CHICAGO BOARD OPTIONS EXCHANGE

Regulatory Circular RG10-102

To: Trading Permit Holders

From: Trading Operations and Legal Divisions

Date: October 4, 2010

Subject: FLEX Third Friday-of-the-Month Expiration Requirements

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A rule change that permits certain FLEX Options to trade under the FLEX trading procedures for a limited time on a closing only basis has recently become effective (see SR-CBOE-2010-078). In light of the recent rule change, CBOE will permit FLEX Options that expire on a third Friday-of-the-month expiration to have American-style exercise (previously only European-style exercise was available).

CBOE is issuing this circular to remind members of the additional requirements that apply to FLEX Options that expire on a third Friday-of-the-month expiration. Trading in FLEX Options that expire on a third Friday-of-the-month is the same as trading in FLEX Options that expire on any other business day, subject to the following additional conditions:

Requirements for FLEX Options Expiring on a Third Friday-of-the-Month Expiration:

- Exercise Style: FLEX Options that expire on a third Friday-of-the-month expiration (or any other business day) may have a European- or American-style exercise.[1]

- Look-Alikes: The following fungibility and trading procedure requirements apply to "look-alike" FLEX and Non-FLEX Options that have a third Friday-of-the-month expiration. As long as the options on an underlying security or index are otherwise eligible for FLEX trading, FLEX Options are permitted in any series that is not already available for trading as a Non-FLEX Options series (i.e., a FLEX Option put (call) series can be listed as long as it does not have the same expiration date, exercise style, and same exercise price as any Non-FLEX Option put (call) series that is already available for trading on the same underlying security or index). In addition, FLEX Options are permitted before the options are listed for trading as Non-FLEX Options. Once and if a "look-alike" option series is listed for trading as a Non-FLEX Options series, (i) all existing options positions established under the FLEX trading procedures will be fully fungible with the transactions in the look-alike Non-FLEX Option series (i.e., the FLEX Option position would convert over to a Non-FLEX Option position); and (ii) any further trading in the series would be as Non-FLEX Options subject to the Non-FLEX trading procedures and rules. However, for American-style options only, in the event a Non-FLEX look-alike series is added intra-day, a position established under the FLEX trading procedures would be permitted to be

[1] European-Capped-style exercises are also permitted. However, the European-Capped-style exercise methodology has not been actively utilized on CBOE. Questions about using this exercise style should be referred to the CFLEX Helpdesk at 312-460-1941.

closed using the FLEX trading procedures for the balance of the trading day on which the Non-FLEX series is added against another closing only FLEX position.[2]

> *Example 1:* Assume that on October 4, 2010 a FLEX Trader establishes a FLEX Option position in a European-style, am-settled SPX 1650 Call option series with an expiration of August 16, 2013 (which would be a third-Friday-of-the-month expiration). In such an instance, once and if the Non-FLEX, European-style, am-settled SPX 1650 Call option series that expires on August 16, 2013 is listed for trading, the established FLEX Option position would be fully fungible with transactions in the Non-FLEX Option series. Any further trading in the series would be as Non-FLEX Options subject to the Non-FLEX trading procedures.

> *Example 2:* Assume that on October 4, 2010 a FLEX Trader establishes a FLEX Option position in an American-style, pm-settled GOOG 485 Call option series with an expiration of August 16, 2013 (which would be a third-Friday-of-the-month expiration). In such an instance, once and if the Non-FLEX, American-style, pm-settled GOOG 485 Call option series that expires on August 16, 2013 is listed for trading, the established FLEX Option position would be fully fungible with transactions in the Non-FLEX Option series. Any further trading in the series would be as Non-FLEX Options subject to the Non-FLEX trading procedures; however, the GOOG position established under the FLEX trading procedures would be permitted to be closed using the FLEX trading procedures for the balance of the trading day on which the Non-FLEX GOOG series is added against another closing only FLEX GOOG position.

- <u>Position & Exercise Limit Aggregation:</u> As long as the options positions remain open, positions in FLEX Options with a third Friday-of-the-month expiration day shall be aggregated with positions in Non-FLEX Options and be subject to the Non-FLEX position limits set forth in Rule 4.11, 24.4, 24.4B or 29.5, as applicable, and the Non-FLEX exercise limits set forth in Rule 4.12, 24.5 or 29.7, as applicable. (FLEX Options that expire on any business day other than a third Friday-of-the-month expiration are subject to the position and exercise limits for FLEX Options set out in Rules 24B.7 and 24B.8, as applicable.)

- <u>Expiration Friday Clarification:</u> As with Non-FLEX Options, any FLEX Options that expire on a third Friday-of-the-month expiration will cease trading on Friday and actually expire on Expiration Saturday in accordance with the OCC Rules. Using the examples above, the FLEX Options that would expire on the third Friday-of-the-month expiration in August 2013 would discontinue trading on Friday, August 16, 2013 and expire on Saturday, August 17, 2013.

- <u>Automatic vs. Ex-by-Ex Procedures for FLEX Index Options:</u> In accordance with the OCC Rules, any FLEX Index Option with an exercise settlement amount of $1.00 or more will be automatically exercised on its expiration date. In comparison, an expiring

[2] For such FLEX series, the FLEX Official will make an announcement that the FLEX series is now restricted to closing transactions; a FLEX Request for Quotes may not be disseminated for any order representing a FLEX series having the same terms as a Non-FLEX series, unless such FLEX Order is a closing order (and it is the day the Non-FLEX series has been added); and only responses that close out an existing FLEX position are permitted. Any transactions in a restricted series that occur that do not conform to these requirements will be nullified by the FLEX Official pursuant to Rule 24B.14.

Non-FLEX Index Option with an exercise settlement amount of $1.00 or more (except quarterly and weekly options) is subject to OCC's "exercise-by-exception" procedures under which the option will be exercised on its expiration date if the option holder does not give contrary exercise instructions. Therefore, please take note that a FLEX Index Option that is converted to a Non-FLEX Index Option (see "Look-Alikes" discussion above) would cease to be subject to the OCC's automatic exercise at expiration and will instead be subject to OCC's exercise-by-exception procedures. For additional information, please refer to OCC Rule Filing No. SR-OCC-2009-05.

For further information on FLEX trading requirements, please refer to Regulatory Circulars RG10-21 and RG10-22 and Chapter XXIVB of the CBOE Rules, which are located at www.cboe.org/legal. Additional questions may be directed to Andy Lowenthal at 312-786-7180, Lisa Morano at 312-786-7319 or Jennifer Lamie at 312-786-7576.

(Replaces Regulatory Circular RG10-23)