SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
MARKET REGULATION

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Mr. James E. Brucki, Jr.
Vice President
Department of Compliance
Chicago Board Options Exchange, Inc.
LaSalle at Jackson
Chicago, Illinois 60604

Dear Mr. Brucki:

This is in response to your letter of October 9, 1974 in which you raised a series of questions regarding the application of 17 CFR Section 240.15c3-3 under the Securities Exchange Act of 1934 ("the Act") as it relates to a broker or dealer effecting transactions in options. With respect thereto, we are providing the following responses in the form of questions and answers.

In this connection for purposes of Section 240.15c3-3:

The term "daily options marking price" means an amount equal to the product of (i) the unit of trading for the series of options of such option contract and (ii) the higher of (a) the closing premium per unit in Exchange transactions pertaining to such series of options on the preceding business day or (b) the current highest asked per unit premium quotation for options of the same series on an Exchange at or about the close of the preceding business day. Notwithstanding the foregoing, the daily options marking price of any options contract may be such higher amount as the Options Clearing Corporation ("OCC") may require.

The term "qualified letter of credit" means: (a) letters of credit issued by banks or trust companies approved by the OCC for the purpose of meeting the margin requirements of the OCC and (1) shall contain the unqualified commitment of the issuer of the letter of credit to pay a specified sum of money to OCC immediately on demand at any time prior to the expiration of the letter of credit, (2) shall expire at 2 p.m. Central Time (3 p.m. Eastern Time) on either the March 1 or September 1 immediately following the issuance thereof, (3) shall be irrevocable except upon the issuer's written notice to OCC of its intent to do so

given not less than two full business days prior to the date fixed for such revocation. In addition to the foregoing, letters of credit described in (a) above, when used as margin at OCC for the customer's account of a broker or dealer maintained with OCC, will not be deemed a qualified letter of credit unless OCC undertakes that it will at no time apply such letters of credit to satisfy other obligations of the broker or dealer to OCC until all claims in the customer's account are first satisfied.

1. Q. Is a broker or dealer who executes all securities and option transactions in accordance with the exemptive provisions of subparagraph (k)(2)(ii) of 17 CFR Section 240.15c3-3 exempt from the provisions of that section?

   A. Yes. Subparagraph (k)(2)(ii) provides that a broker or dealer who introduces and clears all transactions with and for customers on a fully disclosed basis with a clearing broker or dealer, and who promptly transmits all customers' funds and securities received to the clearing broker or dealer who carries the accounts of such customers, may be exempt from the provisions of Section 240.15c3-3. The fact that a broker or dealer introduces option transactions to another broker or dealer on a fully disclosed basis will not of itself preclude the availability of the (k)(2)(ii) exemption for such introducing broker or dealer.

2. Q. Is a broker or dealer who executes all option transactions in accordance with the exemptive provisions of subparagraph (k)(2)(ii) and all other securities transactions in accordance with the exemptive provisions of subparagraph (k)(2)(i) of 17 CFR Section 240.15c3-3 entitled to an exemption from the provisions of Section 240.15c3-3?

   A. Yes. A broker or dealer who introduces only a portion of his securities transactions on a fully disclosed basis to another broker or dealer on a fully disclosed basis may still be exempt from the provisions of 17 CFR Section 240.15c3-3 by subparagraph (k)(2)(ii) if all other transactions are effected in accordance with the provisions of subparagraph (k)(2)(i). In such cases, the broker's or dealer's claim for exemption shall be under subparagraph (k)(2)(i) and not (k)(2)(ii).

3. Q. Are fully paid for long options listed on a registered national securities exchange and held by OCC or carried in a special omnibus account in conformity with Section 4(b) of Regulation T considered to be in the possession or control of the broker or dealer or his correspondent?

A. Yes, except that, with respect to long positions carried in special omnibus accounts, the introducing broker or dealer pursuant to subparagraph (c)(2) of Section 240.15c3-3 is generally required to instruct such carrying broker or dealer to maintain physical possession or control of the long options free of any charge, lien or claim of any kind in favor of such carrying broker or dealer or any persons claiming through such broker or dealer.

4. Q. Are customer fully paid securities deposited as margin with OCC considered to be under the control of the broker or dealer for the purpose of Section 240.15c3-3?

A. (1) Where a customer secures his obligation as a writer with a specific deposit of the security underlying the option, such securities when placed on "Specific Deposit" with OCC are deemed under the control of the broker or dealer within the meaning of subparagraph (c)(1) of Section 240.15c3-3.

(2) Where a customer secures his obligation as a writer with fully paid securities other than the security underlying the option, e.g., Treasury bills or equities, those securities generally may not be subjected to a lien by OCC and thus, may not be the subject of a "bulk deposit" with the OCC and must be within the broker's or dealer's possession or control as required by Section 240.15c3-3. Securities in the OCC bulk deposit account are securities upon which OCC has a lien and are thus not deemed in the control of the broker or dealer.

