

## PROSPECTIVE PAYMENT ASSESSMENT COMMISSION

### Notice of Meeting

Notice is hereby given of the meetings of the Prospective Payment Assessment Commission on Tuesday and Wednesday, September 23 and 24, 1997, at the Madison Hotel, 15th & M Streets, NW, Washington, DC, 202/862-1600.

The Full Commission will convene at 9:00 a.m. on September 23, 1997, and adjourn at approximately 5:00 p.m. On Wednesday, September 24, 1997, the meeting will convene at 9:00 a.m. and adjourn at approximately 12:30 p.m. The meetings will be held in Executive Chambers 1, 2, and 3 each day.

All meetings are open to the public.

**Donald A. Young,**

*Executive Director.*

[FR Doc. 97-24431 Filed 9-15-97; 8:45 am]

BILLING CODE 6820-BW-M

## SECURITIES AND EXCHANGE COMMISSION

### Proposed Collection; Comment Request

Upon written request, copies available from: Securities and Exchange Commission, Office of Filings and Information Services, Washington, DC 20549.

Extension: Rule 29, File No. 270-169, OMB Control No. 3235-0149; Rule 83, File No. 270-82, OMB Control No. 3235-0181.

Notice is hereby given that, pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501, *et seq.*), the Securities and Exchange Commission ("Commission") requests comments on the collections of information summarized below. The Commission plans to submit these collections of information to the Office of Management and Budget for extension and approval.

Rule 29 [17 CFR 250.29] states that "[a] copy of each annual report submitted by any registered holding company or any subsidiary thereof to a State Commission covering operations not reported to the Federal Energy Regulatory Commission shall be filed with the Securities and Exchange Commission no later than ten days after such submission." The Commission receives about 62 annual reports per year under this regulation, which imposes an annual burden of about 15.5 hours.

Rule 83 [17 CFR 250.83] authorizes an exemption from the "at cost" requirements of Section 13(b) for "the performance of any service, sales, or

construction contract for any associate company which does not derive, directly or indirectly, any material part of its income from sources within the United States and which is not a public utility company operating within the United States \* \* \*." The Commission receives about one application per year under Rule 83, which imposes an annual burden of about three hours.

The estimates of average burden hours are made for the purposes of the Paperwork Reduction Act and are not derived from a comprehensive or even a representative survey or study of the costs of Commission rules and forms.

It should be noted that "an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number."

Written comments are invited on (a) whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (b) the accuracy of the agency's estimate of the burden of the collection of information; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology. Consideration will be given to comments and suggestions submitted in writing within 30 days of this publication.

Please direct your written comments to Michael E. Bartell, Associate Executive Director, Securities and Exchange Commission, 450 5th Street, N.W. Washington, DC 20549.

Dated: September 5, 1997.

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 97-24545 Filed 9-15-97; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39032; File Nos. SR-Amex-96-19; SR-DBOE-96-79; SR-PCX-97-09]

### Self-Regulatory Organizations; Order Granting Approval to Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 to Proposed Rule Change by the American Stock Exchange, Inc. and the Chicago Board Options Exchange, Inc., and Order Granting Approval to Proposed Rule Change by the Pacific Exchange, Inc., Relating to the Elimination of Position and Exercise Limits for FLEX Equity Options

September 9, 1997.

#### I. Introduction

On May 21, 1996, December 27, 1996, and April 1, 1997, respectively, the American Stock Exchange, Inc. ("Amex"), the Chicago Board Options Exchange, Inc. ("CBOE"), and the Pacific Exchange, Inc. ("PCX") (collectively the "Exchanges"), submitted to the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> proposed rule changes to eliminate position and exercise limits<sup>3</sup> for FLEX Equity options under a two-year pilot program.<sup>4</sup>

Notice of the proposed rule changes appeared in the **Federal Register** on June 12, 1996, January 17, 1997, and May 20, 1997, respectively.<sup>5</sup> No comments were received on the proposed rule changes. The Amex subsequently filed Amendment No. 1 to its proposed rule change on February 3,

<sup>1</sup> 15 U.S.C. 78s(b)(1) (1988).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Position limits impose a ceiling on the aggregate number of option contracts on the same-side of the market that an investor, or group of investors acting in concert, may hold or write. Exercise limits impose a ceiling on the aggregate long positions in option contracts that an investor, or group of investors acting in concert, can or will have exercised within five consecutive business days.

