

## **LONDON NOTICE No. 3069**

ISSUE DATE: 4 September 2008  
EFFECTIVE DATE: 5 September 2008

### **BCLEAR IN THE UNITED STATES**

### **REVISED DISCLOSURE DOCUMENT**

#### **Executive Summary**

This Notice informs Members that, on and from Friday 5 September 2008, contracts in certain UK Equity and UK Index Options may be reported via Bclear by or on behalf of “Qualified Broker-Dealers” and “Qualified Institutions” in the United States. It also provides Members with a revised Disclosure Document reflecting this change.

#### **1. Introduction**

- 1.1 Members are advised that, on and from 5 September 2008, OTC Trades in respect of certain UK Equity and UK Index Options may be reported for confirmation, administration and clearing via Bclear by or on behalf of a person located in the United States but only if that person is a Qualified Broker-Dealer or a Qualified Institution, acting for its own account or the accounts of other Qualified Broker-Dealers or Qualified Institutions or managed accounts of non-US persons within the meaning of Rule 902(k)(2)(i) of Regulation S under the US Securities Act of 1933 (“the Act”).
- 1.2 To be Qualified, each such entity must have had prior actual experience in the US domestic options markets. In addition, such entities must meet qualifications as a “qualified institutional buyer” under Rule 144A of the US Securities and Exchange Commission (“SEC”) or as an entity excluded from the definition of “US person” by Rule 902(k)(2)(vi) of Regulation S of the Act.
- 1.3 The definitional qualification means, in general, that a Qualified Broker-Dealer must be registered as such with the SEC and must in the aggregate own and invest on a discretionary basis at least \$10 million of securities (as defined and provided in Rule 144A). A Qualified Institution must come within the categories of non-broker-dealer entities defined as qualified institutional buyers in Rule 144A and must in the aggregate own and invest on a discretionary basis at least \$100 million in securities (as defined and provided in Rule 144A). Alternatively, a Qualified Institution must, as provided in Rule 902(k)(2)(vi) of Regulation S under the Act, be a specified international organisation.

Web site: [www.nyx.com/liffe](http://www.nyx.com/liffe)

The **Euronext Derivatives Markets (“Liffe”)** comprise the markets for derivatives operated by Euronext Amsterdam, Euronext Brussels, Euronext Lisbon, Euronext Paris and LIFFE Administration and Management, referred to respectively as the Amsterdam, Brussels, Lisbon, Paris and London markets. Euronext is part of the NYSE Euronext group.

- 1.4 Members should refer to General Notice No. 436, issued on 16 June 1992, for a fuller description of the arrangements for dealing with US persons in respect of UK Individual Equity Options and Index Options, albeit that references to “orders” therein do not apply, on the basis that the Bclear service involves the reporting of OTC Trades to the Exchange for confirmation, administration and clearing.
- 1.5 In accordance with General Notice No. 436, Members must ensure that Qualified Broker-Dealers and Qualified Institutions have, amongst other things, received the LIFFE Disclosure Document prior to their OTC Trades being submitted to Bclear (i.e. submitted either by or on behalf of such entities) and that the Member has completed and returned Form SEC A to the Membership Department at LIFFE. A revised Disclosure Document and Form SEC A are attached as Attachment 1 and 2 respectively.
- 1.6 Indeed, all Members who transact UK Equity and UK Index Options on behalf of Qualified Broker-Dealers and Qualified Institutions are required to send such entities the updated Disclosure Document even where such business is to be transacted through LIFFE CONNECT® rather than submitted via Bclear.
- 1.7 Access to Bclear will be provided via Members and will include the intermediated non-Member access functionality described in London Circular No. 06/11, issued on 9 May 2006.

## **2. Contract details**

- 2.1 On and from Friday 5 September 2008, OTC Trades in the following Contracts, involving the US persons mentioned in Section 1 of this Notice, may now be reported via Bclear:
- (a) UK Equity Option Contracts and UK Flexible Equity Option Contracts under the terms of Exchange Contract No. 201 and Exchange Contract 201F respectively;
  - (b) for the purposes of UK Stock Contingent Trades, Equity Share Contracts under the terms of Exchange Contract No. 211; and
  - (c) UK Index Option Contracts and UK Flexible Index Option Contracts under the terms of Exchange Contract No. 129E and Exchange Contract No. 129F respectively (i.e., those based on the FTSE 100 Index),

where such Contracts appear on the List of Approved Options for Sale to US Entities (“the List of Approved Options”).

- 2.2 Contract Details in respect of Exchange Contracts No. 201, No. 201F, No. 129E and 129F, and the List of Approved Options, are available in the London Market Handbook on the Liffe website ([www.nyx.com/londonhandbook](http://www.nyx.com/londonhandbook)).

## **3. Additional Information**

- 3.1 Additional information about Bclear can be found on the Liffe website at the following address: [www.nyx.com/bclear](http://www.nyx.com/bclear).

For further information in relation to this Notice, Members should contact:

Equity Product Management

+44 (0)20 7379 2200

[equities@liffe.com](mailto:equities@liffe.com)

**Special Characteristics and Risks of  
LIFFE Options on Equities and Stock  
Indices**

For Limited Distribution in the United States Only to Qualified Broker-Dealers  
and Qualified Institutions

LIFFE Administration and Management  
10<sup>th</sup> Floor,  
20 Broad Street,  
New York

Registered office:  
Cannon Bridge House  
1 Cousin Lane  
London EC4R 3XX  
United Kingdom

September 2008

This document is intended for distribution only to “Qualified Broker-Dealers” and “Qualified Institutions” in the United States. To be Qualified each such entity must have had prior actual experience in the US domestic options markets. In addition, such entities must meet the same qualifications as a “qualified institutional buyer” under Rule 144A of the US Securities and Exchange Commission (“SEC”) or as an entity excluded from the definition of “US person” by Rule 902(k)(2)(vi) of Regulation S of the US Securities Act of 1933 (the “Act”).

The definitional qualification means, in general, that a Qualified Broker-Dealer must be registered as such with the SEC and must in the aggregate own and invest on a discretionary basis at least \$10 million of securities (as defined and provided in Rule 144A). A Qualified Institution must come within the categories of non-broker-dealer entities defined as qualified institutional buyers in Rule 144A and must in the aggregate own and invest on a discretionary basis at least \$100 million in securities (as defined and provided in Rule 144A). Alternatively, a Qualified Institution must, as provided in Rule 902(k)(2)(vi) of Regulation S under the Act, be a specified international organisation.

Members of The London International Financial Futures and Options Exchange (“LIFFE”) will be advised that they may execute opening options transactions with or for a person located in the United States only if that person is a Qualified Broker-Dealer or a Qualified Institution, acting for its own account or the accounts of other Qualified Broker-Dealers or Qualified Institutions or managed accounts of non-US persons within the meaning of Rule 902(k)(2)(i) of Regulation S under the Act. Appropriate documentation will be required for this purpose.

LIFFE is governed by rules and trading procedures which are contained in a Rule Book and Trading Procedures Manual. LIFFE’s clearing house, LCH.Clearnet Limited (“LCH.Clearnet”) clears transactions made on LIFFE in accordance with its General Regulations, Default Rules and Procedures. Copies of the Rule Book and Trading Procedures Manual and LCH.Clearnet’s General Regulations, Default Rules and Procedures are available for inspection at the representative office of LIFFE Administration and Management in New York City. The address is 10<sup>th</sup> Floor, 20 Broad Street, New York, 10005. The most recently published annual report of NYSE Euronext, which is the company that owns LIFFE A&M, and the most recently published report of LCH.Clearnet will also be obtainable from that office. A representative in the office will be available to Qualified Broker-Dealers and Qualified Institutions during normal business hours in New York to respond to inquiries of a general or specific nature concerning LIFFE, but not to give advice or receive or direct orders concerning options traded on LIFFE.

This document describes the arrangements for trading, clearing and settling LIFFE Options on equities and stock indices in the normal course of business. In addition, LIFFE, LCH.Clearnet Limited and Euroclear UK and Ireland Limited (the operator of the CREST settlement system) have powers for dealing with emergency situations. These are set out in their respective rule books.

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LIFFE options have not been registered under the US Securities Act of 1933 or any State securities law. Neither the options nor this document have been approved or disapproved by the SEC or any State securities commission. This document is not a solicitation of orders for transactions on LIFFE, nor does it constitute investment advice.

## INTRODUCTION

The London International Financial Futures and Options Exchange (“LIFFE”) is one of the largest financial and equity derivatives markets in the world. Equity and Index Options have been available for trading on LIFFE since March 23, 1992, following the merger of LIFFE with the London Traded Options Market (“LTOM”). LIFFE has been operating since September 1982 while LTOM opened in April 1978 as a market administered by the London Stock Exchange. LIFFE is operated by LIFFE Administration and Management (“LIFFE A&M” or “the Exchange”), a wholly-owned subsidiary of LIFFE (Holdings) plc.

LIFFE (Holdings) plc is ultimately owned by NYSE Euronext.

LIFFE A&M is a Recognised Investment Exchange (“RIE”) under the Financial Services and Markets Act 2000. Recognition as an RIE has been granted to LIFFE A&M by the Financial Services Authority (the “FSA”), the designated agency under the Financial Services and Markets Act 2000. LIFFE A&M operates a central order book and wholesale trading facilities through the LIFFE CONNECT<sup>®</sup> electronic trading platform as “trading services”, subject to the oversight of the FSA. In addition, more recently LIFFE A&M has launched Bclear as a “clearing service” which is also subject to FSA oversight.

Transactions effected through LIFFE CONNECT<sup>®</sup> are conducted on-exchange. In relation to Bclear, transactions are conducted off-exchange and are then brought to LIFFE A&M for trade confirmation, administration and clearing pursuant to the Rules of the London International Financial Futures and Options Exchange, as interpreted or implemented by Notices (the “LIFFE Rules”). Once LIFFE A&M has confirmed a transaction which has been reported via Bclear,<sup>1</sup> such transaction is replaced by novation by LIFFE Contract which is a legal contract in standard terms issued by LIFFE A&M and subject to LIFFE Rules.

Two basic types of options are referred to in this document: LIFFE options on individual stocks that are traded on the London Stock Exchange (“UK Equity Options”) and LIFFE options on stock indices (“Index Options”). LIFFE’s Index Options currently comprise standardized and flexible options on the FTSE 100 Index (“UK Index Options”). Options on other types of underlying stocks or stock indices may be made available in the future to US Entities to whom this document is made available.

UK Equity Options and UK Index Options are available for trading within LIFFE CONNECT<sup>®</sup> and are also capable of being reported via Bclear.

UK Equity Options are currently available for trading on LIFFE CONNECT<sup>®</sup> between the hours of 8.00am and 4.30pm London time on UK business days. The standardized FTSE 100 Index Options are currently available for trading on LIFFE CONNECT<sup>®</sup> between the hours of 8:02am and 4:30pm London time. (Trading hours may be changed from time to time.) Bclear reporting hours for standardized and flexible UK

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<sup>1</sup> References in this document to transactions “reported” via Bclear should be read in the context of applicable LIFFE Rules, where such term refers to the notification of an existing off-exchange transaction. Such term does not refer to the reporting of transactions as used in the United States.

Equity Options and standardized and flexible FTSE 100 Index Options are currently 8:00am and 5:00pm London time.

All transactions creating or closing positions in such options are executed and settled in London by members of LIFFE. LIFFE options are dematerialised (certificateless) transactions and positions are evidenced by statements from LCH.Clearnet to LIFFE clearing members and advices and statements by members to clients (customers).

