SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–44156; File No. SR–CBOE–00–14]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 Thereto by the Chicago Board Options Exchange, Incorporated to Increase Position and Exercise Limits for Nasdaq 100 Index Options, Expand the Index Hedge Exemption, and Eliminate the Near-Term Position Limit Restriction

April 6, 2001.

I. Introduction

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4[2] thereunder, on April 10, 2000, the Chicago Board Options Exchange, Incorporated (''CBOE'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'') a proposal to increase position and exercise limits for Nasdaq 100 Index (full value) options (''NDX'') and Nasdaq 100 Index (1/10th) options (''MNX''),[3] expand the index hedge exemption for NDX and MNX options, and eliminate the near-term position limit restriction. The proposed rule change was published for comment in the **Federal Register** on October 24, 2000.[4] On February 12, 2001, CBOE submitted Amendment No. 1 to the proposal.[5] The Commission received no comments on the proposal. This order and notice approves CBOE's proposal, solicits comment from interested persons on Amendment No. 1 thereto, and approves Amendment No. 1 on an accelerated basis.

II. Description of the Proposal

The Exchange proposed to amend CBOE Rule 24.4 by: (1) Increasing the position limit in NDX options from 25,000 contracts to 75,000 contracts; (2) increasing the position limit in MNX options from 250,000 contracts to 750,000 contracts; (3) increasing the position limit of the index hedge exemption in NDX options from 75,000 contracts to 150,000 contracts; (4) increasing the position limit of the index hedge exemption in MNX options from 500,000 contracts to 1,500,000 contracts; and (5) eliminating the 15,000 contract near-term limit for NDX options. CBOE has stated that exercise limits will continue to correspond to position limits, so that investors may exercise the number of contracts set forth as the position limit during any period of five consecutive business days.

CBOE has made several arguments in support of its request. First, CBOE maintains that the expanded position and exercise limits will give market participants greater flexibility in deciding their portfolios without increasing the risk of market manipulation or disruption. CBOE believes that the pool of securities that comprise the Nasdaq 100 Index is so large that manipulation of the index or its overlying options (such as NDX and MNX) would be extremely unlikely, even with the expanded position limits. In addition, CBOE believes that the expanded limits are necessary to help its options market to compete against the futures markets. CBOE has stated that futures positions that are deemed *bona fide* hedging transactions are exempt from position limit rules under the Commodity Exchange Act and its implementing regulations.[6] Thus, institutions may offset much larger equity positions using index futures products than by using index options. Therefore, CBOE concludes that increasing the position limits for its index options will help maintain competitive equality with the future markets. Finally, CBOE has noted that the Commission has approved similar proposals to increase or remove position and exercise limits in the past.[7]

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act.[8] In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,[9] which requires, among other things, that the rules of an exchange be designed to promote just and equitable principles of trade, to facilitate transactions in securities, and to protect investors and the public interest.

Since the inception of standardized options trading, the options exchanges have had rules imposing limits on the aggregate number of option contracts that a member or customer may hold or exercise. These rules are intended to prevent the establishment of options positions that are sufficiently large as to create incentives to manipulate or disrupt the underlying market in a manner that would benefit the options position. At the same time, the Commission has recognized that position and exercise limits for options must not be established at levels that are so low as to discourage participation in the options market by institutions and other investors with substantial hedging needs, or to prevent specialists and other market-makers from adequately meeting their obligations to maintain fair and orderly markets.

The Commission finds that CBOE's proposal to raise the position and exercise limits for NDX and MNX options is consistent with the Act. As noted above, the Commission has approved similar proposals in the past.[10] The Commission also finds that CBOE's proposal to raise the hedge exemption for NDX and MNX option position limits is consistent with the Act. An increase in these limits will permit more effective hedging of large stock portfolios and may increase the depth and liquidity of the market for NDX and MNX options. At the same time, the Commission does not believe that raising the position, exercise, or hedge exemption limits for these options will substantially increase the likelihood of manipulation of the market for these options or their underlying securities. The Nasdaq 100 Index consists of 100 securities that collectively have a very large market capitalization, which greatly reduces the

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] The Exchange recently listed and traded options (MNX options) based on a value of 1/10th the current value of NDX options and made related changes to position and exercise limits for that option class. *See* Securities Exchange Act Release No. 43000 (June 30, 2000), 65 FR 42409 (July 10, 2000).

