

## CBOE Regulatory Circular RG14-035 C2 Regulatory Circular RG14-012

**Date:** March 17, 2014

**To:** CBOE, C2, and CBSX Trading Permit Holders  
**From:** Regulatory Services Division  
**RE:** Approval of Rule 4.24 – *Supervision*

On March 4, 2014, the Securities and Exchange Commission (“SEC”) approved Chicago Board Options Exchange, Incorporated (“CBOE”) Rule 4.24 - *Supervision*<sup>1</sup> that requires each Trading Permit Holder (“TPH”) to establish and maintain a system to supervise each of its business activities and the activities of its associated persons. Rule 4.24 enacts more definitive supervision requirements on TPHs than previously existed under the Exchange’s general supervision rule (CBOE Rule 4.2 - *Adherence to Law*)<sup>2</sup>.

A summary of certain aspects of the new rule follows. Please refer to Rule 4.24, Rule Filing SR-CBOE-2013-126 and the SEC approval order (Release 34-71644) for additional information. These materials are available on CBOE’s website at [www.cboe.com/legal](http://www.cboe.com/legal).

### Key Points:

- The rule requires each office, location, department, business activity, trading system, and internal surveillance system of a TPH to be under the supervision and control of the TPH establishing it and of an appropriately qualified supervisor (as described in the rule). Each TPH and associated person of a TPH must also be under the supervision and control of an appropriately qualified supervisor (as described in the rule).
- The general partners or directors of each TPH shall provide for appropriate supervisory control and must designate a general partner or principal executive officer to assume overall authority and responsibility for internal supervision and control of the organization and compliance with applicable securities laws and regulations, and with applicable Exchange rules.
- The designated general partner or principal executive officer shall: 1) delegate to qualified principals responsibility and authority for supervision and control of each office, location, department, business activity, trading system, and internal surveillance system and provide for appropriate written procedures of supervision and control; and 2) establish a separate system of follow-up and review to determine that the delegated authority and responsibility is being properly exercised.
- Each TPH must make reasonable efforts to determine that each person with supervisory control is qualified by virtue of experience or training to carry out his or her assigned responsibilities, including meeting the Exchange’s qualification requirements for supervisors, including completion of the appropriate examination(s) (e.g., CBOE Rule 3.6A or C2 Rule 3.4).

<sup>1</sup> CBOE Rule 4.24 is incorporated into Chapter 4 of the C2 Options Exchange, Incorporated (“C2”) Rules and Appendix A of the CBOE Stock Exchange, LLC (“CBSX,” a facility of CBOE) Rules. References to the “Exchange” in this circular mean CBOE, C2 or CBSX, as applicable.

<sup>2</sup> CBOE Rule 4.2 is incorporated into Chapter 4 of the C2 Rules and Appendix A of the CBSX Rules.

- Each person with supervisory control shall reasonably discharge his or her duties and obligations in connection with such supervision and control in order to prevent and detect violations of applicable securities laws and regulations, and applicable Exchange rules.
- Each TPH shall establish, maintain, and enforce written supervisory procedures (“WSPs”), and a system for applying such procedures, to supervise the types of business in which the TPH engages and to supervise the activities of all associated persons (as further detailed in the rule).

At a minimum, the Exchange expects a TPH’s WSPs to address general rules applicable to all TPHs (e.g., qualifications and registration, fingerprinting, etc.), as well as those rules applicable to the types of business activities in which the TPH engages. For example, TPHs with a market-making business are expected to address rules applicable to market-makers (e.g., appointments, market-maker obligations, etc.), while TPHs providing floor brokerage services are expected to address rules applicable to floor brokers (e.g., due diligence, error accounts, etc.).

- Each TPH is required to inspect every office or location of the TPH at least once every three calendar years (as further detailed in the rule). In establishing the inspection cycle, the TPH shall give consideration to the nature and complexity of the securities activities for which the office or location is responsible, the volume of business done, and the number of associated persons at each office or location. The examination schedule and an explanation of the factors considered in determining the frequency of the examinations in the cycle shall be set forth in the TPH’s WSPs.

#### **Annual Compliance Report and Certification:**

In addition, Rule 4.24(g)(2) requires each TPH to prepare a written report on the TPH’s supervision and compliance efforts during the preceding year and on the adequacy of the TPH’s ongoing compliance process and procedures. TPHs are required to file this report (and accompanying certification signed by the TPH’s Chief Executive Officer or equivalent officer) by April 1<sup>st</sup> of each year.

**Due to the recent implementation of Rule 4.24, the Exchange will require that TPHs file their first report required by Rule 4.24(g)(2) by April 1, 2015. All other aspects of this rule are effective immediately.**

Those TPHs that are approved to conduct a non-TPH customer business are still required to file the annual report and certifications required under CBOE Rule 9.8 –*Supervision of Accounts*<sup>3</sup> by April 1, 2014.

#### **Additional Information:**

Please contact Regulatory Interpretations and Guidance at [RegInterps@cboe.com](mailto:RegInterps@cboe.com) or (312) 786-8141 for additional information.

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<sup>3</sup> CBOE Rule 9.8 is incorporated into Chapter 9 of the C2 Rules and Rule 54.6 of the CBSX Rules.