Prices on LIFFE CONNECT<sup>®</sup> for UK Equity and UK Index Options are publicly quoted through quote vendors. All UK Equity Options and UK Index Options are bought and sold in the same currency as the underlying securities (usually British pounds sterling). UK Equity Options and UK Index Options are not fungible or interchangeable with options that are traded on any other market. Thus, any UK Equity and UK Index Options position registered with LCH.Clearnet by a clearing member of the Exchange can be closed only by executing an equal and opposite transaction on LIFFE CONNECT<sup>®</sup> or submitting an equal and opposite transaction through Bclear or exercised by the clearing member giving an Exercise Notice to LCH.Clearnet.

The purpose of this document is to introduce experienced and sophisticated US registered broker-dealers and large US institutions to the special aspects, requirements and risks involved in trading UK Equity Options and UK Index Options. The potential risks which apply generally to all aspects of options transactions are assumed to be known to readers of this document. Accordingly, such entities considering LIFFE should have had actual prior experience in options investment in US markets and therefore be familiar with the risks of all options investments and American-style and European-style options.

This document does not suggest or recommend any types of investment strategy. It is limited to a descriptive overview of:

- (a) LIFFE CONNECT<sup>®</sup> and Bclear;
- (b) the foreign options transactions that may be effected through each of those services and the risks peculiar to such foreign options transactions; and
- (c) the post-trade processing, central counterparty and settlement arrangements applicable to such foreign options transactions (these are the same for all LIFFE options, whether they have been effected through LIFFE CONNECT<sup>®</sup> or Bclear).

The Exchange has developed and lists a range of futures and options on futures related to money market and fixed interest rate instruments, commodities and individual stock and stock index futures, which fall outside the scope of this document.

## TRADING FACILITIES AND THE BCLEAR SERVICE

This section describes LIFFE's trading facilities (i.e. LIFFE CONNECT<sup>®</sup>) and its clearing service, Bclear.

### *LIFFE CONNECT<sup>®</sup>*

On 30 November 1998, trading in LIFFE's UK Equity Options migrated from the Exchange's trading floor in the City of London to LIFFE's automated trading platform, LIFFE CONNECT<sup>®</sup>. LIFFE's standardized FTSE 100 Index Options migrated to LIFFE CONNECT<sup>®</sup> on 2 May 2000.

LIFFE currently makes available for trading on LIFFE CONNECT<sup>®</sup> UK Equity Option contracts on approximately 90 equity securities of large UK companies as well as Index Option contracts on the FTSE 100 Index. In 2007, daily trading volume of Equity Option contracts averaged 19,565 compared with 22,698 during 2006. In relation to standardized FTSE 100 Index Option contracts, the average daily trading volume in 2007 was 30,092 compared with 26,283 in 2006.<sup>2</sup> At the end of 2007, aggregate open interest for all UK Equity Options was 5,911,852 and for standardized FTSE 100 Options was 2,541,711. At the end of 2006, the comparable figure for UK Equity Options was 3,080,466 and for standardized FTSE 100 Index Options was 2,369,771.<sup>3</sup>

The LIFFE CONNECT<sup>®</sup> central order book operates in an anonymous, order-driven environment with orders being matched by the LIFFE CONNECT<sup>®</sup> Trading Host according to the algorithm specified in the Trading Procedures. In order to participate in the market, members require a Trading Application which links to the Trading Host. Some members have developed their own bespoke trading applications, whilst others use systems developed or provided by third party software vendors.

Trading of Equity and Index Options on LIFFE CONNECT<sup>®</sup> is conducted by members who hold the appropriate trading rights, who have one or more "responsible persons" registered to them, and who meet other conditions which the Exchange may prescribe. Responsible persons are required to meet requirements stipulated by the Exchange. All orders are submitted under the user name of a responsible person. Each responsible person is required to have the authority to adjust or withdraw any order, whether from clients or from colleagues within the same firm, which is submitted to the market under his user name. Members are required to record order details as specified by the Exchange and such records must be retained by the member for a period of five years. Members are required to make such records available to the Exchange if requested.

In the absence of a regulatory scheme which would allow foreign exchanges to place securities trading facilities in the US, market users in the US will not themselves have direct access to the LIFFE CONNECT<sup>®</sup> system for the trading of UK Equity Options and UK Index Options. Access to the market will be through

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<sup>2</sup> The statistics regarding average daily trading volume do not include over-the-counter transactions reported to the Exchange via Bclear.

<sup>3</sup> Statistics regarding open interest include over-the-counter transactions reported via Bclear and accepted by the Exchange.



Exchange members and only those members located outside the United States will be able to input orders to LIFFE CONNECT® in respect of UK Equity Options and UK Index Options.

Orders may be submitted at any time during the period from the market Pre-Opening (beginning at 6.30am London time for UK Equity Options) until the Market Close at 4.30pm London time. Trading begins at the Market Opening (8.00am London time) and continues until the Market Close. (Trading hours may be changed from time to time.)

Further information about LIFFE CONNECT® is available from the Exchange.

#### Option Classes, Expiry Months and Series

UK Equity and UK Index Options listed on LIFFE, with the exception of flexible Options, are traded on LIFFE CONNECT® in both puts and calls (“classes”), with several standardized durations (“expiry months”) and several standardized exercise prices (“series”). Flexible Options may be listed as puts or calls and, subject to parameters set by LIFFE A&M, have an investor-specified duration (“expiry date”) and an investor-specified exercise price.

#### UK Equity Option Primary Market Makers

From 2 July 2007, LIFFE has operated a Primary Market Maker (“PMM”) Scheme and a Primary Liquidity Provider (“PLP”) Scheme for all UK Equity Options. The most liquid classes (currently 20) known as the Target Group, have PLPs and PMMs and the remaining classes (currently 68) known as the non-Target Group have PMMs only. The two schemes run in parallel and members are able to participate in a scheme by agreeing to meet minimum size and spread obligations established by LIFFE. Members are able to apply to be a PMM or PLP within LIFFE CONNECT® in respect of one or more class. Each category has pre-determined obligations and benefits. These are set out below:

- PLP Target Group obligations:
  - Ensure that for each assigned class continuous bids and offers are maintained by the PLP in the LIFFE CONNECT® Trading Host in all series with a remaining lifetime of up to and including 13 months.
  - Ensure that the continuous bids and offers meet the maximum spread and minimum size requirements established by LIFFE at the beginning of the scheme (and reviewed periodically by LIFFE).
  - Ensure that the bids and offers remain present in the order book for 90% of the trading period.
- PLP Target Group benefits:
  - An Individual Trading Mnemonic (“ITM”) will be enabled with Market Making Order (“MMO”) functionality which allows a PLP to submit 65 quotes per message.
  - Delta protection will be enabled on MMO orders at the LIFFE CONNECT® Trading Host level to help the PLP to manage his risk efficiently.

- Transaction fee rebates will be provided on the basis of PLP performance in the registered classes in which he quotes in that capacity.
- PMM Target Group obligations:
  - Ensure that continuous bids and offers are maintained by the PMM in the LIFFE CONNECT<sup>®</sup> Trading Host in 10% of all series of a class (subject to a PMM being required to quote in a maximum of 50 series per class).
  - The PMM can select these series in the Near the Money area from series with a maximum remaining lifetime of 13 months.
  - Ensure that continuous bids and offers meet the maximum spread and minimum size requirements established by LIFFE at the beginning of the scheme, (and reviewed periodically by LIFFE).
  - Ensure that bids and offers remaining present in the order books for 90% of the trading period.
- PMM Target Group benefits:
  - A PMM ITM will be enabled with MMO functionality which allows a PMM to submit 7 quotes per message.
  - Delta protection will be enabled on MMO orders at the LIFFE CONNECT<sup>®</sup> Trading Host level to help the PMM to manage his risk efficiently.
  - Transaction fee rebates will be provided against the PMM performance criteria in his registered classes.
- PMM Non-Target Group obligations:
  - Ensure that continuous bids and offers are maintained by the PMM in the LIFFE CONNECT<sup>®</sup> Trading Host in 10% of all series of a class (subject to a PMM being required to quote in a maximum of 50 series per class).
  - The PMM can select these series in the Near the Money area with a maximum remaining lifetime of 9 months.
  - Ensure that continuous bids and offers meet the maximum spread and minimum size requirements established by LIFFE at the beginning of the scheme, (and reviewed periodically by LIFFE).
  - Ensure that bids and offers remain present in the order book for 80% of the trading period.
- PMM Non-Target Group benefits:
  - A PMM ITM will be enabled with MMO functionality which allows a PMM to submit 7 quotes per message.
  - Delta protection will be enabled on MMO orders at the LIFFE CONNECT<sup>®</sup> Trading Host level to help the PMM to manage his risk efficiently.
  - Transaction fee rebates will be provided on the basis of the PMM performance in which he acts in that capacity.

Full details of the PLP and PMM Schemes, including the lists of Target and Non-Target Group classes together with the obligations and benefits in relation to each UK Equity Option, are published by Notice and on the Liffe<sup>4</sup> website ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)).

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<sup>4</sup> Liffe is the brand name for the European derivatives business of NYSE Euronext, comprising the derivative markets in Amsterdam, Brussels, Lisbon, London (i.e. LIFFE) and Paris.

## FTSE 100 Index Option Primary Market Makers and Designated Market Makers

From 2 July 2002, the Exchange has operated a Primary Market Maker (“PMM”) Scheme in the FTSE 100 Index Option. The PMM Scheme runs in parallel with a Designated Market Maker (“DMM”) Scheme with a joint objective to enhance both on-screen and wholesale liquidity.

Members are able to participate in the schemes by applying to the Exchange and by agreeing to meet minimum size and spread obligations established by LIFFE.

- FTSE 100 Index Options: PMM obligations:
  - Ensure that continuous bids and offers are maintained by the PMM in the LIFFE CONNECT<sup>®</sup> Trading Host in 10% of all series subject to quoting in a maximum of 50 series.
  - The PMM can select these series in the Near the Money area with a maximum remaining lifetime of 9 months.
  - Ensure that continuous bids and offers meet the maximum spread and minimum size requirements established by LIFFE at the beginning of the scheme. (and reviewed periodically by LIFFE).
  - Ensure that bids and offers remaining present in the order books for 90% of the trading period.
- FTSE 100 Index Options: PMM benefits:
  - A PMM ITM will be enabled with MMO functionality which allows 7 quotes per message.
  - Delta protection will be enabled on MMO orders at the LIFFE CONNECT<sup>®</sup> Trading Host level to allow the PMM to manage his risk efficiently.
  - Transaction fee rebates will be provided on the basis of PLP performance criteria.

Full details of the PMM Scheme, including the DMM obligations are published by Circular and on the Liffe website ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)).

## FTSE 100 Index Options: DMM Scheme

From 1 April 2003, the Exchange has operated a DMM Scheme in the standardized FTSE 100 Index Option. DMMs were invited to apply for DMM status by agreeing to meet the following fixed obligations as determined by LIFFE:

For 90% of each trading session (that is, contract opening through to close), the DMM is required to quote two way competitive prices and order sizes, either:

- (a) over the telephone; or
- (b) through answering electronic Requests For Quote (“RFQs”) on LIFFE CONNECT<sup>®</sup>.

DMMs are required to choose one of the two methods set out above for the duration of the DMM Scheme. The chosen method may be changed from time to time if notified, in advance, to the Exchange in writing.

DMMs are required to meet the obligations in all expiry months and series listed.

Full details of the DMM Scheme are published by Notice and on the Liffe website.

