Regulatory Circular Number RG92-46

Date: **July 31, 1992**

To: **Member Firms**

From: **Office of the Chairman**

Re: **Expanded Position Limits in Opening Settled S&P 500 Index Options**

Summary: The Securities and Exchange Commission has approved significant changes to the Exchange's position limit rules as they pertain to European-style S&P 500 index options whose settlement value is based on the **opening** prices of the index component stocks on the last business day prior to expiration ("opening-settled"). The rule changes expand position limits for opening-settled S & P 500 index option contracts, but also require that the contract specifications of all newly-listed S&P 500 index options be changed so that their settlement value will be based on opening prices. Therefore, from this date, no new S&P 500 index options whose settlement value is based on closing prices of the index component stocks on the last business day prior to expiration ("closing-settled") will be listed. This circular explains the policies and procedures under which the expanded position limits may be allowed as well as the manner in which existing and new S&P 500 index options series will be identified for trading.

As amended, the rules now stipulate that the basic position limit for opening-settled S&P 500 index option contracts is *45,000* contracts on the same side of the market; in addition, the "telescoping" requirement that reduces maximum near-month holdings to 15,000 contracts has been eliminated for opening-settled S&P 500 index option contracts only. However, all closing-settled S&P 500 index options remain subject to the 25,000 contract overall limit with no more than 15,000 contracts in the near-month series.

Furthermore, the amended rules, with respect to opening-settled S&P 500 index options only: expand the hedge exemption policy for public customer accounts so that the exempted amount may, under certain circumstances, be increased to 150,000 contracts; allow money managers with multiple customer accounts under their control to apply for a hedge exemption of up to 250,000 contracts, with no more than 135,000 contracts for any one account; and, include a new provision that may enable the proprietary account of a member organization to obtain an exemption of up to 100,000 contracts for positions which are used to facilitate public customer orders (irrespective of any use of the basic position limit). Altogether, these changes substantially increase the ability of investors to manage the risk of diversified stock portfolios with European-style, opening-settled S&P 500 index options.

The remainder of this circular describes in more detail the impact of existing and revised policies concerning S&P 500 index options position limits. The last section describes the ticker symbol changes necessary to accompany the addition of opening-settled S&P 500 index options which will commence on Monday, August 24, 1992.

Basic Position Limit: The position limit is now 45,000 contracts on the same side of the market for opening-settled S&P 500 index options, without respect for strategy or hedging. *This rule is now effective and applies to opening-settled S&P 500 index options expiring in September*

1992, December 1992 and March 1993 that currently employ the ticker symbol NSX. Opening- and closing-settled S&P 500 index option positions must be combined for position limit purposes during the transition period (August 24, 1992 to December 18, 1993) when both will exist. *Closing-settled S&P 500 index options remain subject to a position limit of 25,000 contracts, of which no more than 15,000 can be maintained in the front month series.* Therefore, the basic position limit rules now allow up to an additional 20,000 opening-settled S&P 500 index options for those customers currently maintaining the maximum of 25,000/15,000 closing-settled contracts. The basic position limit rules apply to all market participants and may be maintained irrespective of positions eligible for the exemptions described below.

Customer Hedge Exemption: Public customer accounts maintaining a diversified portfolio as defined in CBOE Rule 24.4, may be able to receive an exemption for up to *150,000* opening-settled S&P 500 index options in addition to the basic 45,000 contract limit, when realized (but aggregated with closing-settled contracts). *Exemption requests for closing- settled contracts remain subject to the 75,000 contract limit in effect when those contracts were first listed for trading.* Therefore, the customer hedge exemption rules allow up to an additional 75,000 opening-settled S&P 500 index option contracts for customers currently maintaining the exempted maximum of 75,000 closing-settled contracts. The strategies now eligible for this exemption from the basic position limit applicable to opening-settled S&P 500 index options are:

1) Hedges: long stock[1]/long put or debit put spread[2]; and, short stock/long call;

2) "Covered" Writes: long stock/short call and short stock/short put;

3) Hedgewraps (Collars): long stock/short call/long put or debit put spread.

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[1]For purposes of this memorandum, it is assumed that a long or short stock position qualifies for a hedge exemption because it meets the criteria set forth in CBOE Rule 24.4.

[2]Qualified debit put spreads are defined as those consisting of European-style index put options where the strike price of the long put option is greater than the strike price of the short put option and both have the same expiration date. Please refer to Regulatory Circular #RG91-64 for the terms under which qualified debit put spreads may be effected in a cash account without fully securing the short put with cash or cash equivalents equal to its aggregate strike price.

