

acceptable to the Exchange.” Amendment No. 3 explains the application of the standard “acceptable to the Exchange” to control persons. In the proposed rule change, the Exchange will apply the “acceptable to the Exchange” standard to control persons in the same manner as it has applied that standard to employees of members or member organizations in the past since the rule was first adopted. While the Exchange has not had to exercise this standard in recent years, the Exchange might apply it if, for example, a prospective employee or control person is subject to a statutory disqualification or if the person, while not subject to a statutory disqualification, is barred from the banking industry because he or she stole from customers.

In the original filing, the proposed amendments to Rule 2 of Article VI stated that upon notice to a member or member organization that the President of the Exchange has withheld or withdrawn approval of the employment of any other person, the relationship between the member or member organization and such person shall be terminated. Amendment No. 3 deletes the reference to “the employment of” any such other person.

Rule 2 of Article VI requires members or member organizations that know or in the exercise of reasonable care should know that any prospective employee is subject to one or more statutory disqualifications to submit details on such prospective employee to the Exchange and receive Exchange approval before such person becomes associated with the member or member organization. Rule 2 also requires that each member or member organization take reasonable care to determine the existence of a statutory disqualification prior to employing any prospective employee. Further, if any person already employed by a member or member organization thereafter becomes subject to a statutory disqualification, notice must be sent to the Exchange promptly. Amendment No. 3 clarifies that these provisions are applicable to control persons as well as employees of members or member organizations.

## 2. Statutory Basis

The proposed rule change is consistent with section 6 of the Act in general, and in particular, with Section 6(b)(5), in that it is designed to promote just a equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, as well as to protect investors and the public interest.

The proposed rule change is also consistent with Section 6(c)(3)(B) of the Act, which provides that a national securities exchange may examine and verify the qualifications of an applicant to become a person associated with a member in accordance with procedures established by the rules of the exchange, and require any person associated with a member, or any class of such persons, to be registered with the exchange in accordance with procedures so established.

### *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*

The Exchange understands that the Commission has received comments on SR-CHX-96-11 and Amendments Nos. 1 and 2 thereto.<sup>5</sup> The Exchange believes that issues raised by the commenter are addressed herein, and in Amendment No. 3.<sup>6</sup>

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

Within 35 days of the 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 the 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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W.,

<sup>5</sup> See Letters from C. Philip Curley, Attorney, Robinson Curley & Clayton, P.C., to Jonathan G. Katz, Secretary, SEC, dated May 2, 1996 (“Comment Letters”).

<sup>6</sup> The SEC notes that Amendment No. 3 was submitted in response to the Comment Letter. The comment letter received by the SEC regarding the CHX’s proposal and Amendment No. 3 are available in the SEC’s public reference room in File No. SR-CHX-96-11.

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 at the Commission’s Public Reference Section, 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 the CHX. All submissions should refer to File No. SR-CHX-96-11 and should be submitted by July 16, 1996.

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

Margaret H. McFarland,  
Deputy Secretary.

[FR Doc. 96-16167 Filed 6-24-96; 8:45 am]

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[Release No. 34-37318; File No. SR-OCC-96-03]

### **Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of a Proposed Rule Change Relating to the Clearance and Settlement of Flexibly Structured Equity Options**

June 18, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> notice is hereby given that on April 30, 1996, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared primarily by OCC. 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 purpose of the proposed rule change is to enable OCC to clear and settle flexibly structured equity options.

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

## 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

The purpose of this proposed rule change is to accommodate within OCC's existing By-Laws and Rules the clearance and settlement of flexibly structured options on individual equity securities, as proposed for trading by the American Stock Exchange, Inc. ("AMEX"), the Chicago Board Options Exchange, Incorporated ("CBOE"), the Philadelphia Stock Exchange, Inc. ("PHLX") and the Pacific Stock Exchange, Inc. ("PSE") (collectively, "Exchange" or "Exchanges").<sup>3</sup>

Flexibly structured equity options allow parties to each flexibly structured equity option trade to customize certain terms of the option within specified limits established by the Exchange. Specifically, for each flexibly structured equity option trade parties may establish the exercise price, the exercise style (*i.e.*, American,<sup>4</sup> European,<sup>5</sup> or capped<sup>6</sup>), the cap interval in the case of

capped-style options, the expiration date, and the option type (*i.e.*, put or call).<sup>7</sup> In addition to customization, flexibly structured equity option trades will require a minimum transaction size of 250 contracts in opening trades in currently unopened series and 100 contracts in the case of opening and most closing trades in currently open series. Flexibly structured equity options thus will differ from existing Exchange-traded equity options both in terms of customization and size.

