

SUMMARY OF PROPOSED OPTIONS EXCHANGE BYLAWS & RULES
REGARDING MEMBERSHIP QUALIFICATIONS AND REQUIREMENTS
FOR VARIOUS FORMS OF PARTICIPATION

Qualifications for Membership. Only CBT members are eligible to apply for Class A membership. Any individual, partnership or corporation is eligible to apply for Class B membership. An individual Exchange member may register his membership on behalf of an organization (corporation or partnership) of which he is an officer or partner (subject to the organization meeting the requirements for membership), which will then be deemed a member organization. Conversely, a member organization must designate an executive officer or general partner as its nominee to act for the organization in all matters relating to its Exchange business, and the nominee so designated will have to meet all of the requirements of an individual member. Further, to qualify as a member organization, all general partners in the case of a partnership, and all executive officers, directors, substantial stockholders or other controlling persons in the case of a corporation, must be registered with the Exchange as “approved persons”. No organization will be required to hold (or have registered for it) more than one Exchange membership. However, since only individual members and nominees will be admitted to the floor, some member organizations may wish to obtain additional memberships for the purpose of representation on the floor.

In addition to good character and reputation, applicants for Exchange membership must evidence financial responsibility and must intend to engage in options transactions on the Exchange in a recognized capacity. Applicants must also pledge to adhere to the bylaws and rules of the Exchange. These cover a broad range of members’ activities, including the form of organization of member organizations, financing of members, floor procedures, qualifications

and supervision of personnel, handling of customers' accounts, record keeping and reporting, and the like.

In addition to Exchange regulation, members will be subject to regulation by the SEC. For certain members this may include the necessity of registering with the SEC as a broker-dealer and of becoming a member of the NASD and being subject to regulation by that association. As a member of a national securities exchange, Exchange members will automatically be members of the Securities Investor Protection Corporation (SIPC) and will thereby be subject to certain obligations, including the requirement to make contributions to the SIPC fund. SIPC assessments are based upon the member's gross revenues (so defined as to include the net realized gain on transactions as principal) from the securities business.

Doing Business with the Public. Only member organizations will be able to do business with the public, and in order to do so, they will be required to pay a registration fee of \$3,000 and to obtain special approval after meeting certain higher standards of qualification. Among these are minimum net capital requirements of the greater of \$50,000 or 6 2/3% of aggregate indebtedness, with special reporting requirements if net capital should fall below the greater of \$100,000 or 8 1/3% of aggregate indebtedness. A member organization will only be approved for transacting business with the public if such organization is engaged primarily in the business of a broker or dealer in securities or commodities.

Once registered to do a public business, Exchange members will be subject to Exchange rules governing the handling of customer accounts. Members will be required to screen prospective participants in the options market and will have to "know their customers" through the exercise of due diligence in obtaining relevant facts concerning every options account. This requirement will apply not only to the opening of an account but also to all business handled in

the account, and it will entail the maintaining by members of a special options account card containing information as to the customer's occupation, marital status, investment objectives, financial situation and other related matters. In addition, there will be an Exchange rule governing the appropriateness of recommendations to customers along the lines of the suitability rule appearing in Article III, Section 2, of the NASD's Rules of Practice. The Exchange will also promulgate guidelines to its members designed to give more concrete indications of dividing lines between suitable and unsuitable option investments for various types of customers and various types of option transactions.

Exchange options will be registered under the Securities Act of 1933, and members will be responsible for seeing that their customers have been furnished copies of a current prospectus. Prospectuses will be published by the Exchange Clearing House as issuer of the options, and copies will be made available to all Exchange members for distribution by them to their customers.

Doing Business on the Floor. The Exchange trading floor will be on space leased from the CBT adjacent to the CBT trading floor, permitting dual member firms to use their wire facilities on the CBT floor to handle Exchange orders. The Exchange will be conducted as an auction market, but with several features which distinguish it from existing securities exchanges.

The most striking departure from the procedure of other exchanges will be a separation of the broker and dealer functions that are elsewhere performed conjunctively by a single specialist. On the Exchange floor the brokerage function will be divided among Floor Brokers, whose role will be familiar, and Specialist Brokers, whose role will correspond to the brokerage function of specialists on other securities exchanges. The dealer function on the Exchange floor will be performed by competing Market-Makers, of whom there will be several for each class of

option in which trading is conducted. Their collective role will correspond to the dealer function of specialists on other securities exchanges.

Individual members or nominees of member organizations may apply to the Exchange for registration as Specialist Brokers. The registration process will include the passing of a Specialist Broker examination prescribed by the Exchange. From among those registered, the Exchange will appoint, with their consent, Specialist Brokers to assume responsibility for options on one or more of the securities traded at a given post. In making these appointments, the Exchange will encourage and give special consideration to groups of Specialist Brokers prepared to assume collective responsibility for options on all of the stocks (initially on the order of 10) traded at a particular post. The Specialist Broker's responsibility for execution of orders placed with him, his responsibility for overseeing the performance of Market-Makers in maintaining a fair and orderly market, and other rules and procedures applicable to his function are further discussed in a brochure Doing Business on the Floor of the Chicago Board Options Exchange: An Introduction.

Individual members and nominees of member organizations are also eligible to apply to the Exchange for registration as Market-Makers. An applicant must demonstrate his ability and understanding of the Market-Maker function by passing an examination prescribed by the Exchange, and he must have adequate financial resources to perform the function. Each registered Market-Maker will be appointed by the Exchange, with his consent, to act as such in options on one or more underlying securities. The Exchange will seek to equalize the number of Market-Makers appointed to each option security dealt in.

A Market-Maker will be obligated to engage, to a reasonable degree under the circumstances, in a course of dealings for his own account that is reasonably calculated to

contribute to the maintenance of a fair and orderly market for each option security to which he is appointed. A Market-Maker may also trade in options on other securities so long as his course of dealings so contributes, and he may, in addition, qualify as a Floor Broker, provided that he may not act as both broker and dealer in a particular security during the same trading session.

The obligations of Market-Makers for assisting in the maintenance of a fair and orderly market and other applicable procedures and requirements are further described in the brochure Doing Business on the Floor of the Chicago Board Options Exchange: An Introduction. Clearing Membership. Individual members and member organizations of the Exchange are eligible for clearing membership, but individual members may only clear transactions for their own account. An applicant for clearing membership must satisfy the Board of Directors of the Exchange Clearing House of his or its business integrity, operational capacity and financial responsibility to justify membership. Capital requirements are substantially higher than for any other form of Exchange participation. A further condition of clearing membership is the pledge of an initial, minimum contribution of \$10,000 to a Clearing Indemnification Fund maintained by the Clearing House. The fund will stand behind the Clearing House's obligation to fulfill every option contract entered into on the Exchange. Contributions to the fund may take the form of cash or a deposit of U.S. Government securities. As Exchange activity expands, the size of the indemnification fund will be increased proportionately with resultant increases in contributions that will be prorated among all clearing members on the basis of their respective participations in the Exchange's overall activity. A clearing member's contributions to the fund will be released back to it upon its voluntarily ceasing to be a clearing member.

These and other aspects of clearing on the Exchange are summarized in a brochure, Clearing on the Chicago Board Options Exchange: An Introduction.