CBOE
CHICAGO BOARD OPTIONS EXCHANGE

Regulatory Circular RG07-98

To:	Members, Member Organizations
From:	Division of Member and Regulatory Services
Date:	September 19, 2007
Subject:	Margin and Net Capital Requirements - CBOE NASDAQ-100 Volatility Index Options - CBOE Russell 2000 Volatility Index Options
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KEY POINTS

- Chicago Board Options Exchange ("CBOE") expects to list and trade options on the CBOE NASDAQ-100 Volatility Index (VXN") and the CBOE Russell 2000 Volatility Index ("RVX") beginning on September 27, 2007.

- For margin purposes, both indices are treated as broad-based.

DISCUSSION

On September 27, 2007, CBOE expects to list and begin trading options on the VXN and RVX. Both options will be cash-settled and European-style exercise.

The VXN and the RVX are up-to-the-minute market estimates of expected volatility that are calculated by using real-time NASDAQ-100 index options bid/ask quotes and Russell 2000 index option bid/ask quotes, respectively.

Detailed product specifications may be found on the CBOE website at the following URLs:

http://www.cboe.com/micro/vxn/

http://www.cboe.com/micro/rvx/

CUSTOMER MARGIN

In accordance with CBOE Rule 12.3(c)(4), purchases of puts or calls with 9 months or less until expiration must be paid for in full. For purchases of puts or calls with more than 9 months until expiration, it is required that 75% of the total cost (option current market value) be deposited (maintained). When time to expiration reaches 9 months, the option no longer has value for margin purposes.

VXN and RVX options are considered broad–based indices for margin purposes and option writers are subject to the margin requirements specified in CBOE Rule 12.3(c)(5). The initial and maintenance margin requirement for a short put or call on a broad-based index is 100% of the option proceeds* plus 15% of the aggregate contract value (current index level x $100) minus the amount by which the option is out-of-the-money, if any, subject to a minimum for calls of option proceeds* plus 10% of the aggregate contract value and a minimum for puts of option proceeds* plus 10% of the aggregate exercise price amount. (*For calculating maintenance margin, use current market value instead of option proceeds.)

Where a short option contract is covered by an “escrow agreement” meeting the requirements of CBOE Rule 12.3(d)(2), no margin need be required.

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 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. Therefore, the carrying broker-dealer will most likely require higher margin for spreads.

VXN and RVX options are eligible for portfolio margining. However, the minimum margin requirement must be calculated over a range of index movements of +15%/-15%.

<u>OPTION MARKET–MAKER MARGIN REQUIREMENTS</u>

Pursuant to CBOE Rule 12.3(f), VXN and RVX options may be margined on a basis that is satisfactory to the market-maker and carrying broker-dealer. In cross-margin accounts, a reduction in the margin on VXN and RVX futures contracts will be provided by the CBOE Futures Exchange’s SPAN® file for offsetting VNX or RVX option positions, respectively.[1] Note: clearing firms must set-up a separate account with The Options Clearing Corp. (“OCC”) in order take advantage of VXN and RVX options and futures margin offsets at OCC.

Questions regarding the margin treatment of VXN and RVX options should be directed to James Adams at (312) 786–7718.

<u>NET CAPITAL REQUIREMENTS</u>

VXN and RVX options will each be a separate product group.2 Under risk–based haircuts, the haircut is equal to the maximum potential loss for all option positions calculated over a range of index movements of -15%/+15%, for options market-makers and all other all broker–dealers. No baskets will be permitted. All positions are subject to a minimum charge of $25 per contract. Additionally, VXN and RVX options will receive an offset with VXN and RVX futures, respectively, under risk-based haircuts.

For those firms not utilizing risk–based haircuts, the haircut will be calculated pursuant to SEC Rule 15c3–1a(b).

Questions regarding the net capital treatment of VXN and RVX options should be directed to Robert Gardner at (312) 786–7937.

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[1] “SPAN” is a registered trademark of Chicago Mercantile Exchange Inc., used herein under license. Chicago Mercantile Exchange Inc. assumes no liability in connection with the use of SPAN by any person or entity.

[2] Risk–based haircuts may be applied pursuant to SEC Rule 15c3-1a (Appendix A).