<sup>4</sup> In general, FLEX Equity options provide investors with the ability to customize basic option features including size, expiration date, exercise style, and certain exercise prices. (See Securities Exchange Act Release No. 37726 (September 25, 1996), 61 FR 51474 (October 2, 1996), regarding restrictions on the available exercise prices for FLEX Equity call options (File Nos. SR-Amex-96-29, SR-CBOE-96-56, and SR-PSE-96-31)).

<sup>5</sup> See Securities Exchange Act Release Nos. 37280 (June 5, 1996), 61 FR 29774 (June 12, 1996) (File No. SR-Amex-96-19); 38152 (January 10, 1997), 62 FR 2702 (January 17, 1997) (File No. SR-CBOE-96-79); and 38616 (May 12, 1997), 62 FR 27642 (May 20, 1997) (File No. SR-PCX-97-09).

1997.<sup>6</sup> The CBOE subsequently filed Amendment No. 1 to its proposed rule change on May 13, 1997.<sup>7</sup> This order approves the Exchanges' proposals, as amended, and solicits comments on Amex Amendment No. 1 and CBOE Amendment No. 1.

## II. Background

On February 14, 1996 and June 19, 1996, the Commission approved the Exchanges' proposals to list and trade FLEX Equity options on specified equity securities.<sup>8</sup> According to the Exchanges, those proposals were designed to provide investors with the ability, within specified limits, to designate certain terms of the options. In support of their proposals, the Exchanges stated that in recent years, an over-the-counter ("OTC") market in customized equity options had developed which permitted participants to designate the basic terms of the options including size, term to expiration, exercise style, exercise price, and exercise settlement value. According to the Exchanges, participants in this OTC market were typically institutional investors, who bought and sold options in large-size transactions through a relatively small number of securities dealers. To compete with this growing OTC market in customized equity options, the Exchanges proposed to expand their FLEX options rules<sup>9</sup> to permit the

introduction of trading in FLEX options on specified equity securities that satisfied the Exchanges' listing standards for equity options.<sup>10</sup> The Exchanges' proposals allowed FLEX Equity option market participants to designate the following contract terms: (1) Certain exercise prices; (2) exercise style (*i.e.*, American, European, or capped);<sup>11</sup> (3) expiration date;<sup>12</sup> and (4) option type (*i.e.*, put, call, or spread). In addition, the Exchanges set position and exercise limits for FLEX Equity options at three times the position limits for the corresponding Non-FLEX Equity options on the same underlying security.<sup>13</sup> The Exchanges now propose to eliminate position and exercise limits for FLEX Equity options.

## III. Description

The Exchanges believe that the elimination of position and exercise limits for FLEX Equity options is appropriate given the institutional nature of the market for this derivative product. The Exchanges also believe that large investors currently find the

*Major Market, Institutional, and S&P MidCap Indexes* (File No. SR-Amex-93-05), and 34052 (May 12, 1994), 59 FR 25972 (May 18, 1994) (order approving the trading of FLEX Index options on the Nasdaq 100 Index) (File No. SR-CBOE-93-46).

<sup>10</sup> See, *e.g.*, Amex Rule 915 which contains initial listing standards for a security to be eligible for options trading. In addition, the Exchanges may trade FLEX options on any options-eligible security regardless of whether standardized Non-FLEX options overlie that security and regardless of whether such Non-FLEX options trade on the Exchanges.

<sup>11</sup> An American-style option is one that may be exercised at any time on or before the expiration date. A European-style option is one that may be exercised only during a limited period of time prior to expiration of the option. A capped-style option is one that is exercised automatically prior to expiration when the cap price is less than or equal to the closing price of the underlying security for calls, or when the cap price is greater than or equal to the closing price of the underlying security for puts.

<sup>12</sup> The expiration date of a FLEX Equity option cannot, however, fall on a day that is on, or within two business days of, the expiration date of a Non-FLEX Equity option.

<sup>13</sup> Position and exercise limits for FLEX Equity options are set forth below as compared to existing limits for Non-FLEX Equity options on the same underlying security.

Non-FLEX Equity position limit	
4,500 contracts.	
7,500 contracts.	
10,500 contracts.	
20,000 contracts.	
25,000 contracts.	
FLEX Equity position limit	
13,500 contracts.	
22,500 contracts.	
31,500 contracts.	
60,000 contracts.	
75,000 contracts.	

The Commission notes that there is no aggregation of positions or exercises in FLEX Equity options with positions or exercises in Non-FLEX Equity options for purposes of the limits.

use of exchange-traded options impractical because of the constraints imposed by position limits. According to the Exchanges, with no position limits, additional investors will be attracted to exchange-traded options, thereby reducing transaction costs as well as improving price efficiency for all exchange-traded option market participants.

