

Regulatory Circular RG97-10

To: All Exchange Members

From: Membership Department

Date: January 17, 1997

Re: Lease Agreement Requirements and Lessor Exposure

In response to questions raised by members concerning Exchange rules relating to the leasing of memberships and the obligations of lessors, the Membership Committee has determined to reissue this memorandum. The memorandum does not reflect any new rules or requirements, but rather, is intended to remind members of the current rules which set forth the provisions that are required in all membership lease agreements and to discuss certain aspects of the owners' financial exposure when leasing a membership to another member or when registering a membership for a member organization.

Lease Requirements

There are four specific provisions that must be contained in all lease agreements. CBOE Rule 3.16(b) sets forth the requirements as follows:

- 1) the duration (length of time) of the lease agreement
- 2) the consideration to be paid by the lessee
- 3) the assignability of the respective interests of the lessee and lessor in such lease agreement
- 4) which party shall exercise the voting rights of the membership and which party shall provide the funds necessary to satisfy all applicable Exchange dues, fees and other charges.

Lessor Financial Exposure

When an owner (lessor) leases his/her membership to an individual or organization, the lessor has potential financial exposure resulting from the lessee's activities while on the leased membership to the extent provided by Rule 3.16. Rule 3.16(b)(iii) establishes that when the owner (lessor) effects the sale of the leased membership, claims against the proceeds from the sale of such membership may be made in accordance with CBOE Rule 3.15 by member creditors of both the lessee and lessor.

The rule further provides that priority is given to claims against the lessee. In addition, with respect to sums due the Exchange, Rule 3.16(b)(i) establishes that, notwithstanding any contractual division of responsibility between the lessee and lessor with respect to the payment of dues, fees and other charges, the lessor will remain obligated to pay all amounts due the Exchange. Exchange rules do not provide a mechanism by which one member can force another

member to sell his/her membership to satisfy either lessor or lessee debts. However, if sums are due the Exchange, the Exchange is empowered to direct the sale of a membership pursuant to CBOE Rule 2.23 in order to satisfy such obligations.

Any devices utilized by lessors in an attempt to reduce or eliminate their financial exposure to other members for a lessee's actions, (e.g., hold harmless or indemnification agreements) are a matter of private contract and do not affect the rights of third parties, such as member creditors. CBOE rules do not provide any mechanism for a lessor to reduce or eliminate financial exposure relating to the leasing of a membership.

Similarly, when an individual member registers his/her seat for a member organization, the member may also have financial exposure arising out of the member organization's activities during the course of such arrangement. CBOE Rule 3.15, which provides for the distribution of proceeds from the sale of Exchange memberships, establishes that when a membership is sold, the proceeds may be used to pay certain sums due from both the member and the member organization on whose behalf the membership was registered.

If you have any questions regarding this circular, please contact Lawrence J. Bresnahan at (312) 786-7713 or Rae Tapia-Pancake at (312) 786-7460.

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