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SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-71764; File No. SR-CBOE-2014-003)

March 21, 2014

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of Proposed Rule Change to List and Trade CBOE Short-Term Volatility Index Options

I. Introduction

On January 27, 2014, the Chicago Board Options Exchange, Incorporated (“Exchange” or “CBOE”) filed with the Securities and Exchange Commission (“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 list options on the CBOE Short-Term Volatility Index (“VXST”). The proposed rule change was published for comment in the Federal Register on February 6, 2014.³ The Commission received no comments on the proposed rule change. This order grants approval of the proposed rule change.

II. Description of the Proposed Rule Change

The Exchange proposes to list and trade A.M. cash-settled, European-style options on the VXST, which will expire every week. According to the Exchange, VXST is designed to measure investors’ consensus view of future (nine day) expected stock market volatility, and VXST options will trade alongside the existing CBOE Volatility Index (“VIX”) options (which

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 71458 (January 31, 2014), 79 FR 7239 (“Notice”).

expire on a monthly basis and measure a 30 day period of implied volatility).⁴ The Exchange states that the calculation of VXST is based on the VIX methodology as applied to option series on the S&P 500 index that expire on every Friday.⁵ The constituent S&P 500 index options that expire on a Friday (i.e., nine days from the VXST option expiration date, which is typically a Wednesday in the preceding week) may include the following types of options on the S&P 500 index: standard monthly options, End-of-Week (“EOW”) expirations, and Quarterly Index (“QIX”) expirations. According to the Exchange, because some of the constituent options used to calculate VXST are A.M.-settled and some are P.M.-settled, the amount of time covered by a specific contract will vary slightly depending on the type of series used for any given A.M.-settled VXST option.⁶

Similar to VIX and VIX options, the cash (spot) VXST value will be calculated using premium quotations and the exercise settlement value for VXST options will be calculated using the actual opening premium prices of the constituent S&P 500 index options on the expiration day of the VXST option.⁷ The Exchange will compute values for VXST on a real-time basis throughout each trading day, from approximately 8:30 a.m. (Chicago time) until approximately

⁴ According to the Exchange, the VXST index was introduced by CBOE on October 1, 2013 and has been disseminated at least once a day on every trading day since that time. See Notice, supra note 3, at 7239-40.

⁵ The Exchange states that VXST is calculated in the same manner as other volatility indexes (e.g., VIX). A more detailed explanation of the method used to calculate the VIX may be found on the CBOE’s website at <http://www.cboe.com/micro/vix/vixwhite.pdf>. See Notice, supra note 3, at 7240.

⁶ For a VXST option contract calculated using A.M.-settled standard S&P 500 index options, the period of implied volatility covered by the contract will be exactly nine days. For a VXST option contract calculated using P.M.-settled EOW or QIX on the S&P 500 index, the period of implied volatility covered by the contract will be nine days, plus 390 minutes. See Notice, supra note 3, at 7240.

⁷ See id.

3:15 p.m. (Chicago time).⁸ VXST levels will be calculated by CBOE and generally disseminated at 15-second intervals to major market data vendors.⁹ The trading hours for VXST options will be from 8:30 a.m. to 3:15 p.m. (Chicago time).¹⁰

The Exchange proposes to list up to 12 near-term VXST option expiration weeks, and that new series will be permitted to be added up to and including on the last day of trading for an expiring VXST option contract.¹¹

As proposed, the exercise settlement value for a VXST option will be calculated on the specific date (usually a Wednesday) identified in the option symbol for the series.¹² If that Wednesday or the Friday in the business week following that Wednesday (i.e., nine days away) is an Exchange holiday, the exercise settlement value will be calculated on the business day immediately preceding the Wednesday.¹³ According to the Exchange, on the day the exercise settlement value is calculated for VXST options, modified Hybrid Opening System (“HOSS”)

⁸ See id.

⁹ According to the Exchange, when VIX options and VXST options expire on the same day, as the calculator of volatility indexes, CBOE would not begin disseminating the spot (cash) values for any volatility index that CBOE calculates until the S&P 500 index option series that CBOE will use to calculate the exercise settlement value for VIX options have opened. On all other VXST option expiration days, as the calculator of volatility indexes, CBOE would not begin disseminating the spot (cash) values for any volatility index that CBOE calculates until the S&P 500 index option series that CBOE will use to calculate the exercise settlement value for VXST options have opened. See id., at n. 8.

¹⁰ See id., at 7241.

¹¹ See CBOE Rules 24.9(a)(2) and 24.9.01(c).

¹² See CBOE Rule 24.9(a)(6). According to the Exchange, option symbols are constructed as follows: Symbol + Expiration Date (Year, Month, Day) + Call or Put + Strike Price (in dollars to three decimal places). See Notice, supra note 3, at n. 14.

¹³ See CBOE Rule 24.9(a)(6).

opening procedures will be used to calculate the exercise settlement value.¹⁴ The exercise settlement value of a VXST option will be calculated by the Exchange as a Special Opening Quotation (“SOQ”) of VXST using the sequence of opening prices of the options that comprise the VXST index.¹⁵ The opening price for any series in which there is no trade will be the average of that option’s bid price and ask price as determined at the opening of trading.¹⁶ The “time to expiration” used to calculate the SOQ will account for the actual number of days and minutes until expiration for the constituent option series.¹⁷

The expiration date of a VXST option will be on the same day that the exercise settlement value of the VXST option is calculated.¹⁸ The last trading day for a VXST option will be the business day immediately preceding the expiration date of the VXST option (typically a Tuesday).¹⁹ When the last trading day is moved because of an Exchange holiday, the last trading day for an expiring VXST option contract will be the day immediately preceding the last regularly scheduled trading day.²⁰ Exercise will result in delivery of cash on the business day following expiration. The exercise-settlement amount will be equal to the difference between the exercise-settlement value and the exercise price of the option, multiplied by \$100.

