

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40172; File No. SR-PCX-98-33]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Pacific Exchange, Inc. Relating to an Increase in Position and Exercise Limits for Standardized Equity Options

July 6, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act" or "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 1, 1998, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The PCX is proposing to modify Rule 6.8 and Rule 6.9 relating to position and exercise limits. The PCX proposes to increase the position and exercise limits on standardized equity options traded on the Exchange to three times their current levels.

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

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in sections A, B and C below, of the most significant aspects of such statements.

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

###### 1. Purpose

Currently, PCX Rule 6.8 subjects equity options to one of five different position limits depending on the trading volume and outstanding shares of the underlying security. The levels are:

4,500; 7,500; 10,500; 20,000; and 25,000 contracts on the same side of the market. Under the proposed changes the new limits would be: 13,500; 22,500; 31,500; 60,000; and 75,000 contracts on the same side of the market. The Exchange believes that sophisticated surveillance techniques at the options exchanges adequately protect the integrity of the markets for the options that will be subject to these increased position and exercise limits. The Commission recently approved a similar request from the National Association of Securities Dealers ("NASD") to triple the position and exercise limits for conventional equity options with new limits set at 13,500; 22,500; 31,500; 60,000; and 75,000 contracts on the same side of the market.<sup>3</sup>

Commentary .01 of PCX Rule 6.9 refers to the established exercise limits as 4,500; 7,500; 10,500; 20,000; and 25,000 options contracts. The rule states that the exercise limits established pursuant to PCX Rule 6.9(a) shall be 4,500; 7,500; 10,500; 20,000; and 25,000 options contracts of any particular class of option and it shall be the responsibility of each Member or Member Organization accepting orders for the purchase (in opening transactions) of option contracts to inform customers of the applicable exercise limits. The PCX proposes to change the exercise limits in PCX Rule 6.9 to 13,500; 22,500; 31,500; 60,000; and 75,000 options contracts of any particular class of option.

The Exchange believes that the existing surveillance procedures and reporting requirements at options exchanges and clearing firms that have been developed over the years are able to properly identify unusual and illegal trading activity. In addition, PCX believes that routine oversight inspections of PCX's regulatory programs by the Commission have not uncovered any material inconsistencies or shortcomings in the manner in which the Exchange's market surveillance is conducted.

*Position and Exercise Limits Restrict Legitimate Options Use and Competition.* In the Exchange's view, equity position limits prevent large customers like mutual funds and pension funds from using options to gain meaningful exposure to individual stocks, resulting in lost liquidity in both the options market and the stock market. The Exchange further believes

that equity position limits also act as a barrier to the use of options by corporations wishing to implement options strategies with their own stock.<sup>4</sup>

The Exchange believes that equity position limits put listed options at a competitive disadvantage of over-the-counter ("OTC") derivatives. OTC dealers can execute options trades through overseas subsidiaries not subject to NASD regulation, and therefore not subject to position limits. As a result, the largest trades can go unobserved and unmonitored for regulatory and oversight purposes. An increase in the position limits is consistent with the Commission's reasons for the elimination of FLEX equity option position limits. The Commission recently approved the elimination of position limits for FLEX equity options stating that the elimination will allow the listed options markets to better compete with the OTC market.<sup>5</sup>

In addition, the Commission recently approved the NASD's proposed rule change to raise the position and exercise limit for conventional equity options (*i.e.*, those options not issued, or subject to issuance by the Options Clearing Corporation) to three times their current levels (which is the same as three times the levels established by current exchange rules for standardized options). Because conventional options often have nearly identical term as standardized, exchange-traded options, the Exchange believes the position limits for standardized options should be at least as high as those for conventional options.

###### 2. Basis

The Exchange believes that the proposal is consistent with Section 6(b)<sup>6</sup> of the Act, in general, and Section 6(b)(5)<sup>7</sup> of the Act, in particular, in that it is designed to perfect the mechanisms of a free and open market, to promote just and equitable principles of trade, to

<sup>4</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>5</sup> See Exchange Act Release No. 39032 (September 9, 1997) 62 FR 48683 (September 16, 1997). The Commission stated that "the elimination of position and exercise limits for FLEX equity options allows the Exchanges to better compete with the growing OTC market in customized equity options, thereby encouraging fair competition among brokers and exchange markets." *Id.* at 48685. The Commission notes that approval of the elimination of position and exercise limits for FLEX equity options was granted for a two-year pilot period and was based on several other factors including, in large part, additional safeguards adopted by the exchanges to allow them to monitor large options positions.

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

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

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

<sup>3</sup> See Exchange Act Release No. 40087 (June 12, 1998), 63 FR 33746 (June 19, 1998). The NASD's position limit filing established position and exercise limits for conventional equity options identical to those being proposed by PCX in this filing.

facilitate transactions in securities, and in general, to protect investors and the public interest.

#### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

#### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

Written comments on the proposed rule change were neither solicited nor received.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submission should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., 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, located at the above address. Copies of such filing will also be available for inspection and copying at the principal office of the self-regulatory organization. All submissions should

refer to File No. SR-PCX-98-33 and should be submitted by August 4, 1998.