From a clearance and settlement perspective, flexibly structured equity options can be treated and processed like any other equity option in virtually all respects. While Exchange rules permit a Request for Quotes<sup>8</sup> to specify a quote either as a dollar amount or as a percentage of the underlying stock price, when a trade is reported to OCC the option premium always will be expressed as a dollar amount. Therefore, when a flexibly structured equity option trade is reported to OCC by one of the Exchanges all of the terms of that option will have been established in the Exchange's report, and the terms will correspond to existing equity options term categories. As a result, on receipt of a matched trade report from an Exchange, OCC will establish long and short flexibly structured equity option positions in clearing member accounts in precisely the same way it does for existing equity options. Furthermore, flexibly structured equity option positions will exhibit virtually the same characteristics as existing equity options.

Because of the similarities between existing equity options and flexibly structured equity options, only a few of OCC's By-Laws and Rules need adjustment to accommodate flexibly structured equity options.<sup>9</sup> OCC proposes to amend Section 1 of Article I to add an all-purpose definition of "flexibly structured option." Thus, the

than or equal to the closing price of the underlying security for puts).

<sup>7</sup> Although the rules of the Exchanges provide for capped-style flexibly structured equity options, the Exchanges advised OCC that they do not intend to provide a market in capped-style flexibly structured equity options at the outset. Accordingly, this proposed rule change does not include the rules that would be required for the clearance and settlement of such options. The commencement of trading in capped-style flexibly structured equity options will require that the Commission approve another proposed rule change filed by OCC under Section 19(b)(1) of the Act.

<sup>8</sup> A Request for Quotes is the initial request supplied by the submitting exchange member to initiate FLEX bidding and offering.

<sup>9</sup> The specific changes to OCC's By-Laws and Rules are set forth in OCC's proposed rule change, which is available for review at the principal office of OCC and the Commission's Public Reference Room.

definitions for "flexibly structured option" as set forth in Articles XV, XVII, and XXIII will be deleted. The definition of "expiration date" in Article I, Section 1 is being amended to make clear that flexibly structured equity options may expire on dates other than the Saturday following the third Friday of the expiration month. The expiration date of any such option will be the date reported to OCC by the Exchange, subject to such constraints on the range of possible expiration dates as are set forth in the rules of the Exchanges.

Section 11 of Article VI, regarding adjustments to equity and index options, will be amended to apply to the adjustment of flexibly structured equity and index options.<sup>10</sup> OCC also is proposing to add Interpretation and Policy .08 to Section 11 for situations where a European-style flexibly structured equity option is adjusted to require the delivery upon exercise of a fixed amount of cash, such as would normally occur in the event of a merger where the underlying security is converted into a right to receive a fixed amount of cash. In such a circumstance, it is proposed that the expiration of the option will ordinarily be accelerated so that the option will expire on or shortly after the date on which the underlying stock is converted into a right to receive cash. Without this adjustment, the option position would have to be maintained until it could be exercised at its regular expiration even though the amount to be received on exercise has already been fixed. This special adjustment is being proposed to accommodate flexibly structured equity options because unlike existing equity options flexibly structured equity options may have European-style exercise features.

The only change proposed to be made to OCC's Rules is the addition of Interpretation and Policy .03 to Rule 805, which will clarify that OCC's exercise procedures as set forth in Rule 805<sup>11</sup> shall apply to the exercise of flexibly structured equity options. The new interpretation also gives OCC the flexibility, if necessary, to depart from regular expiration date procedures and

<sup>10</sup> Adjustments may be made to the number of option contracts, the unit of trading, the exercise price, and the underlying security with respect to all outstanding option contracts open for trading in an underlying security which is the subject of a dividend, stock dividend, stock distribution, stock split, reverse stock split, rights offering, distribution, reorganization, recapitalization, reclassification or similar event, or the merger, consolidation, dissolution, or liquidation of the issuer of the underlying security.

<sup>11</sup> OCC Rule 805 sets forth the expiration date exercise procedures.

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

<sup>3</sup> For a complete description of flexibly structured equity options, refer to Securities Exchange Act Release No. 36841 (February 14, 1996), 61 FR 6666 [File Nos. SR-CBOE-95-43 and SR-PSE-95-24] (order approving the trading of flexibly structured equity options by the CBOE and PSE). The AMEX and PHLX also have filed proposed rule changes for the trading of flexibly structured equity options. For a complete description of these filings, refer to Securities Exchange Act Release Nos. 37053 (March 29, 1996), 61 FR 15537 [File No. SR-AMEX-95-57] (notice of filing of proposed rule change); and 37048 (March 29, 1996), 61 FR 15549 [File No. SR-PHLX-96-08] (notice of filing of proposed rule change).

<sup>4</sup> An American-style equity option may be exercised at any time prior to its expiration date.

<sup>5</sup> A European-style equity option may be exercised only during a specified period before the option expires.

