Regulatory Circular RG09-148

To: Members
From: Trading Operation and Member & Regulatory Services Divisions
Date: December 24, 2009
Re: Professional Orders

This circular is a follow-up to Regulatory Circular RG09-123.

The SEC has approved CBOE rule filing SR-CBOE-2009-078, which allows the Exchange to implement a new order type, referred to as "Professional" orders. The purpose of this new order type is to distinguish between those public customer orders routed to CBOE which are for non-professional, retail investors and those public customer orders which are for persons or entities that have access to information and technology that enables them to professionally trade listed options in the same manner as a broker-dealer. Given that CBOE rules provide certain marketplace advantages to public customer orders over non-customer orders, such as priority over non-customer orders and Market-Maker quotes at the same price, and, in most classes, the absence of transaction fees for the execution of public customer orders, CBOE believes this rule will help ensure that the balance between professional and public customer users of the Exchange will remain equitable.

In general, this change will not require any action on behalf of members that do not act as agent for public customer accounts. Additionally, those members such as Floor Brokers, who may act as agent for public customer accounts but do not domicile customer accounts, are not expected to undertake any action to track and identify Professional orders under this rule (though they will need to mark orders as Professional when informed).

For all other members that act as agent for and domicile public customer accounts, the new rule will require that they take steps to track, identify and mark orders from customers that qualify as "Professional" customers under CBOE Rule 1.1 (ggg). Under the terms of this rule, a "Professional" is defined as a person or entity that (i) is not a broker or dealer in securities, and (ii) places more than 390 orders in listed options per day - whether executed or not - on any listed options exchange on average during a calendar month for its own beneficial account(s). Such members will be required to review their customers' activity on at least a quarterly basis to determine whether orders that are not for the account of a broker or dealer should be represented as Professional orders or customer orders. Professional orders must be marked with order origin code "W" (other customer orders will continue to be marked with order origin code "C").

Professional orders participating in the CBOE's allocation process will be treated the same as broker/dealers for purposes of execution priority and will incur a per contract transaction fee on any executed business. CBOE will require the use of the new order type beginning Friday, January 8, 2010 (this was previously noted in Regulatory Circular RG09-123).

The new rule text and answers to some frequently asked questions regarding Professional orders are included below. Additional questions may be directed to Eric Frait, Strategic Planning, at (312) 786-7747, Anthony Montesano, Trading Operations, at (312) 786-7365, or Tanja Samardzija, Market Regulation, at (312) 786-7722.

Rule Text

Chicago Board Options Exchange, Incorporated
Rules
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RULE 1.1

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Professional

(ggg) The term "Professional" means any person or entity that (i) is not a broker or dealer in securities, and (ii) places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s). A Professional will be treated in the same manner as a broker or dealer in securities for purposes of Rules 6.2A, 6.2B, 6.8C, 6.9, 6.13A, 6.13B, 6.45, 6.45A (except for Interpretation and Policy .02), 6.45B (except for Interpretation and Policy .02), 6.53C(c)(ii), 6.53C(d)(v), subparagraphs (b) and (c) under Interpretation and Policy .06 to Rule 6.53C, 6.74 (except Professional orders may be considered public customer orders subject to facilitation under paragraphs (b) and (d)), 6.74A (except Professional orders may be considered customer Agency Orders or solicited orders under Interpretation and Policy .09), 6.74B, 8.13, 8.15B, 8.87, 24.19, 43.1, 44.4 and 44.14. The Professional designation is not available in Hybrid 3.0 classes.

Frequently Asked Questions

Question 1: Will transaction fees be applicable to Professional orders?

> *Answer:* Yes. CBOE intends to assess a transaction fee of $.20/contract for executions of professional customer orders in all classes except as follows. There will be a $0.40/contract fee in DXL, OEX, XEO and DVS options and all volatility index options, and a $0.85/contract fee in credit default and credit default basket options. The index option surcharge fees, non-customer linkage fees and options regulatory fee will also apply to Professional orders. Please see the CBOE fee schedule for more information.

Question 2: Will the marketing fee be collected on Professional orders?

> *Answer*: No. Executions of Professional orders will not generate a marketing fee collection in the event that they trade against a market maker. Professional orders will be treated the same as broker/dealer orders.

Question 3: Will members be able to designate a Preferred Market-Maker for Professional orders?

> *Answer*: Yes. Members will be able to designate a Preferred Market-Maker for Professional orders in accordance with Rule 8.13.

Question 4: Will Professional orders be subject to the cancellation fee?

> *Answer*: No. As is the case with Voluntary Professional orders, Professional orders will not be subject to the cancel fee.

Question 5: Can Professionals place orders on both sides of the market?

