

The Commission also believes the proposal is consistent with NSCC's obligations to assure the safeguarding of securities and funds in its custody or control and to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions because the proposed rule change should further reduce NSCC's and DTC's risk exposure by amending the NSCC/DTC Agreement to include cross-guaranties for transactions effected through NSCC's CNS system. The guaranties should, among other things, ensure that debits created in DTC's system continue to be collateralized when the securities serving as collateral are delivered into the CNS system as short covers. Additionally, the guarantees also should reduce risk at NSCC by ensuring that long allocations or the appropriate value of long allocations will be available to NSCC to cover certain exposures.

NSCC has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing. The Commission finds good cause for so approving the proposed rule change because the proposed rule change modifies NSCC's rules and the NSCC/DTC Agreement in anticipation of NSCC's and the securities industry's conversion to SDFS on February 22, 1996. Accelerated approval of the proposal will allow NSCC to effect the conversion and to implement the safeguards provided under the NSCC/DTC Agreement on that date.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. § 552, will be available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing will also be available for inspection and copying at the principal office of NSCC. All submissions should

refer to the file number SR-96-03 and should be submitted by March 19, 1996.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-NSCC-96-03) be, and hereby is, approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.¹²

Margaret H. McFarland,
Deputy Secretary.

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[Release No. 34-36860; File No. SR-OCC-96-02]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Accelerated Approval of a Proposed Rule Change to Modify the Stock Loan/Hedge Program to Accommodate Same-Day Funds Settlement

February 20, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on January 16, 1996, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change (File No. SR-OCC-96-02) as described in Items I and II below, which items have been prepared primarily by OCC. The Commission is publishing this notice and order to solicit comments from interested persons and to grant accelerated approval of the proposed rule change.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The purpose of the proposed rule change is to modify OCC's rules relating to its Stock Loan/Hedge Program ("Hedge Program")² to reflect the conversion of the equity securities processing operations of The Depository Trust Company ("DTC") to a same-day funds settlement ("SDFS") system.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, OCC included statements concerning

the purpose of and basis for the proposed rule change and discussed any comments that it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. OCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.³

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

The purpose of the proposed rule change is to make technical modifications to OCC's rules governing its Hedge Program to accommodate the conversion by DTC of its equity securities processing operations to an SDFS system. DTC is scheduled to convert to an SDFS system on February 22, 1996.

Stock loans under the Hedge Program are effected by a book-entry transfer on the books of a correspondent depository (i.e., a securities depository at which OCC has an account and which provides services to OCC in connection with the Hedge Program). The Midwest Securities Trust Company ("MSTC") had acted as the only correspondent depository since the Hedge Program was established. However, MSTC has withdrawn from the securities depository business,⁴ and OCC has made arrangements for DTC to act as a correspondent depository for the Hedge Program.

Under OCC's rules governing the Hedge Program, after two participating clearing members have agreed to the terms of a stock loan, the lending clearing member transfers the stock that is the subject of the loan by book-entry into OCC's account at a correspondent depository. The lending clearing member's transfer instructions identify the borrowing clearing member and specify the amount of cash to be received as collateral by the lending clearing member. Once the stock is delivered into OCC's account, OCC instructs the correspondent depository to redeliver the stock to the account of the borrowing clearing member against payment of the required collateral. The cash payments also are effected through

³ The Commission has modified the text of the summaries submitted by OCC.

⁴ Securities Exchange Act Release No. 36684 (January 5, 1996), 61 FR 1195 (January 17, 1996) [File Nos. SR-CHX-95-27, SR-DTC-95-22, SR-MCC-95-04, SR-MSTC-95-10, and SR-NSCC-95-15] (order approving arrangements relating to a decision by the Chicago Stock Exchange, Inc. to withdraw from the clearance and settlement, securities depository, and branch receives business).

¹² 17 CFR 200.30-3(a)(12) (1995).

¹⁵ 15 U.S.C. 78s(b)(1) (1988).

² For a description of OCC's Stock Loan/Hedge Program, refer to Securities Exchange Act Release No. 32638 (July 15, 1993), 58 FR 39264 [File No. SR-OCC-92-34] (order granting permanent approval of the Stock Loan/Hedge Program).

the facilities of the correspondent depository.

It is essential to OCC's operation of the Hedge Program that OCC must never have a position against a lending clearing member without an offsetting position against a borrowing clearing member unless one of the two clearing members defaults in its obligations with respect to a stock loan. In order to assure that OCC never has a position against a lending or a borrowing clearing member without an offsetting position against another clearing member, OCC rule 2201, concerning the initiation of stock loans, currently specifies that a transfer of stock from a lending clearing member to OCC will not constitute a final entry on the books of a correspondent depository until the related transfer from OCC to the borrowing clearing member constitutes a final entry on the books of the correspondent depository. Similarly, OCC rule 2208, concerning the unwinding or settlement of stock loans, currently specifies that a transfer of stock from a borrowing clearing member to OCC will not constitute a final entry on the books of the correspondent depository until the related transfer from OCC to the lending clearing member constitutes a final entry on the books of the correspondent depository. These rules were drafted to operate in conjunction with MSTC's next-day funds settlement ("NDFS") system as set forth in MSTC's rules.

