

Regulatory Circular RG98-116

To: Market-Makers and Clearing Firms

From: Membership Committee

Re: Market-Maker Letters of Guarantee

Date: October 15, 1998

This circular replaces and supersedes Regulatory Circular RG98-89.

Requirement to Submit Market-Maker Letter of Guarantee

CBOE Rule 8.5(a) requires that every market-maker have on file with the Exchange a letter of guarantee from a clearing firm. CBOE Rule 8.5(b) requires that this letter of guarantee provide that the issuing clearing firm accepts financial responsibility for Exchange transactions made by the guaranteed market-maker.

The Options Clearing Corporation (OCC) also requires that every market-maker have in place an OCC Account Agreement executed by the market-maker, the market-maker's clearing firm, and OCC. It has been the practice of the Membership Department to accept a market-maker's OCC Account Agreement in satisfaction of the guarantee requirement under Rule 8.5(a). However, the OCC Account Agreement has been drafted for the purposes of OCC's rules and it is not intended to correlate with CBOE's rules. In addition, the OCC Account Agreement does not have quite the same scope as Rule 8.5(b).

Accordingly, the Membership Committee has determined to require that market-makers submit the attached Market-Maker Letter of Guarantee form to the Membership Department. In situations where a market-maker clears through more than one clearing firm (such as when a market-maker executes Exchange transactions through both a sole proprietor market-maker account and through a joint account that each clear through different clearing firms), the market-maker is required to submit a CBOE Market-Maker Letter of Guarantee form from each clearing firm to cover Exchange transactions executed by the market-maker through that respective clearing firm.

The Membership Department will also continue to require market-makers to submit an OCC Account Agreement to ensure that a guarantee is also in place under OCC's rules.

Clearing firms may obtain copies of the attached Market-Maker Letter of Guarantee form from the Membership Department. **Every current market-maker must have a properly executed copy of the form on file with the Membership Department no later than January 15, 1999 from each clearing firm through which the market-maker executes Exchange transactions.**

Scope of Market-Maker Letter of Guarantee

Pursuant to Rule 8.5(b), a clearing firm that executes the attached Market-Maker Letter of Guarantee form accepts financial responsibility for Exchange transactions made by the guaranteed market-maker when executing such transactions through that clearing firm. The attached form has been revised to specifically address situations in which a market-maker clears through more than one clearing firm and clarifies that a clearing firm does not accept financial responsibility for Exchange transactions made by the covered market-maker when that market-maker is executing such transactions through a different clearing firm.

Pursuant to CBOE Rule 1.1(l), the term "Exchange transaction" means a transaction on the floor of the Exchange between members of the Exchange for the purchase or sale of an option contract or the purchase or sale of any other security admitted to trading on the Exchange, or for the closing out of a long or short position in an option contract.

Thus, a Market-Maker Letter of Guarantee form from a clearing firm guarantees any trade on the Exchange made by the guaranteed market-maker when executing such transactions through that clearing firm. In addition, this guarantee is not limited solely to cleared trades. For example, in a situation where a market-maker clears through only one clearing firm, the Market-Maker Letter of Guarantee form from that clearing firm would apply to any uncleared trade that the guaranteed market-maker did in fact enter into on the Exchange. For example, if an arbitration panel were to find in a proceeding concerning an out-trade dispute involving that market-maker that the market-maker entered into a trade on the Exchange, the Market-Maker Letter of Guarantee form would guarantee that trade. Accordingly, parties to an arbitration proceeding concerning an out-trade dispute may wish to request a finding from the arbitration panel as to whether an Exchange transaction occurred.

However, it should also be noted that a Market-Maker Letter of Guarantee form would not guarantee the payment of fees incurred by the guaranteed market-maker because the term "Exchange transaction" does not encompass fees (or anything other than trades on the Exchange made by the guaranteed market-maker).

Any questions regarding this circular may be directed to RaeDell Pancake, Director of the Membership Department, at (312) 786-7460.

To: CBOE Membership Department

From: _____ (Clearing Member Firm)

Re: MARKET-MAKER LETTER OF GUARANTEE

In connection with the qualification of _____ as a Market-Maker on the Chicago Board Options Exchange and pursuant to CBOE Rule 8.5, the undersigned Clearing Member Firm accepts financial responsibility for Exchange transactions made by the above named Market-Maker when executing such transactions through the undersigned Clearing Member Firm. Pursuant to CBOE Rule 1.1(l), the term "Exchange transaction" means a transaction on the floor of the Exchange between members of the Exchange for the purchase or sale of an option contract or the purchase or sale of any other security admitted to trading on the Exchange, or for the closing out of a long or short position in an option contract.

Clearing Member Firm Representative (print name) _____

Clearing Member Firm Representative Title _____

Clearing Member Firm Rep. (signature) _____

Execution Date _____