> *Answer*: Yes. Under CBOE Rule 6.8C, *Prohibition Against Members Functioning as Market-Makers*, members may neither enter nor permit the entry of customer orders into the Exchange's electronic Order Routing System if (i) the orders are limit orders for the account or accounts of the same beneficial owner(s) and (ii) the limit orders are entered in such a manner that the beneficial owner(s) effectively is operating as a market maker by holding itself out as willing to buy and sell such securities on a regular or continuous basis. Since Professionals are treated the same as broker-dealers for purposes of this rule, the restriction does not apply to their orders.

Question 6: When will the rule go into effect?

> *Answer*: The Professional order designation will be available on CBOE beginning on January 4, 2010; however, as described below, members will have until January 8, 2010 to make any necessary changes to properly identify Professional orders. Under the new rule, members will be required to conduct a quarterly review and make any appropriate changes to the way in which they are representing orders within five days after the end of each calendar quarter. Thus, members will need to mark orders as Professional starting with the 1st quarter 2010 based upon trading activity that occurred during the 4th quarter 2009. Within five business days from the end of the 4th quarter 2009 - which is January 8, 2010 - members will have to make any necessary changes to properly identify Professional orders.

Question 7: How will a Professional order be identified on CBOE?

> *Answer*: Members will need to identify each Professional order using "W" in the order origin filed (tag 47 for FIX, ORIGIN field in the message struct for CMI).[1] Firms are

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[1] The W order origin code is the same code that is also used for Voluntary Professional orders (*see* CBOE Rule 1.1(fff)).

advised not to send data in the Account field (tag1 for FIX; ACCOUNT field in the message struct for CMI) for orders with a "W" designation. Testing of message/order formats may be scheduled with the API Group at 312-786-7300 / api@cboe.com.

Question 8: What classes will the Professional order priority be applicable to?

Answer: The Professional order priority will be applicable to all classes except those trading on the Hybrid 3.0 platform (currently only SPX). If an order is entered into an SPX option series using the W order origin code, the order will continue to be treated the same as an order using the C order origin code.

Question 9: When can members start testing the order origin code with CBOE?

Answer: Now. Please contact the API Group at (312) 786-7300 to coordinate testing.

Question 10: Will it be possible for a Professional to revert back to a non-professional, public customer and use origin code C?

Answer: Yes. If a customer exceeds the 390 average daily order threshold during any month in a given quarter, the customer's orders will need to be marked Professional for the entire next quarter. However, if the customer thereafter averages 390 orders or less per day during each month of a quarter, the customer's orders would be entitled to be marked as a regular customer using order origin code C during the next quarter.

Question 11: Will the 390 average daily order requirement only apply to orders entered on CBOE?

Answer: No. In determining the average daily number of orders, all orders entered for the same beneficial account(s) of a non-broker-dealer customer should be considered without regard to the options exchange where the order is routed.

Question 12: Will cancel/replace, IOC, crossing, complex, and open outcry orders need to be included in the calculation?

Answer: Yes. Unless an order type is specifically excluded (currently only orders in any FLEX Option series) all option orders will count in the 390 average daily order calculation. In the case of a cancel/replace, if a customer places an order and submits a cancel/replace, then the cancel/replace will count as a separate order. If an order is pegged to the NBBO, then each time a cancel/replace is used to follow the NBBO will count as a separate order.

Question 13: If a customer places a reserve order or similar type order that automatically replenishes, will each "replenish" need to be counted?

Answer: No. Members will only need to count the original entry of the order.

Question 14: If a customer places a single original order that is then broken up by the member into multiple orders to achieve a specific execution strategy, will each individual order need to be counted?

Answer: No. Members will only need to count the single original order.

Question 15: Will trades received via CMTA need to be counted by the receiving member?

> *Answer*: No. Trades that are CMTA'd will not need to be counted by the receiving member. The executing member should have already counted the orders associated with these trades.

Question 16: Will customer accounts associated with orders linked by exchanges need to be identified?

> *Answer*: No. Orders linked by exchanges (or exchange outbound routing brokers) in the course of fulfilling their obligations under the Options Order Protection and Locked/Crossed Market Plan will not need to be counted.

Question 17: If a non-broker-dealer person or entity places orders for multiple accounts, will the orders need to be aggregated?

> *Answer*: Yes. All orders for accounts controlled by the same person or entity must be aggregated when determining whether or not the 390 average daily order threshold has been exceeded by that person or entity.

Question 18: Will members be able to aggregate accounts by Taxpayer Identification Number or by In-Concert Number?

> *Answer*: Yes. Either of these will be acceptable identifiers to aggregate orders from related accounts.

Question19: If accounts have different Taxpayer Identification Numbers, is it okay to not aggregate them?

> *Answer*: Not necessarily. Members will need to recognize and aggregate orders from accounts that are obviously related to each other whether or not they have different taxpayer identification numbers. For example, if two accounts are named XYZ-I and XYZ-II and executions are regularly allocated between them, CBOE would expect a member to aggregate orders placed for these accounts even though they might have different Taxpayer Identification Numbers.