Notice of Current Amendment

(March 2022)

This document may be amended from time to time, resulting in the addition, deletion, or modification of content. Each time this document is amended, changes to the content will be incorporated into the document and provided in this chapter.

This chapter will provide details on the changes made to the document with <u>underlined</u> text indicating new text added and ~~strikethrough~~ text indicating text deleted. The substantive changes made to the prior version of this document are below and provide additional language highlighting that index products may have a multiplier other than 100 as established by the listing exchange by providing examples of index options with a one dollar multiplier. Additionally, this chapter includes administrative corrections to chapter subtitles found in the original text of the ODD and updated references to sections in the document.

The following changes are made to accommodate the trading of certain index and index flex options with a one dollar multiplier.

The last full paragraph on page 8 is amended as indicated below.

The contract size of a cash-settled option other than a binary option or a range option is determined by the multiplier that is fixed by the options market on which the options series is traded. The multiplier determines the aggregate value of each point of the difference between the exercise price of the option and the exercise settlement value of the underlying interest. For example, a multiplier of 100 means that for each point by which a cash-settled option is in the money upon exercise, there is a $100 increase in the cash settlement amount. Similarly, if an option with a multiplier of 100 is trading at a premium of, say, $4, then the aggregate premium for a single option contract would be $400. <u>As another example, a multiplier of 1 means that for each point by which a cash-settled option is in the money upon exercise, there is a $1 increase in the cash settlement amount. Similarly, if an option with a multiplier of 1 is trading at a premium of, say, $4, then the aggregate premium for a single option contract would be $4</u>. The contract size of a range option is determined by the option's multiplier and its maximum range exercise value. The contract size of a binary option is its cash settlement amount, which is fixed by the options market for any series of binary options at or before the opening of trading in that series. Some options markets define the cash settlement amount for binary options as being the multiplier times a fixed settlement value. Other options markets define the cash settlement amount for binary options without reference to a multiplier.

The following example is added after the first example on page 9.

<u>EXAMPLE: Assume that a holder of a cash-settled call on the XYZ index that has an exercise price of 80 exercises it when the exercise settlement value of the index is 85. If the multiplier for XYZ index options is 1, the assigned writer would be obligated to pay, and the exercising holder would be entitled to receive, a cash settlement amount of $5 ($85 minus $80 multiplied by 1 = $5).</u>

The Example on page 33 is amended as indicated below.

EXAMPLE: An investor purchases a December 100 index call at $2.15. The multiplier for that option is 100. The aggregate dollar amount of the premium is $215.00 ($2.15 times 100 = $215.00). Had the options market used a multiplier of 200, a premium of $2.15 would have meant an aggregate premium of $430.00. <u>Had the options market used a multiplier of 1, a premium of $2.15 would have meant an aggregate premium of $2.15.</u>

The following example is added after the Example of page 71.

EXAMPLE: A holder of an index put option that settles based on the closing prices of the constituent securities and that has an exercise price of 30 directs his broker to exercise at 10:00 A.M., when the level of the underlying index is 28. If the underlying index stays at that level until the close of trading that day, the holder will be entitled to receive \$2 in settlement (assuming a multiplier of 1). If, however, the index level rises to 32 based on the closing prices of the constituent securities, the holder will be required to pay \$2 to the assigned writer, thereby sustaining a \$2 loss on the exercise.

The last paragraph beginning on page 72 is amended as indicated below.

If a panel delays fixing an exercise settlement value for a series of index options past the last trading day before expiration of that series, normal expiration exercise procedures will not apply to the affected series. Instead, exercise settlement will be postponed until the next business day following the day when the panel fixes the exercise settlement value, and each long position in the affected series will be treated as having been exercised if the exercise settlement amount per contract is equal to or greater than the exercise threshold amount used in normal expiration exercise procedures. For example, for an index option with a multiplier of 100, each long position in the affected series will be treated as having been exercised if the exercise settlement amount per contract for that series is \$1.00 or more, and i. ~~I~~f the exercise settlement amount per contract is less than \$1.00, the option will be treated as having expired unexercised. Similarly, for an index option with a multiplier of 1, each long position in the affected series will be treated as having been exercised if the exercise settlement amount per contract is \$0.01 or more, and if the cash settlement amount per contract is less than \$0.01, the option will be treated as having expired unexercised. As a result of these procedures, holders of expiring index options may not know whether their options have been exercised, and writers of such options may not know whether they have been assigned an exercise notice, until after the expiration date. Investors should contact the listings options market to obtain the exercise threshold amount of the options they trade. A panel's determinations shall be conclusive, binding on all investors, and not subject to review.

The following are administrative changes to correct certain references to chapter subtitles contained in the original ODD text and to update sections or references to sections in the document.

References to "paragraph" and "paragraphs" that are numbered are changed to "numbered section" and "numbered sections" throughout the document.

The following sub-header is deleted from the bottom of page 19.

~~All Stock Options~~

The following change is made to the fourth paragraph on page 44 of the document.

The principal risks of holders and writers of foreign currency options are discussed in Chapter X. Readers interested in buying or writing foreign currency options should not only read this chapter but should also carefully read Chapter X, particularly the discussions under the headings "Risks of Option Holders," "Risks of Option ~~Buyers~~ Writers," "Other Risks," and "Special Risks of Foreign Currency Options."

The following change is made to the last paragraph on beginning on page 47 of the document.