DTC's SDFS system rules are premised on the concept that any securities transfers in DTC's system will become final at the time that the funds relating to the securities transfer are transferred. Accordingly, as a technical matter, DTC's SDFS system rules do not accommodate the concept currently contained in OCC rules 2201 and 2208 that provide one transfer will become final only when another related transfer becomes final. Therefore, the proposed rule change modifies OCC rules 2201(c) and 2208(a). As amended, rule 2201 regarding the initiation of stock loans provides that OCC may initiate an additional transfer to return stock to a lending clearing member if for any reason it appears to OCC that the related transfer from OCC to the borrowing clearing member will not become final on the books of the correspondent depository on the same day as the transfer from the lending clearing member to OCC. Correspondingly, amended rule 2208 regarding settlement of stock loans (*i.e.*, the return of a stock loan) now provides that OCC may initiate an additional transfer to return loaned stock to a borrowing clearing member if for any reason it appears to

OCC that the related transfer from OCC to the lending clearing member will not become final on the books of the correspondent depository on the same day as the transfer from the borrowing clearing member to OCC. The two rules as modified are compatible with DTC's SDFS system while still preserving OCC's ability to assure that in the ordinary course at the end of each day it will have an offsetting borrow position for each loan position and an offsetting loan position for each borrow position.

OCC believes the proposed rule change is consistent with the requirements of Section 17A of the Act and the rules and regulations thereunder because the proposal will conform OCC's rules to DTC's rules thereby improving the linkage and coordination between two clearing agencies.

(B) Self-Regulatory Organization's Statement on Burden on Competition

OCC does not believe that the proposed rule change would impose any burden on competition.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were not and are not intended to be solicited with respect to the proposed rule change, and none have been received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Section 17A(b)(3)(F) of the Act⁵ requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions, to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible, and to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions. The Commission believes that OCC's proposed procedures relating to its Hedge Program are consistent with OCC's obligations under Section 17A(b)(3)(F) for the reasons discussed below.

The Commission believes that the proposed rule change is consistent with OCC's obligations under Section 17A(b)(3)(F) to promote the prompt and accurate clearance and settlement of securities transactions because the proposal modifies OCC's Hedge Program

to enable it to operate in a SDFS environment at DTC thus allowing the continued use of book-entry movements of stock loans. The Commission also believes OCC's proposed procedures should help to assure the safeguarding of securities and funds which are in the custody or control of OCC or for which OCC is responsible because OCC's amended rules will provide OCC with the authority to make an additional stock loan transfer if it appears the related transfer will not become final on the books of the correspondent depository on the same day. These rules should help to assure that absent a clearing member default OCC will never have a position against a borrowing or lending clearing member without an offsetting position against another clearing member.

Additionally, the Commission believes the proposed rule change should foster cooperation and coordination between OCC and DTC because the modification of OCC's Hedge Program procedures conform OCC's rules to DTC's rules regarding the finality of securities transactions and facilitates OCC's use of DTC as a Correspondent depository in its Hedge Program.

OCC has requested that the Commission find good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing. The Commission finds good cause for so approving the proposed rule change because accelerated approval of the proposed modifications will allow OCC to continue to utilize DTC as a correspondent depository in its Hedge Program following the conversion to SDFS on February 22, 1996. Therefore, OCC participants will be able to continue to utilize the Hedge Program without any disruption.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. § 552, will be

⁵ 15 U.S.C. 78q-1(b)(3)(F) (1988).

available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing will also be available for inspection and copying at the principal office of OCC. All submissions should refer to the file number SR-OCC-96-02 and should be submitted by March 19, 1996.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-OCC-96-02) be, and hereby is, approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-36858; File No. SR-PHLX-95-45]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendment Nos. 1, 2, and 3 to the Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Relating to the Industry Index Option Hedge Exemption

February 16, 1996.

On September 18, 1995, the Philadelphia Stock Exchange, Inc. ("PHLX" or "Exchange") submitted to the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² a proposed rule change to amend PHLX Rule 1001A, "Position Limits," to establish a hedge exemption from industry (narrow-based) index option position and exercise limits.³

The proposed rule change was published for comment in the Federal Register on October 23, 1995.⁴ No comments were received on the proposed rule change. On December 20,

1995, on February 14, 1996, and on February 16, 1996, the PHLX amended its proposal.⁵

The PHLX proposes to exempt from position and exercise limits any position in an industry index option that is hedged by share positions in at least 75% of the number of component stocks of that index or securities convertible into such stock.⁶ Under the proposal, no position in an industry index option may exceed two times the narrow-based index option position specified in PHLX Rule 1001A(b)(i)⁷

