EURONEXT DERIVATIVES MARKETS

AMSTERDAM NOTICE No. 08/012

Equivalent Notices are being issued to all Liffe markets.

ISSUE DATE: 14 April 2008

Fair Value Volatilities Consultation

Executive Summary

The purpose of this paper is to consult the market about a specific element of the fair value method within the Corporate Actions Policy. Members are requested to submit in writing any comments on the alternatives outlined in this paper by Friday 2 May 2008 to Quality of Derivative Markets in Amsterdam.

This Notice replicates the substance of Amsterdam Notice 07/046, issued on 19 December 2007, concerning the determination of implied volatilities. Given the nature of the consultation, Liffe would like to urge all Members who have not responded to Amsterdam Notice 07/046 to respond to this Notice setting out whether or not they support the proposed approach for determining implied volatilities. This will be the last opportunity to do so because, once all Member feedback has been assessed following the 2 May 2008 deadline, Liffe will decide whether or not to change the method used to determine implied volatilities.

1. On 15 November 2004, the harmonised Corporate Actions Policy became effective for all Liffe markets. This policy provides for a single approach to adjust contract specifications of Liffe listed options and futures when underlying shares are subject to a corporate action.

2. When there is a cash takeover offer for a company (or an offer which consists 67% or more of cash), the policy determines that outstanding options and futures are settled in cash using the Fair Value method. The purpose of this Notice is to obtain feedback from market participants about a specific element of the Fair Value method, as described below.

3. Currently, the implied volatilities used for Fair Value calculations are based on the implied volatilities of the settlement prices on the last ten business days prior to the announcement of the (proposed) takeover offer. In order to calculate the implied volatilities, interest rates (applicable for the relevant currency) and dividend forecasts (if available from Markit Dividends) are taken into account.

   Liffe has been requested by members to evaluate the current procedure for determining the volatilities because the current method doesn’t cater for call/put parity. After thorough evaluation, Liffe would like to propose a new procedure, as described below.

4. Liffe proposes to determine the implied volatilities for the purpose of Fair Value method based on the volatilities used by Market Services for establishing daily settlement prices, as published. These volatilities, which normally are equal for calls and puts, are intended to replicate market prices by using appropriate interest rates and dividends to achieve this aim. Dividends used may differ from time to time from those published by Markit Dividends. However, for the calculation of Fair Value prices, interest rates (applicable for the relevant currency) and dividend forecasts (if available from Markit Dividends) as published in the corporate action notice on the day of the announcement of the Offer shall be taken into account, even if these differ from those previously used to establish daily settlement prices.

5. Liffe seeks the assistance of market participants in finding the optimal procedure for determining the volatilities for Fair Value purposes. Liffe would appreciate receiving your comments on the following alternatives, although it is open for members to suggest other potential approaches.

6. Alternative approaches to the determination and publication of implied volatilities are:

   (a) Retain the current approach: Calculate implied volatilities based on the settlement prices of the ten last business days prior to the announcement of the (proposed) takeover offer. The average of each series implied volatility is calculated, excluding the lowest and the highest implied volatility of that series over the ten day period. For the calculation of the implied volatilities, interest rates (applicable for the relevant currency) and Markit dividend forecasts (if not available, such dividends determined by Liffe) are taken into account.

   (b) Alternative approach: Determine volatilities based on the volatilities as published with the daily settlement prices by Market Services, whereby the volatilities are determined by calculating the average of the last ten business days prior to the announcement of the (proposed) takeover offer, excluding the lowest and the highest volatility of the series over the ten day period. In this case, the interest rates and dividends used in the calculation of daily settlement prices and published volatilities will not necessarily be the same as those used to determine the Fair Value. Instead, interest rates (applicable for the relevant currency) and Markit dividend forecasts (if not available, such dividends determined by Liffe) as published in the corporate action notice on the day of the announcement of the (proposed) takeover Offer shall be adopted.

7. Members are requested to submit in writing any comments on the alternatives outlined in this paper by Friday 2 May 2008 to Quality of Derivative Markets (PO Box 19163, 1000 GD Amsterdam) or by e-mail at qualityofmarkets@liffe.com.

For further information in relation to this Consultation Notice, please contact:

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