[4] Securities Exchange Act Release No. 43456 (October 17, 2000), 65 FR 63657.

[5] *See* Letter from Timothy Thompson, Assistant General Counsel, CBOE, to Nancy Sanow, Assistant Director, Division of Market Regulation, Commission (February 9, 2001). In Amendment No. 1, CBOE: (1) Revised the tables in the proposed rule text to account for changes that CBOE made to the tables following the Commission's approval of SR–CBOE–00–15 on June 30, 2000; (2) clarified that positions in NDX and MNX options must be aggregated pursuant to CBOE Rule 24.4(d) to determine compliance with the position limits; and (3) provided additional reasons for the Commission to approve the proposed rule change.

[6] *See* 7 U.S.C. 6a(3); 17 CFR 1.3(z) and 1.47.

[7] *See e.g.,* Securities Exchange Act Release No. 40875 (December 31, 1998), 64 FR 1842 (January 12, 1999) (approving increase in position and exercise limits for standardized equity options on CBOE, Amex, PCX, and Phlx). *See also* Securities Exchange Act Release No. 40969 (January 22, 1999), 64 FR 49111 (February 1, 1999) (approving two-year CBOE pilot program to eliminate position and exercise limits for OEX, SPX, and DJX index options and for FLEX options overlying those indexes); Securities Exchange Act Release No. 43867 (January 22, 2001), 66 FR 8250 (January 30, 2001) (extending CBOE pilot program for an additional four months).

[8] In approving this proposal, the Commission has considered its impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[9] 15 U.S.C. 78f(b)(5).

[10] *See supra* note 7.

potential for manipulation of the index or its overlying options (such as NDX and MNX). Furthermore, the Commission previously has stated its belief that CBOE's surveillance programs are ''adequate to detect and deter violations of position and exercise limits, as well as to detect and deter attempted manipulation and other trading abuses through the use of * * * illegal positions by market participants.'' [11]

The Commission also finds that elimination of the front-month limitation for NDA options is consistent with the Act.[12] As the Exchange has noted, a front-month limitation was established for American-style broad-based index options as a measure to lessen market volatility experienced at the close of trading on expiration when stock/index programs were unwound. CBOE has argued that this rationale is not relevant for the NDX option, which is a European-style contract with a settlement value based on a volume weighting of opening stock prices as reported within the first five minutes of trading.[13] Eliminating the front-month position and exercise limits for NDX options may bring additional depth and liquidity, in terms of both volume and open interest, to the NDX without significantly increasing concerns regarding inter-market manipulation or disruption of the index options or the underlying component securities.

The Commission finds good cause for approving Amendment No. 1 to the proposal prior to the thirtieth day after the date of public notice in the **Federal Register**, pursuant to Section 19(b)(2) of the Act.[14] The original filing has been published in the **Federal Register**, and no comments were received. The only material changes to the rule text provided in Amendment No. 1 are increases in the position and hedge exemption limits for MNX options that will make these limits ten times the equivalent limits for NDX options. Currently, CBOE Rule 24.4(d) states that MNX options must be aggregated with NDX options at a ratio of ten-to-one to determine compliance with the position limits. Approving Amendment No. 1 on an accelerated basis will give force to the intent of the existing rule and help eliminate confusion in the application of position limits for NDX and MNX options.

IV. Conclusion

It is Therefore Ordered, pursuant to Section 19(b)(2) of the Act,[15] that the proposed rule change (SR–CBOE–00–14) is approved and that Amendment No. 1 thereto is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[16]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 01–9116 Filed 4–12–01; 8:45 am]

BILLING CODE 8010–01–M

[11] Securities Exchange Act Release No. 43052 (July 18, 2000), 65 FR 45805, 45808 (July 25, 2000) (approving increase in position and exercise limits for narrow-based index options on CBOE).

[12] Currently, the Exchange does not impose near-term limits on MNX options.

[13] Moreover, CBOE has stated that its surveillance procedures during the week of expiration of NDX options include communication with NASD Regulation to determine whether there are any concerns regarding potential manipulation in the securities which comprise the NDX.