Investors in cross-rate options should bear in mind that the magnitude and direction of any change in the value of the underlying currency in relation to the trading currency may be quite different from the magnitude and direction of any contemporaneous change in the value of either of those currencies in relation to a third currency, such as the U.S. dollar. Thus, for example, the British pound may appreciate in relation to the Japanese yen at the same time that the pound depreciates in relation to the U.S. dollar. As discussed in Chapter X under "Special Risks of Foreign Currency ~~Cross-Rate~~ Options," this is of particular significance to investors who intend to convert their profits or losses on cross-rate options into U.S. dollars.

The following change is made to the first paragraph after the first Example on page 48 of the document.

The discussion in this chapter of adjustments under the caption "Special Features of Dollar Denominated Foreign Currency Options" is applicable also to cross-rate options, except that adjustments in the terms of cross-rate options might be made to reflect events affecting the trading currency as well as events affecting the underlying currency.

The following change is made to the numbered section 7 on page 65 of the document.

7. Since the leverage inherent in an option can cause the impact of price changes in the underlying interest to be magnified in the price of the option, a writer of an option that is uncovered and unhedged may have a significantly greater risk than a short seller of the underlying interest. This is illustrated by the table set forth in ~~paragraph 2~~ numbered section 1 under "Risks of Option Holders" above. If an investor had sold short 100 shares of XYZ to Investor A in that table in order to receive $5,000 in proceeds, the investor would have lost $1,200 if the market price of XYZ had increased to 62. On the other hand, if, in order to receive $5,000 in proceeds, the investor had written 10 XYZ 50 uncovered calls, she would have lost $7,000 if the market price of XYZ had increased to 62.

List of Supplements

The list below provides prior supplements incorporated into the 1994 version of *Characteristics and Risks of Standardized Options* (also known as the "Options Disclosure Document" or "ODD"). A summary of each supplement is included, along with a description of the October 2021 version of the ODD.

December 1997—Supplement accommodated cash settled options on indexes of mutual funds.

March 2000—Supplement permitted (i) the acceleration of exercise of options when the underlying security has been converted into the right to receive a fixed amount of cash; and (ii) the automatic exercise of in-the-money flexibly structured index options on the expiration date.

January 2004—Supplement (i) permitted greater flexibility in the methods used for assigning options exercises; and (ii) addressed special considerations with respect to deadlines for the exercise of certain options that expire on a day on which an options market is open for trading.

April 2007—Supplement accommodated non-rate modified cash-settled foreign currency options and rate-modified cash-settled foreign currency options.

May 2007—Supplement (i) reflected modifications made to the definition of "ordinary cash dividend or distribution; (ii) reflected changes made to eliminate the need to round adjusted exercise prices in certain circumstances and to provide more precise compensation for fractional shares eliminated by rounding; (iii) accommodated options on interests in investment companies and similar entities; (iv) addressed special exercise settlement procedures or restrictions that may be imposed upon the occurrence of certain extraordinary events; (v) disclosed that a registration statement and prospectus for the options covered by the ODD are no longer available; (vi) explained OCC's authority to adjust the multiplier for yield-based treasury options and to fix a cash settlement amount for such options in certain circumstances; (vii) addressed the adoption of rules by certain options markets that permit, in very limited circumstances, the cancellation or adjustment of a transaction entered into at a premium based on an erroneously reported value for the underlying interest; and (viii) addressed acceleration of the expiration date of options on equity securities in certain circumstances.

June 2007—Supplement accommodated credit default options. This supplement was amended and restated in its entirety by the January 2011 Supplement.

June 2008—Supplement accommodated delayed start options, binary stock options, binary index options and range options.

December 2009—Supplement (i) accommodated options on variability indexes, strategy-based indexes and dividend indexes; and (ii) addressed adjustment of stock option contracts to reflect cash dividends or distributions on the underlying securities.

May 2010—Supplement accommodated options on index-linked securities.

January 2011—Supplement accommodated credit default options.

March 2011—Supplement accommodated options on any single security volatility index and options on relative performance indexes.

January 2012—Supplement accommodated options on relative performance indexes of which the index components are equity securities (including fund shares).

November 2012—Supplement accommodated the introduction of options originally listed to overlie less than 100 shares.

April 2015—Supplement accommodated the introduction of options on foreign currency indexes and the introduction of implied volatility options whose exercise settlement value is calculated differently than that of existing implied volatility options. This supplement was amended and restated in its entirety by the October 2018 Supplement.

October 2018—Supplement (i) accommodated the introduction of options on foreign currency indexes and the introduction of implied volatility options whose exercise settlement value is calculated differently from other existing implied volatility options, (ii) addressed certain aspects of contract adjustments related to the OCC's authority to determine contract adjustments and how certain adjustments may affect an option's value, and (iii) addressed the change in the regular settlement for option exercises to the second business date following exercise.

October 2021 (ODD Restatement and Supplement)—The October 2021 version of the ODD incorporates all prior supplements into the 1994 version of the document. It also (i) updates exchange information, (ii) removes references to options trading on foreign markets, (iii) adds language indicating not all products described in the ODD may trade at any given time, (iv) modifies or removed obsolete language such as references to currencies that no longer exist, methods of obtaining index closing prices and private quotations, market wide trading halts and the prohibition of buying options on credit, (v) removes all references to an OCC Prospectus, (vi) removes the contract methodology was only in effective for special dividends announced before February 1, 2009, and (vii) removes all references to fractional strike prices. This consolidated version of the ODD also includes supplemental material to accommodate the introduction of a third type of implied volatility option with an exercise settlement value that is calculated differently from other existing implied volatility options.

March 2022—The March 2022 version (i) adds language highlighting that index products may have a multiplier other than 100 as established by the listing exchange by providing examples of index options with a one dollar multiplier and (ii) includes 2022 ODD administrative corrections to chapter subtitles found in the original text of the ODD.