In addition, the Exchanges believe that FLEX Equity options, unconstrained by position limits, may become an important part of large investors' investment strategies. For instance, according to the Exchanges, in the absence of position limits, investors will be able to use exchange-traded options to implement specific viewpoints regarding the underlying common stock; viewpoints that take into account specific near- and long-term expectations for the underlying stock price as well as judgments on price volatility. Similarly, in the Exchanges' view, the ability to execute large exchange-traded option transactions will permit large investors to implement transactions that reflect the strength of their interest in buying or selling the underlying shares, as well as their specific viewpoints on the purchase or sale of the underlying shares.

In further support for their proposals, the Exchanges note that issuers of stocks underlying FLEX Equity options will be able to use such options, primarily through the sale of puts, as part of their stock repurchase programs.<sup>14</sup> While the Exchanges do not expect that corporate issuers will use the sale of put options to buy all the securities that are covered by their repurchase programs, the Exchanges believe that FLEX Equity options without position limits will at least provide issuers with a meaningful alternative.

The Exchanges believe that making the exchange-traded options market more accessible to large investors will create more "complete" markets and thereby better serve investors and issuers. In addition, the Exchanges believe that institutional investors, large individual investors, and corporate issuers repurchasing their own shares will find FLEX Equity options without position limits extremely attractive. Moreover, the Exchanges note that such activity will occur in the regulated, transparent domestic FLEX Equity options markets rather than in the less transparent OTC market or an offshore

<sup>14</sup> The Commission notes that issuers would, of course, need to comply with all applicable provisions of the federal securities laws in conducting their share repurchase programs.

<sup>6</sup> See letter from Claire P. McGrath, Managing Director and Special Counsel, Derivative Securities, Amex, to Lvette Lopez, Assistant Director, Office of Market Supervision, Division of Market Regulation ("Division"), Commission, dated February 3, 1997 ("Amex Amendment No. 1"). In Amex Amendment No. 1, the Amex amended its rule filing to eliminate position and exercise limits for FLEX Equity options under a two-year pilot program and revised the proposed text of Amex Rule 906G to include a reporting requirement and the ability of the Amex to impose higher margin requirements and/or to assess capital charges.

<sup>7</sup> See letter from Timothy H. Thompson, Senior Attorney, CBOE, to Sharon Lawson, Division, Commission, dated May 13, 1997 ("CBOE Amendment No. 1"). In CBOE Amendment No. 1, the CBOE amended its rule filing to eliminate position and exercise limits for FLEX Equity options under a two-year pilot program and revised the proposed text of CBOE Rule 24A.7 to include a reporting requirement and the ability of the CBOE to impose higher margin requirements and/or to assess capital charges.

<sup>8</sup> See Securities Exchange Act Release Nos. 36841 (February 14, 1996), 61 FR 6666 (February 21, 1996) (File Nos. SR-CBOE-95-43 and SR-PSE-95-24), and 37336 (June 19, 1996), 61 FR 33558 (June 27, 1996) (File No. SR-Amex-95-57).

<sup>9</sup> See, *e.g.*, Amex Rules 900G through 909G. At the time of their FLEX Equity option proposals, the Amex and the CBOE had already secured Commission approval to list and trade FLEX options on several broad-based market indexes market indexes composed of equity securities ("FLEX Index options"). See, *e.g.*, *Securities Exchange Act Release Nos. 32781* (August 20, 1993), 58 FR 45360 (August 27, 1993) (Order approving the trading of FLEX Index options on the

market which do not come under Commission oversight.

Finally, the Exchanges have represented that they intend to implement increased surveillance and reporting procedures in order to ensure an enhanced monitoring of the uses and risks associated with both the elimination of position limits and the underlying strategies resulting in such increased positions. Specifically, whenever a member files a report with an exchange (indicating that an account is carrying a position in excess of three times the standardized option position limit or that class), the Options Clearing Corporation ("OCC") will be asked to perform a risk evaluation of the account and its position. If OCC's risk evaluation indicates a cause for concern, the exchange will notify the member carrying the account and assess the circumstances of the transactions along with the firm's view of the exposure of the account, as well as determine whether the account is approved and suitable for the strategies being utilized. According to the Exchanges, this monitoring of accounts should provide the information necessary to determine whether additional margin and/or capital charges should be imposed. Similarly, the adoption of the Exchanges' proposals under a two-year pilot period, with a status report provided to the Commission after one-and-a-half years, should enable the Commission to assess the effects on the markets of the elimination of position and exercise limits on FLEX Equity options.