[14] 15 U.S.C. 78s(b)(2).

[15] 15 U.S.C. 78s(b)(2).

[16] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–44152; File No. SR–CBOE–00–13]

Self Regulatory Organizations; Order Approving Proposed Rule Change by the Chicago Board Options Exchange, Inc. Amending Procedures and Requirements for Trading in Joint Accounts in Equity and Index Options

April 5, 2001.

I. Introduction

On April 3, 2000, the Chicago Board Options Exchange, Inc. (''CBOE'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] a proposed rule change to amend the procedures and requirements for trading in joint accounts in equity and index options. On January 8, 2001, the CBOE filed Amendment No. 1 with the Commission.[3] The proposed rule change was published for comment in the **Federal Register** on February 27, 2001.[4] No comments were received on the proposal.[5] This order approves the proposed rule change, as amended.

II. Description of the Proposal

The CBOE proposes to amend Interpretation .06 to Exchange Rule 8.9 and Exchange Regulatory Circulars RG 98–94 and RG 98–95, which set forth Exchange procedures and requirements for trading in joint accounts in equity and index options, to allow certain transactions between joint accounts that have common participants.

In early 1980s, the CBOE adopted a regulatory interpretation that prohibited trading between related accounts with greater than 10% common ownership. The Exchange later amended Interpretation .06 to Exchange Rule 8.9 (Securities Accounts and Orders of Market-Makers) to extend this trading prohibition to market maker joint accounts that have common participants.[6] Interpretation .06 to Exchange Rule 8.9 and Exchange Regulatory Circulars [7] state that ''no joint account participant shall cause a transaction to be executed for the joint account with another member acting on behalf of another joint account if the member knows, or in the exercise of reasonable care under the circumstances, the member has reason to know that the two joint accounts have one or more common participants.'' [8]

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] Letter from Timothy Thompson, Assistant General Counsel, Legal Department, CBOE, to Deborah Flynn, Senior Special Counsel, Division of Market Regulation (''Division''), Commission, dated October 23, 2000 (''Amendment No. 1''). In response to comments from Commission staff, the Exchange submitted Amendment No. 1, which: (1) represents that staff at the American Stock Exchange LLC, International Securities Exchange LLC, Pacific Exchange, Inc., and Philadelphia Stock Exchange, Inc. have informed the CBOE that their respective regulatory policies do not include any specific rule or regulatory circular that prohibits trading between joint accounts with common participants or that addresses ''wash sale'' transactions (*i.e.,* a transaction in a registered security that involves no change in beneficial ownership, for the purpose of creating a false or misleading appearance of active trading); (2) represents that the proposed rule change makes the CBOE's rules and regulatory policies regarding transactions between related accounts or entities consistent with those in place at the other options exchanges; and (3) provides three letters that were submitted by CBOE members to the Exchange in support of the rule filing.

[4] Securities Exchange Act Release No. 43984 (February 20, 2001), 66 FR 12574 (February 27, 2001).

[5] Although the Commission received no comments on the proposal, three letters were sent to the CBOE and forwarded to the Commission. *See* letters from Patricia Levy, General Counsel, and Steven O'Malley, Compliance & Regulatory Officer, Hull Trading Company, LLC, to Mary Bender, Senior Vice President, Division of Regulatory Services, CBOE, dated August 13, 1999; Michael J. Carusillo, Chief Executive Officer, and Barbara McHugh, President, Fulcrum Investment Group, LLC, to Pat Cerny, CBOE, dated July 17, 1998; and William J. Shimanek, Kessler, Asher Clearing, to Pat Cerny, CBOE, dated April 24, 1996. *See also* Amendment No. 1, *supra* note 3.

[6] *See* Securities Exchange Act Release No. 38286 (February 13, 1997), 62 FR 8287 (February 24, 1997) (SR–CBOE–96–70).

[7] The Regulatory Circular governing joint account trading in certain index options was approved in Securities Exchange Act Release No. 31174 (September 10, 1992), 57 FR 42789 (September 16, 1992). The Regulatory Circular governing joint account trading in equity options was approved in Securities Exchange Act Release No. 36977 (March 15, 1996), 61 FR 11911 (March 22, 1996).

[8] CBOE Rule 8.9, Interpretation .06.