### Placing of Orders

Orders by customers may generally be placed with member brokers for execution either “at market” or at, or better than, a certain price (a limit order). An instruction to “deal at market” means that the member broker will attempt to buy or sell the required number of option contracts for the customer at the best market price currently available. Customers may further specify that an order should only be matched if a minimum volume can be achieved or that it should only be matched if the entire order can be traded. In addition, orders may be entered on the basis that they are Good ‘Til Cancelled (“GTC”) or that they should be matched on an Immediate or Cancel (“IC”) basis.

At the end of the trading day, all orders on LIFFE CONNECT® – with the exception of GTC orders – will be withdrawn automatically from the central order book. Prior to the conclusion of the “session end” period, traders may, in addition, withdraw any GTC orders which they do not wish to remain in the market on the following day.

LIFFE CONNECT® continuously generates price limits in real-time, and rejects orders submitted outside the limits (i.e. bids at a price above the “limit bid” and offers at a price below the “limit offer”). For UK Equity and Index Options, LIFFE A&M calculates a theoretical fair value price for each series. The fair value will generate a spread, the range of which is determined from the applicable option delta value. The spread range is then employed by the Trading Host as the price limit for the option series concerned.

Attempts to enter orders priced outside the prevailing price limits will be rejected by the Trading Host – unless overridden by Exchange Officials - and the responsible person submitting the order will be informed accordingly.

Members may execute cross transactions through LIFFE CONNECT®. Provided orders are entered in accordance with the crossing procedures promulgated by the Exchange, business transacted through LIFFE CONNECT® may be pre-negotiated within the same member, with other members or with clients. Those crossing procedures stipulate that members and responsible persons must ensure that, when pre-negotiating a client order and/or when executing client business by way of a cross transaction, they act with due skill, care and diligence; and that the interests of the client or clients are not prejudiced. Pre-negotiated business will be transacted at the best bid and offer available in the market.

Members may transact those strategy trades which have been recognized by LIFFE. Details of such strategy trades are contained in the Annexe to the LIFFE CONNECT® Trading Procedures, a copy of which may be found on the Liffe website ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)) under “Trading Information”, “Trading Procedures”. Such strategy trades include Stock Contingent Trades (see below).

## Stock Contingent Trades

Members who are eligible to trade in UK Equity Options may enter strategy trades which involve the simultaneous execution of transactions in options and the underlying stocks. Members may enter a number of different types of Stock Contingent Trades involving various combinations of options against stock. As noted above, details are contained in the Annexe 2 to the Trading Procedures, a copy of which may be found on the NYSE Euronext website ([www.nyseeuronext.com/liffe](http://www.nyseeuronext.com/liffe)) under “Trading Information”, “Trading Procedures”.

Both the UK Equity Option contracts and the underlying company security components of these Stock Contingent Trades must be executed on behalf of the same client or on behalf of the same house account.

Members who are eligible to trade in UK Index Options may also transact volatility trades either for their own account or for their customers. In this case, a volatility trade entails the making of an Index Futures contract simultaneously, and in combination, with one or more UK Index Option contracts (i.e. the FTSE 100 Index Futures Contract with the standardized or flexible FTSE 100 Index Option Contract). The FTSE 100 Index Futures Contract has been approved for sale to US customers.

## Block Trade Facility

The Exchange offers a Block Trade Facility (“the Facility”) for both UK Equity Options and Index Options. This Facility is designed to encourage new large order business to the Exchange that would otherwise not be executed on-exchange, whilst ensuring that price discovery on LIFFE’s electronic trading mechanism remains robust. The Facility permits members (and their wholesale clients) to enter into transactions in large size at a price negotiated between the parties without requiring prior exposure of the transaction to the Exchange’s electronic trading mechanism. Block Trades are subject to LIFFE’s Trading Procedures which specify requirements regarding minimum order size thresholds, fair market value pricing and transaction reporting to LIFFE.

The Facility is restricted to members and, pursuant to customer suitability requirements stipulated by the relevant regulatory agency, those customers with sufficient knowledge, experience and understanding of the Exchange and its contracts and the implications of using the Facility.

On each occasion of quoting a Block Trade price, the member must make it clear to the wholesale client that the price being quoted is a Block Trade price. The price of a Block Trade must represent the fair market value for that trade, that is the price considered by the member to be the best available for a trade of that kind and size. When negotiating a Block Trade price, a member and a client should, in particular, take into account the prevailing price and volume available on the electronic system, the liquidity of the electronic market and general market conditions. Block Trades must be reported to the Exchange within five minutes of the time of trade in relation to trades which are not contingent on a transaction in another instrument, unless there are exceptional market circumstances. If a trade is contingent on a transaction in another instrument, or if there are exceptional market circumstances, trades must be reported within 15 minutes.

Where a trade is authorized by the Exchange, trade details will be published to the market as soon as possible thereafter.

#### Visibility of Quotes and Transactions

A range of information on UK Equity Options and UK Index Options is made available via LIFFE's own systems and a large number of licensed Quote Vendors.

The information that is made publicly available on each series of UK Equity Options and standardized Index Options is shown below.

1. Exercise price and expiry month
2. Current bid and offer premium prices within the LIFFE CONNECT<sup>®</sup> central order book
3. Premium price of last trade
4. Aggregate open interest at the close of LIFFE the previous day
5. Previous day's volume in numbers of contracts
6. Previous day's closing premium bid and offer prices
- 7.\* Current quotation for the underlying security
- 8.\* "Settlement Price", for collateral purposes (and exercise of American-style options), calculated by LIFFE from price of underlying security or index
9. Current matched volume
10. Limit Orders - price and size in the LIFFE CONNECT<sup>®</sup> central order book
- 11.\* Index values and change on day

Note: Items marked with an asterisk (\*) are not provided to Quote Vendors by LIFFE. That information is received by Quote Vendors from the London Stock Exchange or the relevant index provider.

#### Trading Halts

Trading in one or more options may be suspended if events threaten the orderly conduct of business. Such events may include a LIFFE CONNECT<sup>®</sup> technical failure or an act of God or another event outside the Exchange's control. Furthermore, trading in a UK Equity Option may be suspended if trading in the underlying security has been suspended. Similarly, trading in UK Index Options may be halted if market conditions or other circumstances prevent or interrupt timely calculation of the relevant Index.

An announcement of a trading halt will be made as soon as practicable on LIFFE CONNECT<sup>®</sup> or on the display systems of LIFFE's licensed quote vendors or on both. Trading will begin again when, in the opinion of two Exchange Officials, business may be resumed on an orderly basis. No open position may be closed or a new position opened while trading in an option is suspended. When trading in an underlying security has been suspended, option exercise notices may still be submitted. Investors should note that trading may be resumed on LIFFE before or after any suspension on the London Stock Exchange has ended.

## Handling of LIFFE CONNECT® Technical Failures

In the event of a failure of either a Trading Application associated with a particular ITM or a link to the Trading Host, the Host will attempt to transfer any extant orders to a nominated replacement ITM within the member. If there are no replacements nominated, or if none is logged-on, all relevant orders (with the exception of GTC orders) will be withdrawn from the central order book. The Trading Host will confirm the deletion of orders from the order book when the trader re-connects and asks for “retrieve orders”.

In the event of a failure of this sort, the trader may also withdraw GTC orders, if he so wishes, by telephoning designated Exchange officials.

In the event of failure of the Trading Host, the Trading Application will receive a “system error” message and all non GTC orders will be withdrawn. Designated Exchange Officials will decide whether to re-open the market on the same day.

## *BCLEAR*

From 24 October 2005, the Exchange has made available to its members various OTC derivatives processing services, including Bclear. Bclear provides a means by which an OTC options transaction in respect of equity securities may be replaced with an equivalent standardized on-exchange options contract. Appendix One sets out the OTC trades in UK Equity Options and Index Options which are eligible for submission via Bclear by LIFFE members and affiliates and their authorized customers in the United States. Bclear accepts only completed transactions and is not a matching system for orders.

Parties wishing to use the Bclear service negotiate and agree to the terms of an OTC options transaction (the “OTC Trade”) on a product within the scope of Bclear. Products within the scope of Bclear must conform to the requirements of LIFFE’s contract specifications for the listed product, which generally provide for flexible terms. For example, LIFFE contracts may be American-style or European-style exercise, have flexible terms regarding the exercise price and expiration date (subject to Exchange – determined parameters) and may be physically settled (UK Equity Options) or cash settled (UK Equity Options and UK Index Options).

Trades must satisfy the applicable minimum volume threshold for the product (e.g. the current threshold is 250 contracts for UK Equity Options and 500 contracts for FTSE 100 Index Options). Details of all minimum volume thresholds applicable for UK Equity Option and UK Index Option contracts on Bclear are also shown in Appendix One.

Access to Bclear is available to members of LIFFE (including authorized affiliates of members). A LIFFE member may request that its customer be permitted to submit trades directly to Bclear. Any trades so submitted must be authorized by the relevant LIFFE member before they are subjected to the Exchange’s trade confirmation checks and accepted or rejected as appropriate.

A LIFFE member may trade for its own account or it may act on behalf of a non-member customer or it may act in each capacity. The LIFFE member or its authorized customer (or in the case where more than one LIFFE member is party to the OTC Trade, the LIFFE member as agreed between the parties) will submit specific trade information regarding the OTC Trade to LIFFE and LIFFE will either accept or reject the trade. Trade details are required to be submitted as soon as practicable and, in any event, within one hour of the time the trade was entered into.

If the Exchange accepts an OTC Trade, the trade is replaced by a LIFFE contract, subject to LIFFE Rules, and having LCH.Clearnet as the central counterparty. Please see the section entitled the “Contractual basis of LIFFE business” on page 16 for further details. The Exchange is not obligated to accept a trade that is submitted to Bclear and may reject a trade for a number of reasons. For example, the trade may be rejected if it does not meet the applicable contract requirements, if LIFFE does not consider the trade to have been entered into at a fair value, or if it does not satisfy the applicable minimum volume threshold. If a trade is rejected, the trade will be cancelled by the parties to the trade unless they agree to remain bound by its terms, albeit as an OTC contract.

For the avoidance of doubt, Bclear is totally distinct from LIFFE CONNECT<sup>®</sup> because LIFFE CONNECT<sup>®</sup> is an order matching system while Bclear is a mechanism to submit completed OTC transactions to the exchange. OTC trade submissions via Bclear are accomplished in any one of three ways: (1) through a secure, web-based application that members access via their own internet connections; (2) through the Bclear API, which members can integrate with their own in-house systems; or (3) through Cscreen, which has a direct link to Bclear. Cscreen is an electronic bulletin board for posting indications of interest in the over-the-counter derivatives market. Cscreen does not provide for the matching of trades.

Contracts confirmed through Bclear that have become Exchange contracts upon acceptance by the Exchange may share the same standardized economic characteristics as those available for trading through LIFFE CONNECT<sup>®</sup>, as well as contracts that may subsequently made available for trading through LIFFE CONNECT<sup>®</sup>. In each case, such contracts will be fungible with those available for trading through LIFFE CONNECT<sup>®</sup>. This arrangement is designed to maximize the efficiencies of post-trade administration and clearing and to realize the regulatory benefit of netting-out outstanding financial exposures wherever desirable.

The counterparties to an OTC Trade which is to be submitted for confirmation within Bclear may choose whether or not they wish the trade details to be published upon confirmation. Information about trades that are confirmed and published on Bclear is made available on a dedicated website hosted by a third party. The information is available at <http://bcleartrades.euronext.co.uk> The information that is made publicly available on each published trade is shown below:

1. Name of contract
2. Contract code
3. Expiry month
4. Call or Put
5. Strike Price



6. Time of trade
7. Trade price
8. Reported trade's volume in numbers of contracts

#### Trade submission hours

The trade submission hours on Bclear for UK Equity Options and UK Index Options are currently 8.00am to 5.00pm London time.