#### IV. Discussion

The Commission finds that the proposed rule changes are consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) (5). Specifically, the Commission believes that the rule proposals are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Commission also believes that the proposed rule changes are consistent with Section 11A of the Act in that the elimination of position and exercise limits for FLEX Equity options allows the Exchange to better compete with the growing OTC market in customized equity options, thereby encouraging fair competition among brokers and dealers and exchange markets. The attributes of the Exchanges' options markets versus

an OTC market include, but are not limited to, a centralized market center, an auction market with posted transparent market quotations and transaction reporting, parameters and procedures for clearance and settlement, and the guarantee of the OCC for all contracts traded on the Exchanges.

While the Commission has generally taken a gradual, evolutionary approach toward expansion of position and exercise limits, the Commission is willing to approve the two-year pilot program for FLEX Equity options for several reasons. First, the FLEX Equity options market is characterized by large, sophisticated institutional investors (or extremely high net worth individuals), who have both the experience and ability to engage in negotiated, customized transactions. For example, with a required minimum size of 250 contracts to open a transaction in a new series, FLEX Equity options are designed to appeal to institutional investors, and it is unlikely that many retail investors would be able to engage in options transactions at that size. Second, all of the Exchanges' other current rules and provisions governing FLEX Equity options remain applicable.<sup>15</sup> Third, the OCC will serve as the counter-party guarantor in every exchange-traded transaction. Fourth, the proposed elimination of position and exercise limits for FLEX Equity options could potentially expand the depth and liquidity of the FLEX equity market without significantly increasing concerns regarding intermarket manipulations or disruptions of the options or the underlying securities. Finally, the Exchanges' surveillance programs will be applicable to the trading of FLEX Equity options and should detect and deter trading abuses arising from the elimination of position and exercise limits.

As described above, the Exchanges have adopted important safeguards that will allow them to monitor large positions in order to identify instances of potential risk and to assess additional margin and/or capital charges, if necessary. The Exchanges require each member or member organization (other than a Specialist, a Registered Options Trader, a Market Maker, or a Designated Primary Market Maker) that maintains a position on the same-side of the market in excess of three times the position limit level established pursuant to the applicable exchange rule for Non-FLEX Equity options of the same class, to report information to the exchange regarding the FLEX Equity option position, positions in any related

instrument, the purpose or strategy for the position, and the collateral used by the account.<sup>16</sup> By monitoring accounts in excess of three times the Non-FLEX Equity option position limit in this manner, the Exchanges should be provided with the information necessary to determine whether to impose additional margin and/or whether to assess capital charges upon a member organization carrying the account. In addition, this information should allow the Exchanges to determine whether a large position could have an undue effect on the underlying market and to take the appropriate action.

Given the size and sophisticated nature of the FLEX Equity options market, along with the new reporting and margin requirements, the Commission believes that eliminating position and exercise limits for FLEX Equity options for a two-year pilot period should not substantially increase manipulative concerns. Nevertheless, the Commission will be able to assess the effects on the markets of the Exchanges' proposals during the two-year pilot period. If problems were to arise during such pilot period, the Commission believes that the enhanced market surveillance of large positions should help the Exchanges to take the appropriate action in order to avoid any manipulation or market risk concerns.

Preliminarily, the Commission believes that it is reasonable to treat FLEX Equity options differently than regular standardized options. FLEX options compete directly with OTC options. The Commission believes that it would be beneficial to attract OTC activity back to a more transparent market with a clearinghouse guarantee. Hence, a liberalization of position limits for FLEX Equity options is a measured deregulatory means to enable the Exchanges to compete with the OTC market while preserving important oversight safeguards.

In summary, because of the special nature of the Flex Equity markets, the Commission believes that the Exchanges' proposals should be approved. Nevertheless, because this is the first time the Commission has agreed to eliminate position and exercise limits for a derivative product, the Commission cannot rule out the potential for adverse effects on the securities markets for the component securities underlying FLEX Equity options. To address this concern, the

<sup>16</sup> The Exchanges also require that an updated report be filed when a change in the options position occurs or when a significant change in the hedge of that position occurs.

<sup>15</sup> See, e.g., Amex Rules 900G through 909G.

