

Regulatory Circular RG97-113

Date: September 5, 1997

To: Membership

From: Operations Planning Division

Re: Responsibilities of Floor Brokers

A Floor Broker handling an order is to use due diligence to execute the order at the best price or prices available to him, in accordance with Exchange rules. The responsibilities of a Floor Broker, as set forth in Rule 6.73, extend to all members acting in an agency capacity, including independent Floor Brokers who operate at a single trading station, independent Floor Brokers who operate from a booth location, Floor Brokers employed by member firms and Floor Brokers employed by Designated Primary Market Makers who execute agency orders on behalf of a DPM.

Use of Due Diligence

As a general matter, a Floor Broker has an obligation to assure that all “marketable” orders are continuously represented at the station where the option is traded. For these purposes, the Exchange has defined a “marketable” order to include all market orders and limit orders where the limit price of a buy (sell) order is equal to or higher (lower) than the displayed bid (offer). A Floor Broker’s use of due diligence in executing an order includes ascertaining whether a better bid or offer than is being displayed is available in the trading crowd. In so doing, a Floor Broker must make all persons in the trading crowd aware of his request for a quotation. A Floor Broker’s use of due diligence also includes taking the necessary measures to ensure the proper execution of an order at the price and size that it is entitled to under the firm quote rule. Where, consistent with his obligations to use due diligence, a Floor Broker bids or offers on behalf of a customer order at a price which is better than the disseminated market quote and that bid or offer is not immediately accepted, under the firm quote rule, the Floor Broker remains entitled to the price disseminated when the order was announced in the amount prescribed under the firm quote rule, as long as the Floor Broker promptly requests satisfaction on the order.

Priority of Bids and Offers

All bids and offers for a particular series of options must be made by public outcry at the trading station where that class of options is traded. All bids and offers must be general ones and shall not be specified for acceptance by particular members. The highest bid (lowest offer) shall have priority, but where two or more bids (offers) for the same option contract represent the highest (lowest) price and one such bid (offer) is displayed in the public customer limit order book, the book's bid (offer) has priority over any other bid (offer) at the post. If two or more bids (offers) represent the highest (lowest) price and a bid (offer) from the customer limit order book is not involved, priority shall be afforded to such bids (offer) *in the sequence in which they are made*.

A Floor Broker should make every effort to determine the sequence in which bids or offers are made in response to the Floor Broker's request for such bids or offers. The member who responded first in sequence at the highest bid or lowest offer is entitled to take any portion or all of the contracts available. Only if the first member to respond determines that he does not intend to take all of the available contracts may the Floor Broker allocate contracts to the member whose bid or offer was next in sequence at the transaction price.

With respect to Designated Primary Market Makers (DPMs) acting as agent, all transactions involving an order represented by the DPM and the DPM's principal account must be announced by public outcry. Due to the DPMs prior knowledge of the agency order, in such a transaction, a DPM employee acting on behalf of the DPM's market maker account cannot be deemed the first to respond to the request for a market from a floor broker who is also employed by the DPM.

Crossing Orders

The procedures for crossing orders are set forth in Rule 6.74. A Floor Broker who holds orders to buy and sell the same option series may cross such orders provided that he proceeds in the manner set forth in the Rule. With respect to regular (non-facilitation) crosses, a Floor Broker must first request a market in the series for which he holds crossable orders. Upon receiving the current market, the Floor Broker must bid above the highest bid and give a corresponding offer at the same price or a price differing by the minimum fraction or he must offer below the lowest offer and give a corresponding bid at the same price or a price differing by the minimum fraction. Only if the higher bid or lower offer is not taken may the Floor Broker cross the orders at the higher bid or lower offer by announcing by public outcry that he is crossing and giving the quantity and price.

Section (b) of Rule 6.74 sets forth the procedures for effecting a "facilitation" cross transaction. A Floor Broker who holds an order for a public customer of a member organization and a "facilitation order" may cross such orders provided that he proceeds in accordance with the Rule. The member organization must disclose on its order ticket for the public customer which is subject to facilitation, all the terms of the order. The Floor Broker must then request bids and

offers for the execution of all of the components of the order. After providing an opportunity for such bids and offers to be made, the Floor Broker must, on behalf of the customer order that is subject to facilitation, bid above the highest bid or offer below the lowest offer in the market, identifying the order as being subject to facilitation. After all other market participants have had an opportunity to accept the bid or offer on behalf of the customer order that is subject to facilitation, the Floor Broker may cross all or any remaining part of the customer order with the facilitation order by public outcry. In such a transaction, a customer order (the order that is subject to being facilitated) is given precedence over any other bid or offer in the trading crowd to trade immediately with the facilitation order.

Acts or practices of Floor Brokers which have as their purpose the redirection of orders from another execution facility (e.g. RAES or the public limit order book) to the Floor Broker will be deemed as inconsistent with just and equitable principles of trade. For example, the placement of an order in the public limit order book for the purpose of “blocking” or otherwise eliminating RAES trades at that price is improper activity. Additionally, requesting or accepting a limit order with instructions to “protect” the order if transactions take place at the limit price of the “protected” order without that order also being executed (“book-or-protect orders”) is inappropriate since a Floor Broker cannot “protect” an agency order under Exchange rules.

The information contained in this memorandum is a summary of areas of the Exchange rules concerning the obligations of members acting in an agency capacity. For a full understanding of the obligations of members when acting in an agency capacity, Members should review the full text of each Exchange rule concerning the handling and representation of orders.

Questions concerning this memorandum may be directed to Edward L. Provost, Operations Planning Division, at 312-786-7717.