There are days on which LIFFE will be closed when US businesses are open, and vice versa, because of differing national holidays. In addition, the days on which LIFFE is closed may vary from year to year. A current list of Exchange holidays is available on the Exchange's website at [www.nyseuronext.com/liffehours](http://www.nyseuronext.com/liffehours).

## CONTRACTUAL BASIS OF LIFFE BUSINESS

In the case of trades executed through LIFFE CONNECT® and those confirmed via Bclear, the contractual basis of such business is the same. In each case, members of LIFFE are required by LIFFE Rules to transact business in LIFFE contracts in the legal capacity of a principal. When a customer's order is executed, the requirement that the member executing the transaction contracts as a principal means that such member is the counterparty to the customer on the one hand and, on the other hand, counterparty to the member with whom the trade was conducted on the market. The second of these two contracts (i.e. that created on the market between the two members) will be subject to novation. This means that where a customer has dealt through a non-clearing member of LIFFE, there will be a chain of linked, or "back-to-back", contracts as follows:

- (i) between customer and non-clearing member;
- (ii) between non-clearing member and clearing member; and
- (iii) between clearing member and LCH.Clearnet.

The non-clearing member's customer therefore obtains no contractual relationship with anyone other than the non-clearing member. (The treatment of customer funds and property is explained on page 17 below.) The only difference between the Bclear process and the process by which UK Equity Option and UK Index Option contracts are formed on LIFFE CONNECT® is in the creation of the initial contract. With LIFFE CONNECT®, the initial trade is executed on the Exchange, whereas with Bclear, the initial contract is an OTC Trade, which is executed away from the Exchange and then presented to the Exchange for acceptance.

## TRADING FOR CUSTOMERS

### Broker Responsibilities

Members of LIFFE acting as brokers for customers may also be trading for their own account. Under the requirements of the FSA, brokers must pay due regard to the interests of their customers. There are express rules which require firms to execute customer orders and own account orders fairly and in due turn. The effect of this is to require brokers to give precedence and priority to customer orders over contemporaneous orders for their own account.

LIFFE members are subject to regulation under LIFFE Rules in their market activities and, for UK-based members, in their customer-relationships by the FSA. Firms regulated by the FSA are required to operate under rules concerning the segregation of client funds and the safe custody of client assets. Broadly equivalent requirements apply in respect of members of LIFFE who are resident entities in other jurisdictions.

### Treatment of Customer Funds and Property

Firms authorized by the FSA under the Financial Services and Markets Act 2000 (including all relevant LIFFE members) are subject to the FSA rules, including the rules relating to client assets and client money contained in the Client Assets Sourcebook ("CASS"). Although the application of the CASS rules varies according to the type of firm and the activities involved, the general objective is to impose a statutory trust upon all client money and thereby to protect customers' cash assets in the event of the insolvency of the firm. Under the provisions in CASS, "client money" is money which a firm holds in connection with investment business with or for a customer, or which a firm elects to treat as client money. (Note that EU firms doing business in the UK by virtue of a European passport are subject to the client money rules of their home State. However, implementing measures made under the EU's Markets in Financial Instruments Directive ("MiFID") provide a minimum standard for such rules within the EU.)

CASS 4.3.34R requires client money to be paid into a segregated client bank account (i.e., segregated from the money of the firm) with an approved bank. A firm owes a duty of care to a client when deciding where to place client money and must take reasonable steps to ensure that the banks with which it chooses to place client money are appropriate for that purpose.

In certain circumstances, the FSA rules permit a member to agree with a customer that its money is not segregated from that of the firm (CASS 4.1.8 - 4.1.14). Where the client is an eligible counterparty or a professional client (i.e. not a private customer), the firm may rely upon written acknowledgement from that customer that the money will not be subject to the protections under the client money rules and as a consequence the money will not be segregated from the firm's own money and the customer will rank only as a general creditor of the firm.

Non-cash collateral is handled differently. Its treatment in the event of the insolvency of the firm will depend on the terms on which it has been lodged with that firm (and, where relevant, on the terms that the firm has lodged it with others, such as a custodian or clearing house). CASS 6 imposes detailed

custodianship requirements in respect of a client's investments, including giving to the member the responsibility for safekeeping of documents of title and certificates and requiring the registration of investments in the customer's name or in another name in circumstances as specified in the CASS rules. A number of disclosures must also be made to the customer in certain circumstances in order that the customer understands the custodian arrangements.

#### Broker Insolvency

A compensation scheme has been established under the Financial Services and Markets Act 2000 (and the FSA's Compensation Sourcebook) under which certain "eligible claimants" are able to claim compensation in the event that a firm defaults and is unable to meet the client's claims upon it. On the basis that the compensation scheme is generally available to private customers, it is unlikely to be available to a US Qualified Broker-Dealer or Qualified Institution.

#### Default

Both LIFFE and LCH.Clearnet have default rules, as required by the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001. If a clearing member appears to LCH.Clearnet to be unable, or to be likely to become unable, to meet its obligations to LCH.Clearnet, it may be declared a defaulter under LCH.Clearnet's default rules in relation to the contracts registered by it with LCH.Clearnet. Where a clearing member has been declared a defaulter by LCH.Clearnet, contracts between such clearing member and its non-clearing members and clients will be dealt with under the Exchange's default rules. A default by a non-clearing member will also be dealt with under the Exchange's rules.

The Exchange's default rules permit the Exchange to direct that open contracts to which a defaulting member is party be dealt with in one of a number of ways including, for example, off-set against matching contracts to which the defaulter is party, closing-out through trading out on the market, transfer to another member or invoicing back.

## SPECIAL FACTORS IN INVESTING ABROAD IN LIFFE CONTRACTS

In addition to the general risks inherent in buying and writing traded options, importantly including market supply and demand effects on the liquidity of particular options series, special risk factors are present and should be considered in transacting in options abroad. These factors include differences in the currency, differences in time zones, differences in settlement periods and procedures, differences in market features and certain differences in option features. Whilst there are features of its operation and self-regulation which LIFFE has in common with US options exchanges and while LIFFE options are American-style in exercisability (with the exception of index options), there are differences. Significant differences in market, contract and settlement features are developed in separate sections of this document. Additional significant factors are referred to below.

### Currency Exchange Rates

As all UK Equity Options and FTSE 100 Index Option premiums, settlements and exercises are payable in British pounds sterling, a US transactor should take into account the exchange rate between US dollars and British pounds sterling. Any movement in the US dollar buying and selling rates for such currencies may alter profit and loss profiles for any LIFFE options position or strategy. If US dollars or dollar-denominated securities are used as margin for written positions, an exchange rate change may also affect the amount of margin required. It should especially be noted that written put option contracts will, on allocation, be required to be satisfied by payment for the underlying security in British pounds sterling.

The high and low currency exchange rates for the US dollar/British pounds sterling over recent years have been as follows:

<b>US\$/GBP</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008<sup>5</sup></b>
High	\$1.5100	\$1.6133	\$1.7943	\$1.9550	\$1.9325	\$1.9815	\$2.1101	\$2.0335
Low	\$1.3682	\$1.4044	\$1.5463	\$1.7481	\$1.7049	\$1.7199	\$1.9225	\$1.7770

Calculation of the equivalent US dollar value of the British pounds sterling exercise price of a LIFFE option and the current British pounds sterling market price on the London Stock Exchange of the security underlying the LIFFE option would permit comparison with a quoted ADR price, if any, in the US for that security.

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<sup>5</sup> Up to 3 September 2008.

## Time Zones and Holidays

The LIFFE CONNECT® trading hours for UK Equity Options are currently 8.00am to 4.30pm London time, while FTSE 100 Index Options currently trade from 8.02am until 4.30pm London time. The trading hours of the London Stock Exchange for the securities underlying such options are currently from 8.00am to 4.30pm London time. Such hours may be changed in accordance with the rules of the relevant market. The Block Trade Facility is available during the normal trading hours of the contract concerned. The reporting hours on LIFFE for eligible products within the Bclear service are currently 8.00am to 5.00pm London time.

US investors should take time zone differentials into account when timing investment decisions and when making required premium or margin payments. The overlap of opening of US markets and the LIFFE trading hours will vary depending on the time of year (standard or daylight saving time in the US and the UK) and in which US time zone the investor is located. Greenwich Mean Time is five hours ahead of Eastern Standard Time; that is, 9.00am Eastern Standard Time in New York is 2.00pm Greenwich Mean Time in London. London does not always switch from Greenwich Mean Time to British Summer Time, or back, on the same date that New York switches from Eastern Standard to Eastern Daylight Saving Time, or back.

For US investors the time periods allowed by brokers for payment of premium or provision of margin may be abbreviated by the time zone differential, since deadlines are stated in London time throughout. In this connection, allowance may also have to be made for the time needed for US-UK communication. An effect of the time zone difference is that if the US markets were to fall during their afternoon, UK Equity Options and Index Options positions could not be closed out until the next morning London time.

There are days on which LIFFE will be closed when US businesses are open, and vice versa, because of differing national holidays. In addition, the days on which LIFFE is closed may vary from year to year. A current list of Exchange holidays is available on the Exchange's website [www.nyseuronext.com/liffehours](http://www.nyseuronext.com/liffehours).

## UK EQUITY OPTIONS

### Underlying Securities

The UK Equity Options traded on and reported to LIFFE will be subject to regular review by LIFFE A&M. Those available within LIFFE CONNECT® are physical delivery options and have American-style exercise. Such options are also capable of being reported via Bclear, along with cash settled American-style exercise options, physical delivery European-style exercise options and cash settled European-style exercise options.

UK Equity Options have been introduced on stocks usually drawn from the most highly capitalized securities traded on the London Stock Exchange. All stocks underlying LIFFE's UK Equity Options are traded on the Stock Exchange Electronic Trading Service ("SETS"). SETS is the London Stock Exchange's electronic order driven trading platform for all FTSE 100 Index constituent stocks (and a number of smaller stocks). SETS was introduced on 20 October 1997 to replace the old quote driven system known as "SEAQ". SETS trades are published immediately.

Trades in excess of eight times Normal Market Size<sup>6</sup> may be executed away from SETS by means of a Worked Principal Agreement. This enables the principal to offset market risk prior to trade publication. Details of such trades are published when 80% of the risk has been offset or by the end of the trading day, whichever is earlier.

Other trades executed on the Stock Exchange but away from the central order book are reported and published within three minutes.

SETS trades, and those executed by means of Worked Principal Agreements, currently settle on a T+3 basis.

It should be noted that most London Stock Exchange listed stocks of British companies, including those on which LIFFE trades options, have a market price of lower than £15 per share, the average price being around £6 (600p).

The London Stock Exchange sometimes lists for trading equity securities that are new; they are being initially publicly offered and distributed in the UK. In some cases during this period, LIFFE may list options on these securities. LIFFE may restrict its members, or the issuer may prohibit underwriters, from entering into transactions in such options under LIFFE Rules with US entities during and for some period after such distributions.

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<sup>6</sup> Normal market size will generally result in a transaction involving in excess of £250,000.

## Expiry Months and Dates

For the majority of UK Equity Options traded on LIFFE CONNECT®, the maximum life is nine months. However, those UK Equity Options in the “Target Group” of UK Equity Options on the top 20 UK stocks have a maximum life of two years. The expiry dates are arranged on a quarterly cycle. The cycle is: March-June-September-December.