Commission has approved the proposals for a two-year pilot period. The Exchanges will undertake to monitor, among other things, open interest and potential adverse market effects and to report to the Commission on the status of the program no later than eighteen months after the order's date of effectiveness. The reporting of the Exchanges' experiences should include, among other things, such information as: (i) The type of strategies used by FLEX Equity options market participants and whether FLEX Equity options are being used in lieu of existing standardized equity options; (ii) the type of market participants using FLEX Equity options both before and during the pilot program, including how the utilization of FLEX Equity options has changed; (iii) the average size of the FLEX Equity option contract both before and during the pilot program, the size of the largest FLEX Equity option contract on any given day both before and during the pilot program, and the size of the largest FLEX Equity option held by any single customer/member both before and during the pilot program; and (iv) any impact on the prices of underlying stocks during the establishment or unwinding of FLEX positions that are greater than three times the standard position limit. Finally, the Commission expects the Exchanges to take prompt action, including timely communication with the Commission and other marketplace self-regulatory organizations responsible for oversight of trading in component stocks, should any unanticipated adverse market effects develop.

The Commission finds good cause to approve Amex Amendment No. 1 and CBOE Amendment No. 1 to the proposed rule filings prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. Specifically, by restricting the elimination of position and exercise limits for FLEX Equity options to a two-year pilot period, as well as requiring members holding large positions to report such positions to the Amex and to the CBOE, the proposed rule changes are more restrictive than the original proposals, which are published for the entire twenty-one day comment period and generated no responses. In addition, by authorizing the Amex and the CBOE to impose margin and/or assess capital charges, the Commission believes that the Amex and the CBOE have established important safeguards to address concerns regarding potential manipulation or other market disruptions. Accordingly, the

Commission believes that it is consistent with Section 6(b)(5) of the Act to approve Amex Amendment No. 1 and CBOE Amendment No. 1 to the proposed rule changes on an accelerated basis.

Interested persons are invited to submit written data, views, and arguments concerning Amex Amendment No. 1 and CBOE Amendment No. 1 to the rule proposals. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule changes that are filed with the Commission, and all written communications relating to the proposed rule changes 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 at the Commission's Public Reference Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filings also will be available for inspection and copying at the principal offices of the Amex and the CBOE. All submissions should refer to File Nos. SR-Amex-96-19 and SR-CBOE-96-79 and should be submitted by October 7, 1997.

## V. Conclusion

For the foregoing reasons, the Commission finds that the Exchanges' proposals to eliminate position and exercise limits for FLEX Equity options for a two-year pilot period, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>17</sup> that the proposed rule changes (SR-Amex-96-19), SR-CBOE-96-79 and SR-PCX-97-09), as amended, are approved on a pilot basis until September 9, 1999.

By the Commission.

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 97-24443 Filed 9-15-97; 8:45 am]

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<sup>17</sup> 15 U.S.C. 78s(b)(2) (1988).

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39035; File No. SR-Amex-97-10]

### Self-Regulatory Organizations; Order Approving Proposed Rule Change by the American Stock Exchange, Inc. Relating to Amendments to Rule 170.01 Relating to Specialists Establishing a Position in Specialty Stocks

September 9, 1997.

## I. Introduction

On February 24, 1997, the American Stock Exchange, Inc. ("Amex" 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"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> the proposed rule to change to permit specialists to engage in certain types of transactions by removing existing restrictions that currently limit specialists approval when establishing or increasing a position in their specialty stocks.<sup>3</sup> Notice of the filing appeared in the **Federal Register** on May 12, 1997.<sup>4</sup> No comment letters were received concerning the proposed rule change. This order approves the Amex's proposal.

## II. Description of the Proposal

The Amex, pursuant to Rule 19b-4 of the Act, proposes to amend Amex Rule 170.01 ("Rule") to remove certain restrictions on specialists' ability to establish or increase their positions in their specialty stocks.

### Purpose

Amex Rule 170 governs specialists' dealings in their specialty stocks. In particular, Amex Rule 170.01 describes certain types of transactions to establish or increase a specialist's position which are not to be effected unless they are "reasonably necessary to render the specialist's position adequate to" the needs of the market. Additionally, these types of transactions require floor official approval unless they are conducted in "less active markets" where such transactions are an essential part of a proper course of dealings and where the amount of stock involved and the price change, if any, are normal in relation to the market.<sup>5</sup> Currently, such

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 38573 (May 5, 1997).

<sup>4</sup> FR 25984 (May 12, 1997).

<sup>5</sup> See Amex Rule 104.10(5)(i).