  
 MNX @ 345

To calculate the margin requirement, the short NDX call can be viewed as equivalent to 10 contracts with an exercise price of 350.

Short 5 MNX DEC (2000) 350 calls  
 Short 5 MNX DEC (2000) 340 calls  
 Short 10 \*\*\* DEC (2000) 350 puts

Margin Requirement Calculation:

Short Straddle: Short 350 calls (5) vs. Short 350 puts (5)

Call

$$\begin{array}{rcl} 5 \times 5 \times 100 & = & 2,500 \\ (.15 \times 345) - (350 - 345) \times 5 \times 100 & = & \underline{23,375} \\ & & 25,875 \end{array}$$

Put

$$\begin{array}{rcl} 5 \times (1/10 \times 9) \times 100 & = & 450 \\ .15 \times 345 \times 5 \times 100 & = & \underline{25,875} \\ & & 26,325 \end{array}$$

Short Straddle Requirement:  $\$26,325 + \$2,500 = \$28,825$

Short Combination: Short 340 calls (5) vs. Short 350 puts (5)

Call

$$\begin{array}{rcl}
 5 \times 2 \times 100 & = & 1,000 \\
 .15 \times 345 \times 5 \times 100 & = & \underline{25,875} \\
 & & 26,875
 \end{array}$$

Puts

$$\begin{array}{rcl}
 5 \times (1/10 \times 9) \times 100 & = & 450 \\
 .15 \times 345 \times 5 \times 100 & = & \underline{25,875} \\
 & & 26,325
 \end{array}$$

Short Combination Requirement:  $\$26,875 + \$450 = 27,325$

The total margin requirement for the straddle and combination positions is \$56,150 ( $\$28,825 + \$27,325$ ). For the same underlying index, with the same index multiplier, the margin requirement for each short straddle and short combination is the requirement on the short call or short put, whichever is greater, plus the premium on the other side.

## OPTION MARKET-MAKER MARGIN REQUIREMENTS

Pursuant to CBOE Rule 12.3(f), MNX options and “permitted offset” positions of MNX options market-makers may be margined on a basis which is satisfactory to the market-maker and carrying broker-dealer. A qualified stock basket is eligible for permitted offset treatment. In the case of the MNX index, the basket must contain no less than 50% of the capitalization in the index, in order to qualify as a permitted offset.

Questions regarding the margin and capital treatment of MNX options should be directed to Jim Adams at (312) 786-7718 or Rich Lewandowski at (312) 786-7183.