Regulatory Circular RG03-49

Date: **July 2, 2003**

To: **Members**

From: **Legal Division**

Re: **SEC Approval of $1 Strike Price Intervals in Equity Option Classes**

The SEC recently approved a proposed rule change by CBOE initiating a one-year pilot program that allows CBOE to list strike prices at $1 intervals on up to five equity option classes when the underlying stock is trading below $20. The SEC has approved similar rule changes submitted by the other option exchanges. The following is an overview of the rules and procedures for listing $1 strike prices that are applicable at all option exchanges. If you have any questions, please contact Jim Flynn in the Legal Division at (312) 786-7070.

Eligible Option Classes

- Each options exchange can choose 5 equity option classes as part of the $1 Strike Pilot Program.
- An exchange can also list $1 strike price intervals on any class another options exchange selects, but is not required to list $1 strike intervals on another exchange's pick.
- To be eligible, an underlying stock must close below $20 in its primary market on the previous trading day.

Procedures for Adding $1 Strike Prices

- After an option class is added to the $1 Strike Program, an exchange can list $1 strike prices from $3 to $20 that are no more than $5 from the closing price of the underlying security. LEAPS are not eligible for $1 strikes.
- An exchange cannot list $1 strike prices that bracket existing $2.50 intervals (*e.g.*, an exchange cannot list $7 and $8 strike prices around a $7.50 strike).

  - Example. Stock closes $8.00. At expiration, an exchange can list a new month with the following $1 strike prices: 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13. An exchange could also list the $15 and $20 strike prices, as those are not in $1 intervals.

Phasing-Out of 2.5 Strike Price Intervals

- After an option class is added to the $1 Strike Program, an exchange must begin the process of phasing out existing $2.50 intervals below $20 on the same class in favor of $1 strike prices.
- Upon the addition of $1 strikes in an existing series month, an exchange will delist those $2.50 intervals below $20 in which there is no open interest. (If an exchange does not list $1 strikes in a series month in a class that has been added to the Program, it is not required to delist those $2.50 intervals in which there is no open interest.)
- An exchange cannot add $2.50 intervals below $20 in a new expiration month when the existing month expires after an option class is added to the $1 Strike Program.

  - Example. Stock closes at $6.50. At expiration, an exchange can list a new month with the following strike prices: 3, 4, 5, 6, 7, 8, 9, 10, 11. An exchange cannot list the 2.50, 7.50, 12.50 or 17.50 strike prices. An exchange could also list the $15 and $20 strike prices, as those are not in $1 intervals.