The expiry date of a UK Equity Option on LIFFE CONNECT® is currently set as the third Friday of the expiry month.

Trading in an Equity Option can occur during an expiry day until the usual time for close of business.

For each UK Equity Option within LIFFE CONNECT®, multiple series intervals are applicable per expiry month. The around the money series have smaller series intervals in comparison to the deeper in- and out-of-the-money series. In this way, LIFFE A&M seeks to create more diversity between the series available for trading. A minimum number of series per expiry month is introduced depending on the remaining lifetime of the expiry month. The minimum number of in-the-money (“ITM”), at-the-money (“ATM”) and out-of-the-money (“OTM”) series to be introduced initially for short-term, mid-term and long-term expiry months is as follows<sup>7</sup>:

- short-term - 1, 2 and 3 months - 3 ITM + 1 ATM + 3 OTM
- mid-term - 6, 9 and 12 months - 2 ITM + 1 ATM + 2 OTM
- long-term - 18, 24 and 36 months - 1 ITM + 1 ATM + 1 OTM

The exercise price of each such series is fixed in accordance with the following scale:

Interval Scheme denominated in Pence						
Range	Exercise Prices			Interval Scales in pence		
				Scale A	Scale B	Scale C
1	1	-	< 50	1	2	4
2	50	-	<100	2	4	8
3	100	-	< 250	5	10	20
4	250	-	< 500	10	20	40
5	500	-	< 1000	20	40	80
6	1000	-	< 2000	50	100	200
7	2000	-	< 4000	100	200	400
8	≥ 4000			200	400	800

<sup>7</sup> The option series whose price differs the least from the price of the underlying is considered to be the at the money series. There will be no at the money series in a situation where the market price of the underlying security is exactly halfway between two series.



Subsequent to an expiry month being initially listed on LIFFE CONNECT®, the minimum number of series per expiry month will be as follows:

**≤ 3 months to expiry**

For expiry months with a remaining lifetime of up to and including 3 months:

At least 7 series

- 3 series around the money: Interval Scale A 1<sup>st</sup> ITM+ATM+1<sup>st</sup> OTM

- 4 series: Interval Scale B 2<sup>nd</sup> ITM+3<sup>rd</sup> ITM+  
2<sup>nd</sup> OTM+3<sup>rd</sup> OTM

**> 3 to ≤ 12 months to expiry**

For expiry months with a remaining lifetime exceeding 3 months and up to and including 12 months:

At least 5 series

- 3 series around the money: Interval Scale B 1<sup>st</sup> ITM+ATM+1<sup>st</sup> OTM

- 2 series: Interval Scale C 2<sup>nd</sup> ITM+2<sup>nd</sup> OTM

**> 12 months to expiry**

For expiry months with a remaining lifetime exceeding 12 months:

At least 3 series

- 3 series around the money: Interval Scale C 1<sup>st</sup> ITM+ATM+1<sup>st</sup> OTM

The following tables provide a summary of the exercise prices per expiry month at time of listing:

Time to maturity	1,2,3 months	6,9,12 months	18,24,36 months
	<div> <div>3<sup>rd</sup> 2<sup>nd</sup> Scale B</div> <div>1<sup>st</sup> ATM Scale A</div> <div>1<sup>st</sup> 2<sup>nd</sup> 3<sup>rd</sup> Scale B</div> </div>	<div> <div>2<sup>nd</sup> Scale C</div> <div>1<sup>st</sup> ATM Scale B</div> <div>1<sup>st</sup> 2<sup>nd</sup> Scale C</div> </div>	<div> <div>1<sup>st</sup> ATM Scale C</div> <div>1<sup>st</sup></div> </div>

A price established on a trading day (T) will be the reference used to determine the introduction of additional series on the next trading day (T+1) to have at least the minimum number of in- and out-of-the-money series listed.

The Exchange may apply an alternative scale of exercise price intervals to specified individual Equity Option contracts if appropriate. Such alternative scales are notified by means of a Notice.

In relation to Bclear, the exercise price is configurable by the member, subject to parameters established by LIFFE A&M which are published by Notice and on the Liffe website ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)).

Special Features of flexible Options

It should be noted that:

- (i) a flexible UK Equity Option cannot be introduced with the same expiry day and exercise price as an existing standardized American-style exercise, physical delivery UK Equity Option; and
- (ii) when a standardized American-style exercise, physical delivery UK Equity Option contract is listed with the same exercise price and expiry date as an existing flexible Option series, the existing flexible Option series will be novated into the corresponding American-style exercise, physical delivery UK Equity Option contract series.

#### Contract Size

While the premium for an Equity Option is quoted in pence per share, the minimum unit of trading in UK Equity Options is one contract, which normally represents the options on 1,000 shares of the underlying security. Occasionally, it is necessary to adjust the size of existing option contracts to reflect changes in the capitalisation of companies concerned.

All orders in UK Equity Options should refer to the number of contracts and not to the number of shares of the underlying security to which the option contracts relate; e.g. an order for options on 5,000 shares of the underlying security, where each contract represents options on 1,000 shares, should be placed as an order for 5 contracts. Orders cannot be executed in fractions of a contract.

#### Corporate Actions Policy

LIFFE A&M's methodology for handling the consequences of Corporate Actions is based on the principle that, when the shares underlying an Equity Option (which has not been exercised) become ex entitlement, options on such shares should be amended to reflect in economic terms (as far as practicable) a holding equivalent to the ex entitlement shares and the relevant entitlement, and may be effected as follows:

- by altering the exercise prices and the lot size of UK Equity Options; or
- by substituting the underlying shares in a proportion determined by the ex entitlement holding with the new underlying shares; or
- by settling (closing) UK Equity Options at their respective Fair Value.

As a general matter, contract adjustments are not made to reflect payment of normal dividends, whether cash or scrip. However, where a dividend is identifiable as a "special dividend" outside the normal pattern of payments, it will be treated as a capital event leading to adjustment of the option exercise price and contract size. Full details of the Exchange's Corporate Action Policy are published via Notice and on the Liffe website ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)).

## Position Limits

LIFFE A&M imposes no limits on the number of UK Equity Option contracts which any individual or single group of investors may hold. However, the number of contracts held by any one investor or group of investors in respect of a particular UK Equity Option must (pursuant to the Companies Act 1985) be disclosed to the relevant UK authority unless the holding of such contracts either alone or in conjunction with a holding of the underlying shares is less than 3% of the relevant share capital of the issuer.

## Premiums

Premiums on UK Equity Options are currently quoted in pounds sterling. Please refer to the Lists of Contract Details for Exchange Contract No. 201 and No. 201F ([www.nyseuronext.com/liffe](http://www.nyseuronext.com/liffe)) for information about the minimum price increment for each option. For UK Equity Options traded on LIFFE CONNECT<sup>®</sup>, the premium is the only variable factor, all other terms of the options contract being pre-determined. The premium is expressed as an amount per option on a single share of the underlying equity. It is payable to LCH.Clearnet by the buying clearing member in full in cash pounds sterling, with respect to each options contract (usually of 1,000 shares), by 10.00am London time on the business day following the trade. Such premium will be made available by LCH.Clearnet to the selling clearing member by 1.30pm London time on that day.

## Exercise by Holders

If the holder of an option wishes to exercise the right to buy or sell the underlying security at the specified price (or to receive cash settlement in the case of certain flexible UK Equity Options), the holder should instruct its broker to ensure that an Exercise Notice is submitted to LCH.Clearnet. An Exercise Notice may be submitted to LCH.Clearnet either manually or automatically. Options will only be exercised if an Exercise Notice is submitted to LCH.Clearnet. On the Last Trading Day, expiring UK Equity Options that are in-the-money by the amount specified by the Clearing Member in CPS (the Clearing Processing System<sup>8</sup>) – or, if the Clearing Member has not so specified, by the amount established as the CPS default setting - will be exercised by an Exercise Notice being sent automatically to LCH.Clearnet.

In relation to UK Equity Options with American-style exercise, holders are entitled to exercise UK Equity Options on any LIFFE business day during the option's life. In contrast, UK Equity Options with European-style exercise may only be exercised on the expiry day. If the quotation of an

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<sup>8</sup> Two main functions are available through CPS. They are Position Maintenance and Margin Calculation. CPS updates members' positions in "real time" from trade based information delivered through the Trade Registration System. Members of LIFFE are able to interrogate CPS to determine the positions on their accounts for all contracts during the trading day. CPS updates users' historic positions and allows for various transfer and settlement operations in order that members' end of day positions can be reconciled so that the margining process can take place. At the end of the trading day, and once position maintenance activities are complete, a set of processes is initiated to enable CPS to calculate initial and variation margin for all member positions.

underlying security on which LIFFE options are listed is suspended by the London Stock Exchange, the holder of an option may still submit an Exercise Notice.

All exercise instructions need to be given before certain cut-off times on each business day that are established by the LIFFE broker with respect to its clients, because the broker will need to ensure that LCH.Clearnet receives the Exercise Notice before 5.20pm (6.00pm on an expiry day) London time. The deadline is strictly observed by LCH.Clearnet. The exercise instructions are submitted to LCH.Clearnet by the relevant clearing member via a computer terminal. The clearing system allocates the exercise instructions to the open short positions held by LCH.Clearnet in the same series by means of a computer program which randomly allocates the clearing members' accounts at LCH.Clearnet without discrimination.

#### Allocation to Writers

By 7.00am London time on the day after timely submission of an Exercise Notice, LCH.Clearnet will have randomly allocated a clearing member by way of an Allocation Notice, requesting that it or one of its clients who is an option writer in that series fulfil the terms of the options contract. If a clearing member's customer account is allocated, the clearing member is required, by random non-discriminatory selection, to designate a customer who is a writer to receive the Allocation Notice.

Once a writer has received an Allocation Notice, the writer may not then close its position in that contract by way of a closing purchase but must honour that contract by delivering the underlying security in the case of a call option, or by taking delivery of the underlying security in the case of a put option (or to cash settle in the case of certain flexible UK Equity Options). If, in light of the underlying security price, a writer of an option were to anticipate an allocation and early in the morning purchase an equivalent option to close the open position, the writer may not assume that its obligations as a writer have been extinguished until it receives confirmation from its broker. If the writer has been allocated but not yet informed by its broker, the attempt to close the written position will have resulted in the writer's having purchased an option to open a new position and the writer still having to fulfil the obligations of the written position which was allocated.

LCH.Clearnet is a principal to the clearing members in respect of the equity transactions resulting from the exercise of an option.

Upon receipt of written confirmation from LCH.Clearnet by both the clearing member that provided the Exercise Notice and the clearing member that was allocated, both members are required to ensure that details of the resulting equity transactions with LCH.Clearnet are input to CREST for settlement (in relation to physical delivery UK Equity Options). Any stock transactions that result from an Equity Option exercise remain subject to the LIFFE Contract Terms and thus to standard equity settlement procedures via CREST.

## Dividends

The holder of a call contract is not entitled to receive any payment of dividend, whether or not in the form of cash, declared on the underlying security. Consequently, no adjustment is made to the terms of LIFFE Equity Option contracts as the result of the underlying security being marked “ex dividend” with respect to normal dividends, although allowance for this may be reflected by changes in the premiums at which contracts trade in the market. It should be noted that in the UK, dividend payments may be more random and hence less predictable than in the US. Many UK companies do not pay dividends on fixed dates each year, are more likely to do so half-yearly than quarterly, and sometimes pay special dividends.

