given time. Specifically, there may be up to three expiration months from the March, June, September, and December cycle plus up to three additional near-term months so that the two nearest term months will always be available. As described in more detail below, the Exchange also intends to list several Index LEAPS series that expire from 12 to 36 months from the date of issuance.[26]

Lastly, the options on the Index will expire on the Saturday following the third Friday of the expiration month (''Expiration Friday''). Accordingly, because options on the Index will settle based upon opening prices of the closed-end fund securities comprising the Index on the last trading day before expiration (normally Expiration Friday), the last trading day for an expiring Index option series will normally be the second to the last business day before expiration (normally a Thursday).

G. Listing of Long-Term Options on the Full-Value or Reduced-Value Emerging Markets Index

The proposal proves that the Exchange may list long-term Index options that expire from 12 to 36 months from listing based on the full-value Index or a reduced-value Index that will be computed at one-tenth of the full-value Emerging Markets Index.[27] Existing Exchange requirements applicable to full-value Index options will apply to full-value and reduced-value Index LEAPS.[28] The current and closing Index value for reduced-value Emerging Markets LEAPS will be computed by dividing the value of the full-value Index by 10 and rounding the resulting figure to the nearest one-hundredth. For example, an Index value of 125.46 would be 12.55 for the reduced-value Index LEAPS and an Index value of 125.44 would be 12.54 for the reduced-value Index LEAPS. The reduced-value Index LEAPS will also be European-style and will be subject to the same rules that govern the trading of Index options, including sales practice rules, margin requirements and floor trading procedures. Pursuant to CBOE Rule 24.9, the strike price interval for the reduced-value Index LEAPS will be no less than $2.50 instead of $5.00.

H. Position and Exercise Limits, Margin Requirements, and Trading Halts

Exchange rules governing margin requirements,[29] position and exercise limits,[30] and trading halt procedures [31] that are applicable to the trading of narrow-based index options will apply to options traded on the Index. The proposal further provides that, for purposes of determining whether given positions in full-value and reduced-value Index LEAPS comply with applicable position and exercise limits, positions in full-value and reduced-value Index LEAPS will be aggregated with positions in the regular Index options. For these purposes, ten reduced-value contracts will equal one full-value contract.

I. Surveillance

Surveillance procedures currently used to monitor trading in each of the Exchange's other index options will also be used to monitor trading in regular Index options and in full-value and reduced-value Index LEAPS. These procedures include complete access to trading activity in the shares of the mutual funds comprising the Index. Further, the Intermarket Surveillance Group Agreement will be applicable to the trading of options on the Index.[32]

III. Findings and Conclusions

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 and, in particular, the requirements of Section 6(b)(5).[33] Specifically, the Commission finds that the trading of Emerging Markets Index options, including full-value and reduced-value Index LEAPS, will serve to promote the public interest and help to remove impediments to a free and open securities market by providing investors with a means of hedging exposure to market risk associated with emerging Asian and Latin American market securities.[34]

The trading of options on the Emerging Markets Index, including full-value and reduced-value Index LEAPS, however raises several issues related to index design, customer protection, surveillance, and market impact. The Commission believes, for the reasons discussed below, that the CBOE has adequately addressed these issues.

A. Index Design and Structure

The Commission finds that it is appropriate to treat the Emerging Markets Index as a narrow-based index under CBOE rules for purposes of applicable position and exercise limits, trading halt and suspension procedures, and margin treatment. Although the closed-end funds represented in the Index, in aggregate, hold in excess of 270 individual Asian and Latin American market securities,[35] the Emerging Markets Index is composed of securities representing only 23 closed-end mutual funds.[36] Accordingly, in light of the number of closed-end fund securities contained in the Index, the Commission believes it is proper to treat the Emerging Markets Index as narrow-

[26] See *supra* note 8.

[27] *Id.*

[28] See CBOE Rule 24.9(b).

[29] Pursuant to CBOE Rule 24.11, the margin requirements for the Index options will be: (1) for short options positions, 100% of the current market value of the options contract plus 20% of the underlying aggregate Index value, less any out-of-the-money amount, with a minimum requirement of the options premium plus 10% of the underlying Index value; and (2) for long options positions, 100% of the options premium paid.

[30] Pursuant to CBOE Rules 24.4A and 24.5, respectively, the position and exercise limits for the Index options will be 10,500 contracts, unless the Exchange determines, pursuant to such rules, that a lower limit is warranted.

[31] Pursuant to CBOE Rule 24.7, the trading on the CBOE of Index options and Index LEAPS may be halted or suspended whenever trading in underlying mutual fund shares whose weighted value represents more than 20% of the Index value are halted or suspended.

[32] The Intermarket Surveillance Group (''ISG'') was formed on July 14, 1983 to, among other things, coordinate more effectively surveillance and investigative information sharing arrangements in the stock and options market. *See* Intermarket Surveillance Group Agreement, July 14, 1983. The most recent amendment to the ISG Agreement, which incorporates the original agreement and all amendments made thereafter, was signed by ISG members on January 29, 1990. *See* Second Amendment to the Intermarket Surveillance Group Agreement, January 29, 1990. The members of the ISG are: the Amex; the Boston Stock Exchange, Inc.; the CBOE; the Chicago Stock Exchange, Inc.; the National Association of Securities Dealers, Inc. (''NASD''); the NYSE; the Pacific Stock Exchange, Inc.; and the Philadelphia Stock Exchange, Inc. Because of potential opportunities for trading abuses involving stock index features, stock options, and the underlying stock and the need for greater sharing of surveillance information for these potential intermarket trading abuses, the major stock index features exchanges (*e.g.*, the Chicago Mercantile Exchange and the Chicago Board of Trade) joined the ISG as affiliate members in 1990.

[33] 15 U.S.C. 78f(b)(5) (1988).

[34] Pursuant to Section 6(b)(5) of the Act, the Commission must predicate approval of any new option proposal upon a finding that the introduction of such new derivative instrument is in the public interest. Such a finding would be difficult for a derivative instrument that served no hedging or other economic function because any benefits that might be derived by market participants likely would be outweighed by the potential for manipulation, diminished public confidence in the integrity of the markets, and other valid regulatory concerns. In this regard, the trading of listed Index options and full-value and reduced-value Index LEAPS will provide investors with a hedging vehicle that should reflect the overall movement of Asian and Latin American market securities, excluding Japanese securities, represented through the holdings of closed-end mutual funds traded in the U.S.

[35] See August 16 Letter, *supra* note 12.

[36] The narrow-based Emerging Markets Index, which consists of the same component mutual fund components as the Index and is calculated by dividing the Index value by ten, is identical to the Emerging Markets Index.