⁵ On December 20, 1995, the PHLX amended its proposal to specify certain requirements and monitoring procedures which the Exchange will use in connection with the hedge exemption. See Letter from Gerald D. O'Connell, First Vice President, Market Regulation and Trading Operations, PHLX, to Michael Walinskas, Branch Chief, Office of Market Supervision ("OMS"), Division of Market Regulation ("Division"), Commission, dated December 20, 1995 ("Amendment No. 1"). Among other things, Amendment No. 1 indicates that the PHLX will monitor accounts utilizing the hedge exemption on a daily basis; that the hedging portfolio must be previously established and that options must be carried in an account with an Exchange member; that initiating or liquidating positions should not be conducted in a manner calculated to cause unreasonable price fluctuations or unwarranted price changes; and that the PHLX's Market Surveillance Department must be notified of any material change in the portfolio or futures positions which materially affects the unhedged value of the portfolio. Amendment No. 2 modifies the proposal by providing that the industry index hedge exemption will be two times the existing position and exercise limit rather than three times the limit because the hedged option position is held in addition to the contracts currently permitted under the Exchange's rules. In addition, Amendment No. 2 indicates that offsetting positions in stock index futures options must be deducted from the total market value of the net stock position to determine the value of the hedging portfolio. See Letter from Gerald D. O'Connell, First Vice President, Market Regulation and Trading Operations, PHLX, to Michael Walinskas, Branch Chief, OMS, Division, Commission, dated February 14, 1996 ("Amendment No. 2"). On February 16, 1996, the PHLX amended its proposal by adding subparagraph (C) to paragraph (b)(2) of Commentary .01 in order to make clear that economically equivalent positions must be deducted from the market value of the net stock position to determine the value of the underlying portfolio. See Letter from Gerald D. O'Connell, First Vice President, Market Regulation and Trading Operations, PHLX, to Michael Walinskas, Branch Chief, OMS, Division, Commission, dated February 16, 1996 ("Amendment No. 3").

⁶ The PHLX permits the use of convertible securities in its equity option hedge exemption. See Securities Exchange Act Release No. 32174 (April 20, 1993), 58 FR 25687 (April 27, 1993) (order approving File No. SR-PHLX-92-22). Similarly, other options exchange permit the use of convertible securities in broad-based index hedge exemptions. See Securities Exchange Act Release No. 35738 (May 18, 1995), 60 FR 27573 (May 24, 1995) (File Nos. SR-Amex-95-13, SR-CBOE-95-13, SR-NYSE-95-04, SR-PSE-95-05, and SR-PHLX-95-10) (permanently approving hedge exemption pilot programs).

⁷ PHLX Rule 1001A(b)(i) provides the following position limits for industry index options: 6,000 contracts if any single stock accounted, on average, for 30% or more of the index value during the 30-day period preceding the review; 9,000 contracts if

and the value of the index option position may not exceed the value of the underlying hedging portfolio. The value of the underlying hedging portfolio is determined as follows: (1) the total market value of the net stock position, less (2) the value of: (a) the notional value⁸ of any offsetting calls and puts in the respective index option class; (b) the notional value of any offsetting positions in stock index futures or options; and (c) any economically equivalent positions.⁹

Under the proposal, exercise limits will continue to correspond to position limits, so that investors may exercise the number of contracts set forth as the position limit, as well as those contracts exempted by the proposal, during five consecutive business days.

The proposed exemption requires that both the options and stock positions be initiated and liquidated in an orderly manner. Specifically, a reduction of the options position must occur at or before the corresponding reduction in the stock portfolio position.

The proposed exemption will be available to firm and proprietary traders, as well as public customers. According to the PHLX, because customers rely, for the most part, on a limited number of proprietary traders to facilitate large-sized orders, failure to include such traders in the exemption could effectively reduce the benefit of the exemption to customers.

The PHLX believes that the hedge exemption provision is necessary to better meet the needs of investors who would use PHLX industry index options for investment and hedging purposes. The PHLX states that many institutional traders and portfolio managers deal in dollar amounts much greater than permissible under current position limit levels and have expressed that Exchange position limits hamper their ability to fully utilize Exchange index options. As a result, the PHLX believes that many index options are ineffective for such traders, who may as a result choose to

any single stock accounted, on average, for 20% or more of the index value or any five stocks together accounted, on average, for more than 50% of the index value, but no single stock in the group accounted on average, for 30% or more of the index value during the 30-day period preceding the review; or 12,000 contracts if none of the above conditions apply. See Securities Exchange Act Release No. 36194 (September 6, 1995), 60 FR 47637 (order approving File No. SR-PHLX-95-16) (increasing position limits for industry index options to 6,000, 9,000 or 12,000 contracts).

⁸ Notional values are determined by adding the number of contracts and multiplying the total by the multiplier, expressing that number in dollar terms.

⁹ See Amendment Nos. 2 and 3, *supra* note 5.

⁶ 17 CFR 200.30-3(a)(12) (1995).

¹ 15 U.S.C. 78s(b)(1) (1988).

² 17 CFR 240.19b-4 (1995).

³ Position limits impose a ceiling on the number of option contracts which an investor or group of investors acting in concert may hold or write in each class of options on the same side of the market (i.e., aggregating long calls and short puts or long puts and short calls). Exercise limits prohibit an investor or group of investors acting in concert from exercising more than a specified number of puts or calls in a particular class within five consecutive business days.

⁴ See Securities Exchange Act Release No. 36380 (October 17, 1995), 60 FR 54403.