In order to receive the benefit of a dividend, a holder of a call contract must exercise before the underlying security is declared “ex dividend” by the London Stock Exchange. The London Stock Exchange seeks to provide a minimum of three business days’ notice of declaration of a security going ex dividend, but under UK practice the timing of such declarations is within the discretion of the issuer company. To exercise an equity option “cum dividend” for an equity going ex dividend, it is necessary to submit an Exercise Notice prior to the exercise deadline on the last day on which the stock is trading “cum dividend”.

## UK INDEX OPTIONS

LIFFE makes available two different options on the FTSE 100 Index. These are the standardized FTSE 100 Index Option with European-style exercise (LIFFE CONNECT<sup>®</sup> and Bclear) and the flexible FTSE 100 Index Option with European-style exercise or American-style exercise (Bclear only).

The stocks constituting the FTSE 100 Index represent the leading UK equity shares listed on the London Stock Exchange, in terms of capitalisation and liquidity. The FTSE 100 Index reflects the values and risks of a broader and marginally different universe of companies than the aggregate of those for which trading exists in UK Equity Options. Some UK Equity Options are on stocks that are not included in the FTSE 100 Index.

### Development of UK Indices

The FT 30 Industrial Share Index was first published in 1935 in response to demand from investors for a yardstick by which to measure the performance of the UK equity market and the behaviour of their portfolios. For more than fifty years it served as the barometer of day-to-day movements in share prices in the UK. It is an unweighted Index.

As equity investment became more sophisticated, the need was felt for a more refined measurement of the market, and in 1962 the Financial Times in collaboration with the Institute of Actuaries developed the “FT Actuaries Share Indices”. The resultant “All-Share Index” covers more than 740 different companies divided into six main groups and sub-divided into thirty-five different market sectors. These FT Actuaries Indices are “weighted” i.e. the larger the company the greater the influence on the Index.

The creation of the Financial Times-Stock Exchange 100 Share Index (“FTSE 100 Index”) marked a further stage in this process of development. It is a capitalisation weighted index which is representative of the market, and sufficiently compact to be calculated every 15 seconds throughout the trading day.

### How the FTSE 100 Index is compiled

The Index is calculated by FTSE International (“FTSE”). It has been published since 3 January 1984, with a base value of 1000.0. The value is calculated to one decimal place. The annual high-low range of the FTSE 100 Index in recent years has been:

	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008<sup>9</sup></b>
High	6360.3	5362.3	4491.8	4826.2	5647.2	6260.0	6732.40	6376.6
Low	4219.8	3609.9	3277.5	4283.0	4765.4	5506.8	5858.94	5150.6

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<sup>9</sup> Up to 3 September 2008.

With few exceptions, the largest 100 London Stock Exchange-listed companies by market capitalisation are included in the FTSE 100 Index. These leading 100 companies account for approximately 80 per cent<sup>10</sup> of the total market value of all UK equities, so the Index covers a very substantial part of the market and correlates closely to the FT Actuaries All-Share Index.

In accordance with the Ground Rules for the management of the UK Series compiled by the FTSE Actuaries Share Indices Steering Committee, the Europe/Middle East/Africa Indices Committee, composed of market users and representatives from the FTSE International, the London Stock Exchange, and LIFFE A&M, meets periodically to consider any changes in the constituents of the FTSE 100 Index which may be necessary, principally by reason of size and weighting changes.

The performance of a portfolio of stocks, other than one composed of all stocks in the FTSE 100 with appropriate weightings, will not necessarily be mirrored by the performance of such Indices. It may not be possible to purchase a portfolio of stocks constituting the FTSE 100 Index nor to sell such a portfolio, at the Index price.

#### Calculation of the FTSE 100 Index

The value of the FTSE 100 Index is calculated by FTSE every fifteen seconds by taking actual traded prices of the constituent securities and applying an arithmetical formula. The Index may exist in the following states:

1. Firm

The Index is being calculated during the Official Market Hours<sup>11</sup> of the London Stock Exchange on actual trades from SETS. No message will be displayed against the Index value.

2. Closed

FTSE has ceased calculating the Index for the day. The message “CLOSE” will be displayed against the Index value calculated by FTSE.

3. Held

During Official Market Hours, the Index has exceeded pre-set operating parameters (i.e. the Index level has moved by more than 10% within a given trading session) and real time calculation of the Index has been suspended. The message “HELD” will be displayed against the last Index value calculated by FTSE.

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<sup>10</sup> As at 25 May 2006.

<sup>11</sup> Official Market Hours are defined as that period when SETS is open for order execution, i.e. between 08.00 and 16.30 (London Time).

#### 4. Indicative

If there is a system problem or situation in the market that is judged to affect the quality of the constituent prices at any time when the Index is being calculated, the Index will be declared indicative (e.g. normally where a 'fast market' exists in the equity market). The message “IND” will be displayed against the Index value calculated by FTSE.

On the third Friday of each month FTSE International calculates the Expiry Value for expiring FTSE 100 Index Futures and Options. The Expiry Value is derived from an intra-day auction in each of the 100 stocks within the Index, as explained on page 33. During the auction period, an indicative Expiry Index is calculated and published. The Expiry Index effectively indicates the level at which the final settlement price of expiring FTSE 100 Index Options would be set if the intra-day auction were to cease at that moment.

FTSE 100 Index Options may continue to be available for trading when the FTSE 100 Index is “Held” or “Indicative”. Currently, standardized FTSE 100 Index Options are not available for trading when the Index is “Closed”, while flexible FTSE 100 Index Options are available until 5.00pm (London time).

The closing value of the Index is calculated from the official closing auction uncrossing prices published by the London Stock Exchange following the closing auction call. The closing auction call period for all SETS securities runs from 4.30pm to 4.35pm (London time) (specifically, the closing auction call period has a random end time between 4:35:00pm and 4:35:30pm). In addition, the closing auction call period may be extended under certain circumstances in order to reduce the likelihood of unrepresentative prices being generated. During the closing auction, continuous trading is disabled, although London Stock Exchange member firms are able to enter and delete orders. Orders are then matched during the closing auction uncrossing period using the London Stock Exchange’s uncrossing algorithm.

#### The FTSE 100 Index Option Contract Specification

LIFFE lists two types of FTSE 100 Index Options, a standardized European-style exercise Option and a flexible Option (which may be European-style exercise or American-style exercise). European-style FTSE 100 Index Options are exercisable only on their expiry day, whereas American-style FTSE 100 Index Options are exercisable on any business day up to and including their expiry day.

Each FTSE 100 Index Option represents a notional value of £10 multiplied by the FTSE 100 Index. This means that if the FTSE 100 Index stands at 6000, each contract has an underlying value of £60,000.



## Expiry Months and Exercise Prices:

	<b>Standardized FTSE 100 Index Option (European-style)</b>	<b>Flexible FTSE 100 Index Option (American and European-style)</b>
Expiry Months/Expiry Days	Eight quarterly months on March, June, September, December cycle plus such additional months that the four nearest calendar months are always available for trading.	Any business day as specified by the counterparties, up to, and including, the business day five years and six months from the date the contract is made.
Exercise Prices	Please see below	Any whole number of index points

For FTSE 100 Index Options within LIFFE CONNECT®, multiple series intervals are applicable per expiry month. The around-the-money series have smaller series intervals in comparison to the deeper in-and-out-of-the-money series. In this way, LIFFE seeks to create more diversity between the series available for trading.

LIFFE will introduce a minimum number of series per expiry month depending on the remaining lifetime of the expiry month. The minimum number of in-the-money (ITM), at-the-money (ATM<sup>12</sup>) and out-of-the-money (OTM) series to be introduced initially will be as follows:

### **≤ 1 month to expiry**

For expiry months with a remaining lifetime of up to and including 1 month:

At least 21 series

- 5 series around the money - Interval Scale A: 1<sup>st</sup> ITM+2<sup>nd</sup> ITM+ATM+1<sup>st</sup> OTM+2<sup>nd</sup> OTM
- 16 series - Interval Scale B: 3<sup>rd</sup> ITM until 10<sup>th</sup> ITM+  
3<sup>rd</sup> OTM until 10<sup>th</sup> OTM

### **> 1 to ≤ 4 months to expiry**

For expiry months with a remaining lifetime exceeding 1 month and up to and including 4 months:

At least 21 series

- 15 series around the money - Interval Scale B: 1<sup>st</sup> ITM until 7<sup>th</sup> ITM+ATM+  
1<sup>st</sup> OTM until 7<sup>th</sup> OTM
- 6 series - Interval Scale C: 8<sup>th</sup> ITM+9<sup>th</sup> ITM+10<sup>th</sup> ITM+  
8<sup>th</sup> OTM+9<sup>th</sup> OTM+10<sup>th</sup> OTM

<sup>12</sup> The option series whose price differs the least from the price of the underlying index is considered to be the at-the-money series. There will be no at-the-money series in a situation where the market price of the underlying security is exactly halfway between two series.

### > 4 to ≤ 12 months to expiry

For expiry months with a remaining lifetime exceeding 4 months and up to and including 12 months:  
At least 21 series

- 15 series around the money - Interval Scale C: 1<sup>st</sup> ITM until 7<sup>th</sup> ITM+ATM+1<sup>st</sup> OTM until 7<sup>th</sup> OTM
- 6 series - Interval Scale D: 8<sup>th</sup> ITM+9<sup>th</sup> ITM+10<sup>th</sup> ITM+8<sup>th</sup> OTM+9<sup>th</sup> OTM+10<sup>th</sup> OTM

### > 12 to ≤ 24 months to expiry

For expiry months with a remaining lifetime exceeding 12 months and up to and including 24 months:  
At least 21 series

- 7 series around the money - Interval Scale C: 1<sup>st</sup> ITM+2<sup>nd</sup> ITM+3<sup>rd</sup> ITM +ATM+1<sup>st</sup> OTM+2<sup>nd</sup> OTM+3<sup>rd</sup> OTM
- 14 series - Interval Scale D: 4<sup>th</sup> ITM until 10<sup>th</sup> ITM+4<sup>th</sup> OTM until 10<sup>th</sup> OTM

The exercise price of each such series is fixed in accordance with the following scheme:

FTSE 100 Index Interval Scheme in Pence			
Interval Scales			
Scale A	Scale B	Scale C	Scale D
25	50	100	200

The following tables provide a summary of the exercise prices per expiry month at time of listing<sup>13</sup>:

Time to maturity	1 month	2,3,4 months	6,9,12 months	15,18,21,24 months
	<div> <div>Scale B</div> <div>Scale A</div> <div>Scale B</div> </div>	<div> <div>Scale C</div> <div>Scale B</div> <div>Scale C</div> </div>	<div> <div>Scale D</div> <div>Scale C</div> <div>Scale D</div> </div>	<div> <div>Scale D</div> <div>Scale C</div> <div>Scale D</div> </div>
	<div> <div>X</div> <div>IX</div> <div>VIII</div> <div>VII</div> <div>VI</div> <div>V</div> <div>IV</div> <div>III</div> <div>II</div> <div>I</div> <div>ATM</div> <div>I</div> <div>II</div> <div>III</div> <div>IV</div> <div>V</div> <div>VI</div> <div>VII</div> <div>VIII</div> <div>IX</div> <div>X</div> </div>	<div> <div>X</div> <div>IX</div> <div>VIII</div> <div>VII</div> <div>VI</div> <div>V</div> <div>IV</div> <div>III</div> <div>II</div> <div>I</div> <div>ATM</div> <div>I</div> <div>II</div> <div>III</div> <div>IV</div> <div>V</div> <div>VI</div> <div>VII</div> <div>VIII</div> <div>IX</div> <div>X</div> </div>	<div> <div>X</div> <div>IX</div> <div>VIII</div> <div>VII</div> <div>VI</div> <div>V</div> <div>IV</div> <div>III</div> <div>II</div> <div>I</div> <div>ATM</div> <div>I</div> <div>II</div> <div>III</div> <div>IV</div> <div>V</div> <div>VI</div> <div>VII</div> <div>VIII</div> <div>IX</div> <div>X</div> </div>	<div> <div>X</div> <div>IX</div> <div>VIII</div> <div>VII</div> <div>VI</div> <div>V</div> <div>IV</div> <div>III</div> <div>II</div> <div>I</div> <div>ATM</div> <div>I</div> <div>II</div> <div>III</div> <div>IV</div> <div>V</div> <div>VI</div> <div>VII</div> <div>VIII</div> <div>IX</div> <div>X</div> </div>

A price established on a trading day (T) will be the reference used to determine the introduction of additional series on the next trading day (T+1) to have at least the minimum number of in- and out-of-the-money series listed.

