

## II Discussion

Section 17A(b)(3)(F) of the Act<sup>5</sup> requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible. The Commission believes that the proposed rule change is consistent with OCC's obligations under the Act because the proposed rule change increases the effectiveness of OCC's financial surveillance of its clearing members in situations where the clearing member's net capital falls below that level required by its futures clearing organization.

Many of OCC's clearing members are also registered as FCMs under the Commodity Exchange Act and as such are subject to the financial reporting requirements and the early warning notice requirements of the Commodity Futures Trading Commission and of commodity DSROs. Because of differences in the initial and ongoing minimum net capital requirements used by the commodity regulatory organizations and those used by the securities regulatory organizations, a clearing member could fail to meet the net capital requirements of its DSRO and still satisfy the net capital requirements established by OCC. Consequently, a situation could occur where an FCM clearing member is required to give early warning notice to its commodity regulatory authority but nothing currently would require the clearing member to give notice to OCC. As a result, OCC could continue to clear trades without notice for a clearing member that may or may not be able to satisfy its financial obligations.

Therefore, requiring a clearing member to satisfy the higher applicable net capital standard and to provide OCC with early warning notices when it fails to meet the net capital requirements set by its DSRO or by OCC should assist OCC in assessing the ongoing creditworthiness of its clearing members and also should help OCC to safeguard securities and funds in OCC's custody or control.

## III Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act, that the

proposed rule change (File No. SR-OCC-97-12) be and hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>6</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40209; File No. SR-OCC-97-13]

### Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Relating to Adjustments to Exercise Prices

July 15, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on September 22, 1997, the Options Clearing Corporation ("CCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change (File No. SR-OCC-97-13) 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 on the proposed rule change from interested persons and to grant accelerated approval of the proposal.

#### 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 amend OCC's by-laws regarding the adjustment of exercise prices. Specifically, adjustment of exercise prices will be rounded to the next nearest trading increment as specified by the primary market for the underlying security.

#### 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 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.<sup>2</sup>

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

Under the proposed rule change, OCC will amend Article VI, Section 11(i) of its by-laws to provide for the rounding of adjustments of exercise prices to the nearest "trading increment" for the underlying security, as fixed by the primary market for the security.<sup>3</sup> Currently, OCC rounds adjustments to exercise prices to the nearest eighth of a dollar. The securities industry has moved from quoting prices in eighths of a dollar ("eighths") to sixteenths of a dollar ("sixteenths") and is moving towards quoting prices in decimals. Therefore, OCC believes that the adjustment provisions of its by-laws require amendment. Amending its by-laws to provide for rounding to the nearest trading increment will accommodate the interim change to pricing in sixteenths and any final change to decimal pricing.

The proposed rule change also will add a new interpretation .09 to Article VI, Section 11 expressly authorizing OCC's securities committee to adjust exercise prices of outstanding options to a new trading increment (e.g., decimals) to correspond to a change in the trading increment in the underlying security in its primary market. The rule change will not mandate such adjustments, but it will give clear authority to the committee to adjust exercise prices if the committee deems such action to be appropriate in light of the factors cited in Article VI, Section 11(b) of OCC's by-laws.

Currently, exercise prices of newly introduced options series are expressed in half dollar increments. However, there generally will be options series outstanding with exercise prices expressed in eighths or sixteenths as a result of previous adjustments. Eighths cannot be converted to fewer than three decimal places and sixteenths cannot be converted to fewer than four without rounding. As a result, the rule change will provide for rounding adjusted exercise prices to the nearest unit of the applicable trading increment or, where an exercise price is equidistant between two units, to the next lowest unit. Rounding would result in a small gain (\$0.25 per contract in the case of

<sup>2</sup> The Commission has modified the text of the summaries prepared by OCC.

<sup>3</sup> The complete text of the amendments was submitted with OCC's rule filing and is available for inspection and copying at the Commission's Public Reference Room and through OCC.

<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>6</sup> 17 CFR 200.30-3(a)(12).

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

sixteenths and \$0.50 per contract in the case of eighths assuming a trading increment of one cent) for one side of each adjusted contract and a corresponding loss for the other. However, OCC believes that the committee will not use its adjustment authority unless it determines that the benefits of adjusting outweigh the detriments. If approved, the proposed rule change will be disclosed in a supplement to the options disclosure document.

OCC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act<sup>4</sup> because it should promote the prompt and accurate clearance and settlement of securities transactions.

#### *B. Self-Regulatory Organizations' 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 Act<sup>5</sup> requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions. The Commission believes that the proposed rule change is consistent with this obligation because it should ensure that the exercise price of an option on a security can be expressed in the same increment as the price of the underlying security when the pricing increment of an underlying security has been changed after the issuance of the option. As a result, the proposed rule change should increase the accuracy of the clearance and settlement of options transactions and promote the prompt and accurate clearance and settlement of securities transactions.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the publication of notice of the filing. Approving prior to the thirtieth day after publication of notice should immediately reduce the possibility of inaccurate clearance and settlement of

options transactions where the exercise price of the option is expressed in a different increment than the trading increment of the underlying security.

### **IV. Solicitation of Comment**

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 submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, DC 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 NW., Washington, DC 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-97-13 and should be submitted by August 12, 1998.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>6</sup> that the proposed rule change (File No. SR-OCC-97-13) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>7</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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### **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-40199; File No. SR-PCX-97-46]

#### **Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the Pacific Exchange, Inc. Relating to Minimum Trading Increments**

July 14, 1998.

Pursuant to Section 19(b)(1) of 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 December 22, 1997, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II 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 and to grant accelerated approval to the proposed rule change.

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

The PCX proposes to amend its Rule 5.3(b) by adding a new Commentary .02 to permit members to trade on the Exchange in increments smaller than  $\frac{1}{16}$ , in order to match bids and offers displayed in other markets for the purpose of preventing Intermarket Trading System ("ITS") trade-throughs. The text of the proposed rule change is available at the Office of the Secretary, the PCX, and at the Commission

#### **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**

In May 1997, the Commission approved an Exchange proposal to amend its rules to permit trading of stocks in sixteenths when the selling price is \$5 or above.<sup>3</sup> Previously such

<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. 38575 (May 5, 1997), 62 FR 26606 (May 14, 1997) (order granting temporary accelerated approval of File No. SR-PCX-97-16); see also Exchange Act Release No. 38780 (June 26, 1997), 62 FR 36087 (July 3, 1997) (order approving File No. SR-PCX-97-15, amending Rule 5.3(b)).

<sup>4</sup> 15 U.S.C. 78q-1.

<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>6</sup> 15 U.S.C. 78s(b)(2).

<sup>7</sup> 17 CFR 200.30-3(a)(12).