(3) Where a customer writes an option, the proceeds of his writing transaction are normally included in the customer bulk deposit account at OCC. To the extent the market value of the short option increases, the broker or dealer will be required to deposit additional margin in the customer bulk deposit account to secure the customer's writing obligation. Prior to market movement of the option, the broker or dealer is not financing his customer and, therefore, may not use customers' fully paid securities in the bulk deposit account. However, at such time as the market value of the option increases, the customer will have an obligation to the broker or dealer to the extent the broker or dealer has had margin calls to meet the daily marking price requirements of OCC. It is the Division's view that fully paid for securities, whether Treasury bills or equities, held by the broker or dealer to margin such customer's writing obligations, may be used to the extent of 140% of the amount derived by subtracting from the daily marking price deposits required from the broker or dealer by OCC, the original proceeds of the customer's writing transaction. Customers' securities with a market value in excess of 140% of that amount must be maintained in the possession or control of the broker or dealer.

5. Q. What is the basis upon which a broker or dealer determines whether customer debit balances are secured when the debit balances result from the purchase of listed or conventional options which have not been paid for within seven (7) business days as required by Regulation T?

A. (1) With respect to options listed on a registered national securities exchange, secured debits are those debit balances arising from the purchase of an option until the seventh business day following trade date, or for which a Regulation T extension has been granted. Where no extension has been granted, a secured debit is one for which the market value of the option equals or exceeds the debit balance attributable to the purchase of such option. Where the market value of the option

is less than the debit balance a more than one Regulation T extension has been ..nted, such debit should be excluded from the computation of the Formula for Determination of Reserve Requirements of Brokers and Dealers ("Reserve Formula").

(2) With respect to conventional options which remain unpaid for beyond seven (7) business days from trade date, such debit balances should be excluded from the Reserve Formula computation.

6. Q. Can the market value of U.S. Treasury Bills owned by the broker or dealer and placed in the customer "bulk deposit" account with OCC be included as a debit in the Reserve Formula?

A. The market value of U.S. Treasury Bills owned by the firm and placed in the customer bulk deposit account with the OCC may be included as a debit item in the Reserve Formula to the extent of the daily marking price of all options written in customer accounts. Such daily marking price will also be included as a credit in each such writing customer's account.

7. Q. If a clearing member obtains an irrevocable "Letter of Credit" from a bank which may be drawn down by OCC solely to satisfy obligations of the broker or dealer related to the broker's or dealer's customers' account at OCC, can the amount of the "Letter of Credit" be included as a debit in the Reserve Formula?

A. To the extent a broker or dealer has obtained a "qualified" Letter of Credit, as defined herein, secured by customers' securities which may be used by the broker or dealer in conformity with the requirements of Section 240.15c3-3 (See response to Question 4 above) such "qualified" Letter of Credit may be included as a debit item in the Reserve Formula to the extent of the daily marking price of all options contracts written in customers' accounts. Unsecured or non-qualified letters of credit may not be included as a debit item in the Reserve Formula. We note that at present the

letters of credit approved by OCC are not "qualified" but we understand that OCC will submit appropriate amendments to its rules to qualify such letters of credit. Until such time as those amendments are approved by the Commission, letters of credit may not be included as a debit item in the Reserve Formula.

8. Q. What treatment should a broker or dealer apply to a conventional option, which has been purchased and fully paid for by a customer and forwarded to an endorsing NYSE member and not returned to the broker or dealer carrying the customer's account?

A. Such conventional option contracts should be treated like any other security for purposes of Section 240.15c3-3 and be reduced to possession or control within the time frame called for by subparagraph (d)(1) of Section 240.15c3-3. Since such options are fully paid, there is no effect on the Reserve Formula.

9. Q. Would a member who acts solely as a market maker and/or floor broker be deemed a "customer" for the purpose of Section 240.15c3-3?

A. A member who acts solely as a market maker and/or floor broker is not a "customer" pursuant to Section 240.15c3-3(a)(1).

10. Q. Can funds deposited by a broker or dealer with OCC to meet margin calls for customers be included as a debit in the Reserve Formula?

A. The amount of funds deposited by a broker or dealer with OCC to meet margin calls for customers can be included as a debit in the Reserve Formula to the extent of the daily marking price for all option contracts written in customers' accounts. Such funds include cash, the market value of Treasury bills (discussed in Question 6) and the amount of

"qualified" Letters of Credit (discussed in Question 7) to the extent that there are offsetting credits in customers' accounts.

If you have any further questions, please contact us.

Sincerely,

Nelson S. Kibler
Assistant Director
Broker-Dealer Financial Responsibility
and Securities Transactions