



Regulatory Circular RG04-45<sup>1</sup>

DATE: April 1, 2004

TO: Members and Member Firms

FROM: Regulatory Services Division

RE: Aggregation of Accounts for Position and Exercise Limit Purposes

### **Aggregation of Accounts**

The purpose of this memorandum is to summarize the provisions of Exchange rules with respect to the aggregation of accounts for position and exercise limit purposes. Exchange Rules 4.11 and 4.12 require that positions maintained in accounts directly or indirectly controlled by the same individual or entity be aggregated for position and exercise limit purposes. Pursuant to Rule 4.11, control exists when an individual or entity makes investment decisions for an account or accounts, or materially influences directly or indirectly the actions of any person who makes investment decisions. Control is also presumed in the following circumstances: a) among all participants of a joint account who have authority to act on behalf of the account; b) among all general partners to a partnership account; c) when an individual or entity holds an ownership interest of 10% or more in an entity, or shares in 10% or more of profits and/or losses of an account; d) when accounts have common directors or management; and e) where an individual or entity has authority to execute transactions in an account.

### **Non-aggregation of Accounts**

Demonstrating that control does not exist can rebut the presumption of control. The rebuttal proof must be submitted to the Exchange by affidavit and other documentation as may be appropriate. The decision to grant non-aggregation is not retroactive and is handled on a case-by-case basis. The Exchange has granted non-aggregation between the following accounts: between a market-maker's individual account and his joint account in which the market maker's participation in the joint account is limited to providing financial backing to the other member of the account; and between affiliated broker-dealers.

In situations involving requests for non-aggregation treatment between (i) affiliated broker-dealers and (ii) separate and distinct trading units within the same broker-dealer, the Exchange requires, at a minimum, the broker-dealer(s) to satisfy the following conditions:

- (i) Establish that the trading unit(s) requesting non-aggregation operates independently of other trading units of the broker-dealer, which must include the disclosure of the trading unit's trading objective;
- (ii) Create internal firewalls and information barriers to segregate the trading unit(s) receiving non-aggregation treatment from other trading units controlled by the broker-dealer that also have trading accounts;<sup>2</sup>

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<sup>1</sup> This regulatory circular was filed with the SEC in connection with SR-CBOE-2003-35.

- (iii) Maintain all trading activity of the trading unit(s) requesting non-aggregation in a segregated account, which shall be reported to the Exchange as such; and
- (iv) Maintain regulatory compliance oversight and internal controls and procedures.

If the Exchange determines that the broker-dealer that requests non-aggregation treatment has successfully rebutted the presumption of control and grants non-aggregation status, the broker-dealer must, at a minimum, comply with the following requirements:

- (i) Retain written records of information concerning the non-aggregated account, including, but not limited to, trading personnel, names of personnel making trading decisions, unusual trading activities, disciplinary action resulting from a breach of the broker-dealer's systems firewalls and information-sharing policies, and the transfer of securities between the broker-dealer's non-aggregated accounts, which information shall be promptly made available to the Exchange upon its request;
- (ii) Promptly provide to the Exchange a written report at such time there is any material change with respect to the non-aggregated account, at which point the Exchange will reexamine the bases for its determination of non-aggregation;<sup>3</sup> and
- (iii) Provide an acknowledgement to the effect that the Exchange reserves the right to impose additional restrictions and conditions with respect to the granting and removal of non-aggregation as the circumstances warrant.

This memorandum is not intended to be a comprehensive description of all of the rules and requirements relating to the aggregation of accounts for position and exercise limit purposes. For a more detailed description of these rules and requirements members are advised to refer to Exchange Rule 4.11 and the Interpretations and Policies thereunder. Questions pertaining to this memorandum may be directed to Pat Cerny at (312) 786-7722.

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<sup>2</sup> The Exchange will review this category on a case-by-case basis. With respect to physical separation, the presumption of control becomes easier to rebut as the physical separation between the trading units increases. At the minimum, the Exchange will require trading units located on the same floor to be physically isolated from each other to the extent that the Exchange is assured that no communication will take place between individuals staffed in the applicable trading units. In addition, the Exchange will require system firewalls to be in place in order to prevent the flow of information (*e.g.*, trades, positions, trading strategies) between the trading unit(s) that receives non-aggregation treatment and other trading units controlled by the broker-dealer.

<sup>3</sup> The Exchange reserves the right to freeze any position above the standard aggregation limit if the Exchange determines that aggregation is then appropriate due to changed circumstances.