The Exchange may now *verbally* grant a public customer hedge exemption prior to a transaction that places an account above the basic position limit, but such approval must be followed by the submission of the hedge exemption application within five business days. *For closing-settled contracts the policy remains unchanged: a hedge exemption customer must submit all required documentation and receive prior approval from the Exchange before exceeding the basic position limit.*

Aggregation Exemption for Money Managers[3]: In recognition of the fact that intermediaries are hired on behalf of public customers, and that the hedging needs of individual accounts may vary, the new rule allows money managers that use options on behalf of multiple customers a hedge exemption of up to 250,000 contracts in opening-settled S&P 500 index option contracts; however, no more than 135,000 contracts may be on behalf of a single account. Money managers must conform to the strategy rules and approval policy described in "Customer Hedge Exemption" above.

Facilitation Exemption for Member Organizations: Member organizations that wish to facilitate public customer orders pursuant to Exchange Rule 6.74(b) may qualify for an exemption of up to 100,000 contracts in their firm proprietary account in opening-settled S&P 500 index option contracts. The facilitation exemption may be granted verbally and must be followed by the member organization's submission of documentation within five business days as to how the resulting firm position was hedged. This exemption would be available irrespective of a member firm's basic position (see "Basic Position Limit" above), if any.

Ticker Symbol Changes: Long-dated S&P 500 index options notwithstanding, the primary effect of maintaining "SPX" as the symbol for the most active S&P 500 index options at the CBOE[4] is to switch the symbols NSX and NSZ, to SPX and SPZ, respectively. **Effective on Monday, August 24, 1992 , the root symbol for existing closing-settled S&P 500 index options now identified as SPX/SPZ will have been changed to NSX/NSZ. Conversely, all opening-settled S&P 500 index options currently identified as NSX/NSZ will have had their root symbol changed to SPX/SPZ.**

*On that same date, the existing long-dated, closing-settled S&P 500 index options expiring in December 1993 will have their root symbol converted from SPL to **SPB**. Lastly, the long-dated, opening-settled S&P 500 index options expiring in June 1994 that have the root symbol NPL (to be listed August 3, 1992)[5], will have their root symbol converted to **SPL**.*

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[3] Position and exercise limit aggregation for money managers is based on Interpretation .03 of CBOE Rule 4.11.

[4] It is assumed that under the new rules, opening-settled contracts with higher position limits will become the most actively traded. Indeed, closing-settled contracts will not be added as existing ones expire.

[5] See Information Circular IC92-77, dated July 15, 1992.

Some final considerations and reminders are described below:

Opening- and closing-settled S&P 500 index option positions must be combined for position limit purposes during the transition period (August 24, 1992 to December 18, 1993) when both will exist. *The limits pertaining to closing-settled S&P 500 index options when they were first listed may not be exceeded, nor may the aggregate number of contracts on the same side of the market exceed the limits prescribed by the new rules in effect for opening-settled S&P 500 index options.*

As of the date of this circular, only closing-settled S&P 500 index options exist in the October 1992 expiration month[6]. These, too, will have their root symbol converted to NSX/NSZ following August expiration;

Closing-settled S&P 500 index options, to be identified as NSX/NSZ, exist for all quarterly expirations in 1993 except for September; and,

SET remains the ticker symbol for dissemination of the final settlement value for expiring opening-settled S&P 500 index options. This value is not disseminated until all component stocks of the S&P 500 index have opened for trading on the last business prior to expiration, or the close of trading on each component stock's primary market on that day, whichever occurs first.

Reduced-value S&P 500 index options expiring in December 1992 (**LSX**) and December 1993 (**LSW**) will be unaffected. These are closing-settled contracts and no corresponding opening-settled contracts will be listed in those expiration months. The Exchange, however, may list *opening- settled* reduced-value S&P 500 index options expiring in December 1994 and subsequent years.

As a result of the approved rule changes, all closing-settled S&P 500 index options will expire on or before December 18, 1993. The CBOE has developed a brochure containing charts that describe the symbol conversion and expiration month additions that will occur during the transition beginning August 24, 1992. To obtain one, please call 1-800-OPTIONS.

For regulatory and procedural questions concerning position limits, including requests for exemption applications, please contact the CBOE Department of Market Surveillance at (312) 786-7722.

[6]See Information Circular IC92-77, dated July 15, 1992.