<sup>13</sup> Series shown above ATM are OTM calls/ITM puts. Series shown below ATM are ITM calls/OTM puts.

Premiums: For the FTSE 100 Index Options, the premium for each series is quoted in Index points. Thus a quote of, say, 30 Index points would represent a total consideration per contract of £300 (plus commission). The minimum permitted price fraction is 1/2 of an Index point.

#### Special Features of flexible Options

It should be noted that:

- (i) a flexible Option cannot be introduced with the same expiry day and exercise price as an existing standardized European-style exercise FTSE 100 Index Option; and
- (ii) when a standardized European-style exercise FTSE 100 Index Option contract is listed with the same exercise price and expiry date as an existing flexible Option series, the existing flexible Option series will be novated into the corresponding standardized European-style exercise FTSE 100 Index Option contract series.

#### Calculation of Index Value for Exercise of FTSE 100 Index Options

The expiry day (known as the “Last Trading Day”) for the standardized FTSE 100 Index Option is the third Friday of the expiry month. On that day, an intra-day auction is held on the London Stock Exchange which is used to derive the price of each component stock in the FTSE 100 Index. The intra-day auction begins at 10.10.00am (London time) and ends at a random time between 10.15.00am and 10.15.30am (London time) unless pre-set price parameters are breached (in which case the auction in the stock(s) in question is extended until 10.29.30am (London time) at the latest).

The prices derived from the intra-day auction are used to determine the Expiry Value of the FTSE 100 Index on which the final settlement price (known as the “Exchange Delivery Settlement Price” or “EDSP”) of the standardized FTSE 100 Index Option is based. Trading in expiring series ceases as soon as reasonably practicable following determination of the Expiry Value.

The same process is applied to those flexible FTSE 100 Index Options which have an expiry date of the third Friday of the month. For those flexible FTSE 100 Index Options which have an expiry date other than the third Friday of the month, the EDSP will be determined by reference to the prices of constituent stocks derived through the closing auction on the London Stock Exchange. On such days, trading in the expiring series of the flexible FTSE 100 Index Option ceases at 4.30pm (London time).

## Exercise, Assignment and Settlement of the FTSE 100 Index Option

Exercise entitles the holder to cash settlement only, in pounds sterling, of an amount equal to £10 times the difference between the EDSP and the exercise price of the contract. Standardized FTSE 100 Index Options, and those flexible FTSE 100 Index Options with European-style exercise, may only be exercised on the relevant expiry day (Last Trading Day). In contrast, those flexible FTSE 100 Index Options with American-style exercise may be exercised on any business day, up to and including the relevant expiry day. If the holder wishes to exercise an option, the holder should instruct its broker to ensure that an Exercise Notice is submitted to LCH.Clearnet. An Exercise Notice may be submitted to LCH.Clearnet either manually or automatically. Options will only be exercised if an Exercise Notice is submitted to LCH.Clearnet. On the Last Trading Day, expiring FTSE 100 Index Options that are in-the-money by the amount specified by the Clearing Member in CPS (the Clearing Processing System) – or, if the Clearing Member has not so specified, by the amount established as the CPS default setting – will be exercised by an Exercise Notice being sent automatically to LCH.Clearnet.

When a FTSE 100 Index Option contract is exercised, a writer of the same series is randomly allocated overnight. Settlement of the cash consideration then takes place the day after the day of submission of the Exercise Notice (whether effected manually or by automatic exercise).

## Position Limits

There are no position limits for any of the option contracts traded on LIFFE.

## TAXATION AND TRANSACTION COSTS

Before engaging in UK Equity and UK Index Options transactions, US entities should consult their own tax advisors with respect to UK and US federal, state and local tax considerations relevant to them. The following discussion does not purport to be exhaustive or applicable to particular circumstances.

### UK Taxes

Advice has been received from external accountants that US resident investors are not liable for UK income, capital gains, corporation or value added (VAT) taxation on transactions in LIFFE options, unless their options dealings are transacted in the UK through a permanent establishment in the UK, or are associated with such an establishment's trade. A US resident's transactions in LIFFE options through a UK broker who acts for the non-resident as part of its normal business would not alone establish a taxable presence of the US resident in the UK.

There is no stamp duty/Stamp Duty Reserve Tax (or other transfer tax) payable on transactions in UK Equity and Index Options. If the underlying security is bought by exercise of a call option or sold by exercise of a put option, stamp duty/Stamp Duty Reserve Tax will be payable by the purchaser, unless registered as an options intermediary under UK legislation, on the transfer of the underlying security. When the settlement of the underlying security transfer is conducted through the CREST system, the applicable stamp duty/Stamp Duty Reserve Tax is automatically collected and paid to Her Majesty's Revenue and Customs ("HMRC"). Please see page 42 for an explanation of the CREST system.

### US Taxes

Income tax considerations in the US may significantly affect the profitability of options transactions, including those effected abroad. The rules governing federal income taxation of options transactions, domestic and foreign, by US entities are complex and often depend upon an investor's particular situation. In this connection, advice has been received from US counsel that LIFFE options held by US entities will not be subject to the mark-to-market provisions of the Internal Revenue Code (the "Code") or treated as "qualified covered call options" for purposes of the provisions of the Code governing straddles, because LIFFE currently is not designated by the Secretary of the Treasury as a "qualified board or exchange" for those purposes. The position would change if LIFFE were so designated in the future, and US transactors should take that into account. In addition, the acquisition and disposition of pounds sterling by investors whose "functional currency" is the US dollar may be subject to the provisions of the Code governing transactions in foreign currency.

## Transaction costs

The transaction costs borne by investors include brokers' commissions that reflect charges for opening and closing positions and for exercise. LIFFE does not impose minimum or maximum commission rates, which are a matter to be decided between the member broker and customer. LIFFE charges an exchange fee for contracts traded on LIFFE CONNECT<sup>®</sup> (currently 25 pence per contract for UK Index Options, and 37 pence per contract for UK Equity Options). In each case, LCH.Clearnet charges a clearing fee of 3 pence per contract. LCH.Clearnet also charges an exercise fee (currently 20 pence per contract) to the exercisor only plus a £3 CREST "per transaction" charge for UK Equity Option delivery. LIFFE members generally pass these charges on to clients.

Bclear transactions fees and fee caps for UK Equity Options and Index Options are shown below:

### UK Equity Options

Fee per contract		Fee Caps per Transaction			
		Proprietary Business		Client Business	
Exchange Fee	Clearing Fee	Exchange Fee	Clearing Fee	Exchange Fee	Clearing Fee
£0.25	£0.03	£60	£15	£120	£30

### UK Index Options

Fee per contract		Fee Caps per Transaction			
		Proprietary Business		Client Business	
Exchange Fee	Clearing Fee	Exchange Fee	Clearing Fee	Exchange Fee	Clearing Fee
£0.22	£0.03	£600	£150	£1,200	£300

For transactions with multiple legs, each leg is charged separately, up to the fee cap (i.e. for these purposes, each leg is treated as a separate transaction).

## LCH.CLEARNET, CLEARING AND SETTLEMENT

LCH.Clearnet is a Recognised Clearing House under the Financial Services and Markets Act 2000. It provides central counterparty services to the following markets and services:

- London Stock Exchange (LSE)
- Virt-x
- LIFFE
- London Metal Exchange (LME)
- Intercontinental Exchange (ICE) and ICE Futures
- RepoClear and SwapClear

As legal counterparty to each clearing member in respect of registered business, LCH.Clearnet bears any loss arising from the default of a clearing member, beyond the margin deposits held as security in respect of the defaulting member's liabilities. LCH.Clearnet's supplementary resources for use in default cases, should those margin deposits be insufficient, comprise a £582 million Default Fund<sup>14</sup>, which is provided by members and held in cash by LCH.Clearnet, and £200 million of default insurance cover. Each member's Default Fund contribution is assessed every three months on the basis of that member's initial margin and (in the case of exchange traded derivatives) trading volumes over the preceding three months. The Default Fund is mutual in nature, in the sense that any loss faced by LCH.Clearnet as a result of a default which cannot be met from the defaulter's margin cover at LCH.Clearnet or from his contribution to the Default Fund will be met by the Default Fund generally. Customers of a defaulting clearing member have no contractual relationship with LCH.Clearnet, but are protected to the extent of their client agreement and any segregation arrangements in place with that member. LCH.Clearnet uses a stress testing model to ensure that its post-default financial backing is of appropriate size. The stress testing model assesses the adequacy of initial margin requirements and the £582 million Default Fund on the basis of extreme price movements in all contracts cleared by LCH.Clearnet.

### Trade Registration

Once an options trade has been executed in LIFFE CONNECT<sup>®</sup> or confirmed within Bclear, a message will be sent automatically to the trader(s) who have executed/submitted the trade to notify them of such execution/confirmation. At the same time, for both LIFFE CONNECT<sup>®</sup> and Bclear, the details of the trade are transmitted automatically to LIFFE's Trade Registration System ("TRS"), which is a real-time matching system.

TRS provides members with the facility to perform the following post trade administration functions:

- Allocation of Trades: When a trade has been undertaken on a brokerage basis on behalf of another member, TRS provides a facility for the allocation process to take place through a 'give-up' transaction.

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<sup>14</sup> This fund is a single fund used in respect of the markets and services set out above.

- Assignment of Trades: TRS provides a facility to enable members to assign trades to one of a number of specific account types. This process allows trades to be assigned to the correct clearing account prior to clearing processing being undertaken at the end of the day.

In addition, TRS also gives users a wide range of enquiry and trade report functions.

An options trade that has been matched in TRS is passed to LCH.Clearnet for registration after the close of trading on the same day. Registration occurs one hour after TRS' end of day signal is sent to LCH.Clearnet (i.e. the end of day signal is sent when TRS closes, which is normally at 09:45pm London time). Upon registration LCH.Clearnet is interposed as the buyer to every clearing member seller, and seller to every clearing member buyer on a principal-to-principal basis. The day after a trade is made the clearing member buyer will pay premium to LCH.Clearnet, by 10:00am London time, and LCH.Clearnet will pay the premium to the clearing member seller by 1:30pm London time. While no direct link then remains between the buyer and seller in the original trade, for every current holder of an options contract there is a current writer with a corresponding open position.

When a holder exercises a contract, LCH.Clearnet appoints, by a process of random selection, a clearing member who is, or has a customer who is, a writer of a contract in the same series, to deliver or to receive shares or to cash settle in accordance with the terms of the contract. LCH.Clearnet becomes a principal to each resulting equity delivery contract; for example, the clearing member exercisor of a put option will deliver the shares to LCH.Clearnet's account within CREST (the UK equity settlement system), and LCH.Clearnet will deliver the shares to the selected writer.