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

**Margaret H. McFarland,**

*Deputy Secretary.*

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## **DEPARTMENT OF TRANSPORTATION**

### **Federal Aviation Administration**

#### **Index of Administrator's Decisions and Orders in Civil Penalty Actions; Publication**

**AGENCY:** Federal Aviation Administration (FAA), DOT.

**ACTION:** Notice of publication.

**SUMMARY:** This notice constitutes the required quarterly publication of an index of the Administrator's decisions and orders in civil penalty cases. *This publication represents the quarter ending on June 30, 1998.* This publication ensures that the agency is in compliance with statutory indexing requirements.

#### **FOR FURTHER INFORMATION CONTACT:**

James S. Dillman, Assistant Chief Counsel for Litigation (AGC-400), Federal Aviation Administration, 400 7th Street, SW., Suite PL 200-A, Washington, DC 20590; telephone number: (202) 366-4118.

**SUPPLEMENTARY INFORMATION:** The Administrative Procedure Act requires Federal agencies to maintain and make available for public inspection and copying current indexes containing identifying information regarding materials required to be made available or published. 5 U.S.C. 552(a)(2). In a notice issued on July 11, 1990, and published in the **Federal Register** (55 FR 29148; July 17, 1990), the FAA announced the public availability of several indexes and summaries that provide identifying information about the decisions and orders issued by the Administrator under the FAA's civil penalty assessment authority and the rules of practice governing hearings and appeals of civil penalty actions. 14 CFR Part 13, Subpart G.

The FAA maintains an index of the Administrator's decisions and orders in civil penalty actions organized by order number and containing identifying information about each decision or order. The FAA also maintains a cumulative subject-matter index and digests organized by order number. The indexes are published on a quarterly

basis (i.e., January, April, July, and October.)

The FAA first published these indexes and digests for all decisions and orders issued by the Administrator through September 30, 1990. 55 FR 45984; October 31, 1990. The FAA announced in that notice that only the subject-matter index would be published cumulatively and that the order number index would be non-cumulative. The FAA announced in a later notice that the order number indexes published in January would reflect all of the civil penalty decisions for the previous year. 58 FR 5044; 1/19/93.

The previous quarterly publications of the indexes have appeared in the **Federal Register** as follows:

| Dates of quarter     | Federal Register publication |
|----------------------|------------------------------|
| 11/1/89-9/30/90 .... | 55 FR 45984; 10/31/90        |
| 10/1/90-12/31/90 ..  | 56 FR 44886; 2/6/91          |
| 1/1/91-3/31/91 ..... | 56 FR 20250; 5/2/91          |
| 4/1/91-6/30/91 ..... | 56 FR 31984; 7/12/91         |
| 7/1/91-9/30/91 ..... | 56 FR 51735; 10/15/91        |
| 10/1/91-12/31/91 ..  | 57 FR 2299; 1/21/92          |
| 1/1/92-3/31/92 ..... | 57 FR 12359; 4/9/92          |
| 4/1/92-6/30/92 ..... | 57 FR 32825; 7/23/92         |
| 7/1/92-9/30/92 ..... | 57 FR 48255; 10/22/92        |
| 10/1/92-12/31/92 ..  | 58 FR 5044; 1/19/93          |
| 1/1/93-3/31/93 ..... | 58 FR 21199; 4/19/93         |
| 4/1/93-6/30/93 ..... | 58 FR 42120; 8/6/93          |
| 7/1/93-9/30/93 ..... | 58 FR 58218; 10/29/93        |
| 10/1/93-12/31/93 ..  | 59 FR 5466; 2/4/94           |
| 1/1/94-3/31/94 ..... | 59 FR 22196; 4/29/94         |
| 4/1/94-6/30/94 ..... | 59 FR 39618; 8/3/94          |
| 7/1/94-12/31/94 .... | 60 FR 4454; 1/23/95          |
| 1/1/95-3/31/95 ..... | 60 FR 19318; 4/17/95         |
| 4/1/95-6/30/95 ..... | 60 FR 36854; 7/18/95         |
| 7/1/95-9/30/95 ..... | 60 FR 53228; 10/12/95        |
| 10/1/95-12/31/95 ..  | 61 FR 1972; 1/24/96          |
| 1/1/96-3/31/96 ..... | 61 FR 16955; 4/18/96         |
| 4/1/96-6/30/96 ..... | 61 FR 37526; 7/18/96         |
| 7/1/96-9/30/96 ..... | 61 FR 54833; 10/22/96        |
| 10/1/96-12/31/96 ..  | 62 FR 2434; 1/16/97          |
| 1/1/97-3/31/97 ..... | 62 FR 24533; 5/2/97          |
| 4/1/97-6/30/97 ..... | 62 FR 38339; 7/17/97         |
| 7/1/97-9/30/97 ..... | 62 FR 53856; 10/16/97        |
| 10/1/97-12/31/97 ..  | 63 FR 3373; 1/22/98          |
| 1/1/98-3/31/98 ..... | 63 FR 19559; 4/20/98         |

The civil penalty decisions and orders, and the indexes and digests are available in FAA offices. In addition, the Administrator's civil penalty decisions have been published by commercial publishers (Hawkins Publishing Company and Clark Boardman Callahan) and are available on computer on-line services (Westlaw, LEXIS, Compuserve and FedWorld). A list of the addresses of the FAA offices where the civil penalty decisions may be reviewed and information regarding these commercial publications and computer databases appear at the end of this notice.