<sup>6</sup> A capped-style equity option will be exercised automatically prior to expiration if the options market on which the option is trading determines that the value of the underlying interest at a specified time on a trading day "hits the cap price" for the option (*i.e.*, 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

deadlines in the case of flexibly structured equity options. Such departures are not currently anticipated and adequate prior notice will be given to all clearing members.

OCC believes the proposed rule change is consistent with the purposes and requirements of Section 17A of the Act because the proposal provides for the prompt and accurate clearance and settlement of transactions in flexibly structured equity options and because it provides for the safeguarding of related securities and funds. OCC believes the proposed rule change meets such requirements by establishing a framework in which existing, reliable OCC systems, rules, and procedures are extended to the processing of flexibly structured equity options. Finally, OCC believes the proposed rule change will foster cooperation with persons, including OCC clearing members, engaged in the clearance and settlement of securities transactions and will thereby promote the protection of investors and the public interest.

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

OCC does not believe that the proposed rule change will 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**

Within thirty-five 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 ninety 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 OCC 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. 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 Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing also will be available for inspection and copying at the principal office of OCC. All submissions should refer to File No. SR-OCC-96-03 and should be submitted by July 16, 1996.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

Margaret H. McFarland,  
Deputy Secretary.

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**[Release No. 34-37326; File No. SR-PSE-96-13]**

**Self-Regulatory Organizations; Pacific Stock Exchange, Incorporated; Order Granting Approval to Proposed Rule Change Relating to Restrictions on Equity Allocations (10% Rule)**

June 19, 1996.

On April 10, 1996, the Pacific Stock Exchange, Incorporated ("PSE" 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> a proposed rule change to codify a policy that any specialist whose score on a quarterly specialist performance evaluation ranks in the bottom 10% of specialist on his or her trading floor shall not be eligible for allocations of securities, absent mitigating circumstances, until such ranking rises above the bottom 10%.

The proposed rule change was published for comment in Securities Exchange Act Release No. 37142 (April 24, 1996), 61 FR 19328 (May 1, 1996). No comments were received on the proposal.

The Exchange's specialist evaluation program is governed by PSE Rule 5.37. Subsection (a) of that Rule provides that

the Equity Allocation Committee ("EAC") shall evaluate all registered specialists on a quarterly basis. Those evaluations result in overall ratings of specialists that are based upon three separate measures of performance, as specified in the Rule.<sup>3</sup> Subsection (b) provides that any registered specialists who is in the bottom 10% of all registered specialists on that specialist's trading floor,<sup>4</sup> as determined by the overall evaluation scores in any one quarterly evaluation, shall be requested to meet with the EAC (or a panel appointed by the EAC) on an informal basis.<sup>5</sup> If a specialist is in the bottom 10% during any two out of four consecutive quarterly evaluations, the specialist is requested to appear a second time before the EAC to explain his or her performance.<sup>6</sup>

If the EAC finds in its second informal meeting with a specialist that there are no mitigating circumstances that would demonstrate substantial improvement of or reasonable justification for the specialist's most recent evaluation score, the EAC will make a determination that the specialist's performance is below acceptable levels, and notify the specialist of his or her right to a hearing on such determination.<sup>7</sup> The EAC may take a number of actions against a registered specialist found to perform below acceptable levels, including limitation, suspension or termination of the specialist's registration as a specialist, or reallocation of his or her stocks.

<sup>3</sup> The three measures of performance currently utilized by the PSE are: (1) National Market System Quote Performance, accounting for 45% of the overall score, measures the percentage of times in a given quarter that a specialist's bid and/or offer is equal to or greater than the best bid or offer in the consolidated quote system for each dually-traded security; (2) the Specialist Evaluation Questionnaire Survey, also accounting for 45% of the overall score, is composed of questions designed to evaluate a specialist's market-making performance and is to be completed only by floor brokers who regularly trade with a specialists; and (3) SCOREX Limit Order Acceptance Performance, which accounts for the final 10% of the overall score, measures the percentage of P/COAST (formerly SCOREX) limit orders accepted by a specialist. See Securities Exchange Act Release No. 28843 (February 1, 1991), 56 FR 5040 (February 7, 1991) (File No. SR-PSE-87-19) for a more complete description of each of these measures of performance.

<sup>4</sup> The PSE maintains two equity trading floors, one in Los Angeles and one in San Francisco. See PSE Rule 4.1(g).

<sup>5</sup> See PSE Rules 5.37(b)-(e).

<sup>6</sup> SEE Rules 5.37(g)-(i). The EAC also has the authority to bypass the second informal proceeding and commence formal reallocation proceedings after a specialist's second quarter of substandard performance in a rolling twelve-month period. See PSE Rule 5.37.

<sup>7</sup> For a description of the procedures followed in such proceedings, see PSE Rules 5.37(j)-(s).

<sup>12</sup> 17 CFR 200.30-3(a)(12) (1995).

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

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