As the counterparty to every clearing member LCH.Clearnet reduces the scope for counterparty risk between clearing members. LCH.Clearnet is legally responsible for the financial performance of the contracts that it has registered, and any resulting delivery contracts. All clearing members deposit margin with LCH.Clearnet to cover the risk on their net positions.

LCH.Clearnet is not counterparty to trades with customers. Behind contracts between LCH.Clearnet and a clearing member there may exist further "back-to-back" contracts; for example, if a customer buys an option the clearing member is the seller to the client and the buyer from LCH.Clearnet (once the trade has been registered). These customer contracts are subject to LIFFE Rules, but LCH.Clearnet is not a party to them.

#### LCH.Clearnet Participants

LIFFE has two types of clearing members: Individual Clearing Members who clear and settle business for their own account or, in the case of broker-dealers, on behalf of their customers; and General Clearing Members who, in addition, clear and settle business on behalf of other LIFFE members. All trades of non-clearing members must be cleared through a specific clearing member.



All clearing members must also be members of LCH.Clearnet and all are subject to standards of capital adequacy<sup>15</sup>. Clearing members must also satisfy LIFFE and LCH.Clearnet that they have adequate systems and controls to clear and settle trades.

Clearing members undertaking business for clients are subject to UK client money rules or, if they are authorized outside the UK, similar rules of the relevant regulator. In the European Union, those rules are governed by the Markets in Financial Instruments Directive. Most LIFFE clearing members are UK-authorized. They are required to segregate customer funds except in instances where the investor, if permitted to do so, contracts out of the segregation requirement. Each clearing member may have two accounts with LCH.Clearnet: one for segregated customer business (the “Client margin account”), and one for all house and non-segregated client business (the “House margin account”). Neither LCH.Clearnet nor the clearing members can offset liabilities on the House margin account with credits arising on the Client margin account.

#### Time of Settlement

All trades on LIFFE are transacted for settlement by payment of premium and initial deposit of margin by the writer, by 10.00am London time on the business day after the day of trade. Member brokers will require their customers to provide them with the agreed premium, and if writers with margin, before that time. Although a minimum margin is calculated by LCH.Clearnet, a member may increase this for customers at its discretion.

On the business day after the day of trade, LCH.Clearnet makes available to all clearing members statements showing their transactions for the previous day with details of premiums payable and receivable, together with fees and margin requirements. Any payment due must be made to LCH.Clearnet by 10.00am London time and monies payable by LCH.Clearnet will be available to clearing members from 1.30pm. Sterling, dollar and euro transactions are processed with same day value the next business day. Similar arrangements apply in the case of Net Liquidation Value (NLV) payments, which are discussed below.

LCH.Clearnet has established procedures for settlement and margin collection for all of the currencies in which LIFFE contracts are denominated. It is mandatory for clearing members to maintain appropriate currency accounts at LCH.Clearnet approved banks for all contracts they clear. In addition, LCH.Clearnet has formal multi-currency overdraft and borrowing facilities with a number of major banks.

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<sup>15</sup> Standards of capital adequacy are set by LCH.Clearnet rather than by LIFFE. Clearing members will, however, also be subject to capital adequacy requirements set by their regulators.

## Margin Maintenance

Margin provided to LCH.Clearnet by or on behalf of writers is required to be maintained.

LCH.Clearnet revalues the margin position on at least a daily basis to take account of changes or volatility in the market price of the underlying UK security or Index and in LCH.Clearnet's valuation of margin collateral provided in the form of securities. All clearing members must provide LCH.Clearnet with margin cover to cover the risk on their total net positions for each account. Margin is also called on equity delivery contracts resulting from the exercise of UK Equity Options. LCH.Clearnet revalues the margin requirements each night using the London SPAN method. London SPAN (Standard Portfolio Analysis of Risk) was adapted from the Chicago Mercantile Exchange's margining system, which is designed to match margin to risk. London SPAN does this by simulating how a portfolio would react to changing market conditions. Understanding London SPAN is published by LCH.Clearnet and is available from the LCH.Clearnet website at ([www.lchclearnet.com](http://www.lchclearnet.com)). The initial margin requirement for the portfolio is the largest loss identified under these various market conditions that might reasonably occur, taking into account risk offsets within the portfolio, including those between index options and index futures. Initial margin is refunded when the position is closed. It is designed to protect LCH.Clearnet against the worst likely loss from one or two day's move in the market. Net Liquidation Value ("NLV") is the value of the portfolio at closing market prices. It represents the income or expenditure which would be associated with closing out an Equity or Index Option. This figure is added to initial margin to give the total margin requirement. During the day LCH.Clearnet monitors market prices and clearing members' positions and may call for additional margin payments. LCH.Clearnet's margin requirements are only applicable to clearing members. Brokers set the margin requirements applicable to their customers.

## Margin Collateral

Arrangements for the provision of margin cover are a matter for negotiation between the customer, broker and clearing member.

LCH.Clearnet accepts a variety of collateral types from clearing members in respect of their margin liabilities to LCH.Clearnet. These apply to both initial margin and NLV payments. Members may meet margin requirements by cash payments in the following currencies: sterling, US dollars, yen, Swiss francs, and-euro. In addition, LCH.Clearnet will accept an extensive range of collateral including approved bank guarantees, certain UK treasury bills, UK gilts, sterling and US dollar certificates of deposit, German, Italian and Spanish government bonds and UK equities. Any such securities must be charged to LCH.Clearnet by the clearing member in accordance with LCH.Clearnet procedures. Any UK equities charged to LCH.Clearnet as collateral must be registered in the name of a UK depository company approved by LCH.Clearnet. Where customers charge UK equities to clearing members or other brokers, without intending those securities to be charged by a clearing member in favour of LCH.Clearnet, the parties may make such arrangements as they wish for the collateral.

To avoid frequent changes in the amount of collateral provided, clearing members may lodge margin in excess of the LCH.Clearnet minimum. LCH.Clearnet pays interest to clearing members on such

balances. Interest payments are made at the London Deposit Rate. This is currently the overnight London Inter-Bank Bid Rate (LIBID) minus 25 basis points.

With the customer's permission, equities belonging to a client may be "passed through" the customer's broker to the clearing member and to LCH.Clearnet. Any securities over which LCH.Clearnet has a security interest will be used to cover the clearing member's liabilities to LCH.Clearnet; these liabilities are not the same as, and may be significantly larger than, the customer's liabilities to its broker and in the event of a default such securities may be sold by LCH.Clearnet without reference to the customer. Where a customer only permits a security interest in such equities, in favour of its direct counterparty (the broker or clearing member), the clearing member may need to provide other forms of margin cover to LCH.Clearnet.

#### Certificateless Transactions

No certificates of ownership are issued to holders of LIFFE options contracts. LCH.Clearnet maintains a daily record of contracts held and written, and every member firm of LIFFE is required to keep a continuous record of the option contracts held or written by its customers. Transactions in LIFFE options are evidenced by contract notes (advices) and periodic statements issued by members to their customers.

While LIFFE members are subject to general regulatory oversight by LIFFE and most by the FSA, neither LIFFE nor LCH.Clearnet is responsible for inaccuracies or omissions in advices or statements rendered to customers by member firms.

Because option contracts held or written by customers, as well as the day-to-day margin requirements, are in the books of the member through which the original transactions were made, further transactions should be made through the firm which executed the opening purchase or sale. A customer may request the transfer of its open option positions from one firm to another by issuing to both the transferring firm and the receiving firm a written instruction to transfer its account.

## UK EQUITY SETTLEMENT SYSTEM

### LCH.Clearnet Settlement of LIFFE Options Transactions

For both buy and sell transactions in LIFFE options, premiums are payable or receivable on the business day following the trade. Exercise of UK Index Options, and certain flexible UK Equity Options, is for cash only settlement, which takes place on the business day following exercise. Such settlements of opening and closing transactions in all LIFFE options and of exercise of UK Index Options are conducted with LCH.Clearnet. None of these involves the UK equity settlement system.

### Equity Settlement Period

Under three-day rolling settlement, T+3, introduced on 5 February 2003, all securities transactions must be settled three business days after the date of the trade. Equity transactions arising as a result of the exercise of an equity option are settled four days after the Exercise Notice is received by LCH.Clearnet.

### CREST

CREST is the electronic settlement system for shares and other corporate securities in the UK and Ireland. It is owned and operated by Euroclear UK and Ireland Limited, which is a Recognised Clearing House under the UK Financial Services and Markets Act. 2000. CREST provides for the simultaneous exchange of payment and securities. Shares of companies and other corporate securities that are settled through CREST are fully dematerialised; that is, they exist only in electronic form and no certificates exist anywhere for such shares or securities. That said, if a shareholder requires physical certificates he is able to obtain them, through his broker, by using the CREST Courier and Sorting Service ("CCSS"). The CCSS takes receipt of, and dispatches, physical certificates in respect of share transactions being settled through CREST. Certificates received in this way will be passed by CCSS to the registrar for the securities in the case of sales by a person who has physical certificates. The registrar will pass securities to the CCSS in cases where the purchaser has requested a physical certificate. The CCSS matches the certificates with electronic instructions entered into CREST (see below).

The process of settlement begins with the parties to a transaction sending their electronic instructions to CREST as soon as possible after dealing. In the case of the exercise of a UK Equity Option, LCH.Clearnet will be both the principal to the exercising clearing member and to the clearing member which has been selected as the writer of the UK Equity Option. CREST matches each party's electronic instructions. Once this has been done, CREST checks that the seller has adequate stock available to deliver and that the buyer has adequate credit available to pay. If the necessary conditions are satisfied, the transaction will be settled. If not, CREST will continue to check throughout that day and continually thereafter until it is possible to settle the transaction. All transactions are settled gross in CREST and are not netted.

The legal basis for these arrangements is provided by the UK Uncertificated Securities Regulations 2001.

#### Additional Information

A number of booklets are available from LIFFE and LCH.Clearnet which give further details on LIFFE options and the margining and settlement systems for these products. Information about LIFFE Rules is also available.

## APPENDIX ONE

### Bclear

The following are eligible products for submission by US members, affiliates and authorized customers:

Standardized physical delivery UK Equity Options (American-style exercise) and flexible physical delivery and cash settled UK Equity Options (American-style exercise and European-style exercise).

Standardized cash settled FTSE 100 Index Options (European-style exercise) and flexible cash settled FTSE 100 Index Options (American and European-style exercise)

### Minimum volume thresholds

UK Equity Options submitted to Bclear are subject to the following minimum volume thresholds:

Country	Standardized <sup>16</sup>	Flexible
UK	250	1

UK Index Options submitted to Bclear are subject to the following minimum volume thresholds:

Index	Standardized Index Options <sup>17</sup>	Flexible Index Options
FTSE 100	500	100

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<sup>16</sup> Standardised UK Equity Options are those which have the same economic characteristics (i.e. underlying share, exercise price, expiry date, exercise style and settlement style) as those available on LIFFE CONNECT®

<sup>17</sup> Standardised Index Options are those which have the same economic characteristics (i.e. underlying index, exercise price, expiry date, exercise style and settlement style) as those available on LIFFE CONNECT®.

Form SEC A

**LIFFE Equity and Index Options in  
the United States of America**

To:        Membership Department  
             LIFFE  
             Cannon Bridge House  
             1 Cousin Lane  
             London EC4R 3XX

I confirm that we transact or intend to transact business in Approved  
Options in the United States of America.

From:    Name .....

             Position .....

             Member .....

             Date .....