As proposed, VXST options will be quoted in index points and fractions and one point

¹⁴ See CBOE Rules 6.2B.01 and 6.2B.08. The Exchange states that the main feature of the modified HOSS opening procedures is the strategy order cut-off time for the constituent option series that will be used to calculate the exercise settlement value of a volatility index. See Notice, supra note 3, at n. 15.

¹⁵ See CBOE Rule 24.9(a)(6).

¹⁶ See id.

¹⁷ See id.

¹⁸ See id.

¹⁹ See id.

²⁰ See id.

will equal \$100.²¹ The Exchange proposes that the minimum tick size for series trading below \$3 will be 0.05 (\$5.00) and above \$3 will be 0.10 (\$10.00).²² The Exchange proposes to permit \$0.50 (or greater) strike price intervals for VXST options where the strike price is less than \$75. The Exchange also proposes to permit \$1 (or greater) strike price intervals for VXST options where the strike price is \$200 or less. Further, the Exchange proposes to permit \$5 (or greater) strike price intervals for VXST options where the strike price is greater than \$200.²³

The Exchange does not propose to establish any position or exercise limits for VXST options.²⁴ In addition, the Exchange proposes that VXST options be margined as “broad-based index” options.²⁵ The Exchange notes that, except as modified by this proposed rule change, Chapters I through XIX and Chapter XXIV of its rules will apply to VXST options.²⁶

The Exchange states that it has analyzed its capacity and represents that it believes the Exchange and the Options Price Reporting Authority (“OPRA”) have the necessary systems capacity to handle the additional traffic associated with the listing of new series that will result from the introduction of VXST options.²⁷

²¹ See Notice, supra note 3, at 7240.

²² See id., at 7240-41.

²³ See CBOE Rules 5.5.23 and 24.9.01(i). The Exchange also proposes to make a technical change to CBOE Rule 24.9.12, which permits \$0.50 and \$1 strike price intervals for index options used to calculate volatility indexes. Specifically, the Exchange notes that it proposes to add “and \$150” to the rule text as those two words were inadvertently omitted from the proposed rule text changes to Rule 24.9.12 contained in original rule filing, but were described in detail in the purpose section. See Notice, supra note 3, at 7241 and n. 13.

²⁴ See CBOE Rules 24.4(a) and 24.5. According to the Exchange, VXST options will be subject to the same reporting requirements triggered for other options dealt in on the Exchange. See Notice, supra note 3, at 7242 and CBOE Rule 24.4.03.

²⁵ See CBOE Rules 12.3 and 24.4.04.

²⁶ See Notice, supra note 3, at 7242.

²⁷ See id.

The Exchange represents that it will use the same surveillance procedures currently utilized for its other index options to monitor trading in VXST options, as well as enhanced surveillance procedures at expiration, several of which would be automated.²⁸ The Exchange further represents that these surveillance procedures will be adequate to monitor trading in VXST options.²⁹ The Exchange states that, for surveillance purposes, it will have complete access to information regarding trading activity in the pertinent underlying securities.³⁰

III. Discussion and Commission Findings

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.³¹ Specifically, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,³² which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest. Specifically, the Commission believes that VXST options will provide investors with an additional trading and hedging mechanism. In addition, the Commission believes that the Exchange's proposal with respect to position limits, margin, strike price intervals, minimum trading increments, series openings, exercise limits, and other aspects of the proposed rule change are appropriate and consistent with the Act.

²⁸ See id.

²⁹ See id.

³⁰ See id.

³¹ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

³² 15 U.S.C. 78f(b)(5).

As a national securities exchange, the Exchange is required, under Section 6(b)(1) of the Act,³³ to enforce compliance by its members and persons associated with its members with the provisions of the Act, Commission rules and regulations thereunder, and its own rules. In this regard, the Commission notes that trading of VXST options will be subject to Chapters I through XIX and Chapter XXIV of CBOE rules.³⁴ Moreover, the Exchange has represented that it will use the same surveillance procedures currently utilized for its other index options to monitor trading in VXST options, as well as enhanced surveillance procedures at expiration, several of which would be automated.³⁵ The Exchange has represented that these surveillance procedures will be adequate to monitor trading in VXST options.³⁶ The Exchange also stated that it will have complete access to information regarding trading activity in the pertinent underlying securities.³⁷ In approving the proposed listing and trading of the VXST options, the Commission has also relied on the Exchange's representation that it and the OPRA have the necessary systems capacity to handle the additional traffic associated with the listing of new series that will result from the introduction of VXST options.³⁸

³³ 15 U.S.C. 78f(b)(1).

³⁴ See supra note 26 and accompanying text.

³⁵ See supra note 28 and accompanying text.

³⁶ See supra note 29 and accompanying text.

³⁷ See supra note 30 and accompanying text.

³⁸ See supra note 27 and accompanying text.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,³⁹ that the proposed rule change (SR-CBOE-2014-003) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁰

Kevin M. O'Neill
Deputy Secretary

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³⁹ 15 U.S.C. 78s(b)(2).

⁴⁰ 17 CFR 200.30-3(a)(12).