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Deputy Secretary.
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[Release No. 34-37050; File No. SR-CBOE-96-15]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Inc., Relating to the Placing of Orders Over the Outside Telephone Lines at the Equity Trading Posts

March 29, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on March 12, 1996, the Chicago Board Options Exchange, Incorporated ("CBOE" or "Exchange") 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 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 Exchange proposes to amend its Regulatory Circular governing the use of member-owned or Exchange-owned telephones located at the equity trading post on the floor of the Exchange.² The amendment would permit floor brokers to receive orders from CBOE market makers over outside telephone lines at the equity trading posts.

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

The purpose of the proposed rule change is to amend the policy currently governing the use of telephones at equity option trading posts by permitting market makers to place orders with floor brokers over the outside telephone lines.³ Currently, the telephone policy for the equity posts, which has been instituted pursuant to Exchange Rule 6.23,⁴ prohibits orders of any type to be entered via outside telephone lines. The policy for use of the telephones at the equity posts will remain unchanged in every other respect.

The Exchange has determined to make this change in the equity post telephone policy so that market makers may transmit their orders more efficiently even when they need to be off the floor to attend to personal or Exchange business. This change will permit the market makers to provide capital more quickly at option posts in the wake of news or market events and to hedge their positions in response to market news even when they are off the floor of the Exchange temporarily. The change will be particularly useful to those members of the Exchange that are often requested to attend meetings on Exchange matters during the trading day.

The Exchange believes that Exchange rules will prevent this policy from being used by market makers to avoid standing in their respective crowds or to assume de facto an appointment in an option traded at another post. Under the proposed policy, orders placed over the outside telephone lines will be counted as off-floor orders for purposes of determining a market maker's compliance with the 80% requirement of Rule 8.7. Pursuant to Interpretation .03 of Rule 8.7, Obligations of Market-Makers, a market maker must execute in-person 80 percent of his total transactions to receive market maker treatment for off-floor orders. An order that receives market maker treatment is entitled to certain benefits, such as favorable margin treatment under Regulation T; this is a strong incentive for the market makers to satisfy the 80% requirement. In addition, consistent

with Rule 8.7(a), orders placed by a market maker over the outside telephone lines at the equity posts should constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market. Also, Interpretation .03 of Rule 8.7 states that the off-floor orders for which a market maker receives market maker treatment shall be effected for the purpose of hedging, reducing risk of, rebalancing, or liquidating open positions of the market maker. Finally, Interpretation .03 to Rule 8.7 also generally requires a market maker to execute at least 25 percent of this total transactions in-person.

Upon the approval of this new policy as a rule of the Exchange, the Exchange will publish a Regulatory Circular, substantially in the form attached hereto.

As with the current policy governing the use of telephones at the equity trading posts, the Exchange intends to monitor compliance with these conditions by means by customary floor surveillance procedures, including reliance on surveillance by Floor Officials and Exchange employees. In addition, the Exchange will review on a weekly basis clearance data, as it does now, to assure that a market maker meets the 80% in-person requirement.

The Exchange believes that its proposal is consistent with and further the objectives of Section 6(b)(5) of the Securities Exchange Act of 1934 in that they are designed to improve communications to and from the Exchange's trading floor in a manner that promotes just and equitable principles of trade, prevents fraudulent and manipulative acts and practices, and maintains fair and orderly markets. In addition, the Exchange believes that this change in policy will enhance the Exchange's ability to provide capital where it is most needed on the Exchange floor and it will provide market makers with an efficient method to protect their portfolio even when they need to be off the floor.

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

The Exchange does not believe that the proposed 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 on the proposed rule change were neither solicited nor received.

³ Currently, the Exchange permits market makers to place orders with floor brokers via intra-floor lines.

⁴ Exchange Rule 6.23 prohibits members from establishing or maintaining any telephone or other wire communications between their offices and the Exchange floor, and it authorizes the Exchange to direct the discontinuance of any communication facility terminating on the Exchange floor.

¹ 15 U.S.C. § 78s(b)(1) (1988).

² The regulatory circular that governs the use of telephones at the equity trading posts was approved by the Commission on March 2, 1994. See SR-CBOE-93-24, Exchange Act Release 34-33701 (March 2, 1994), 59 FR 11336.

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. 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. Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organizations. All submissions should refer to File No. SR-CBOE-96-15 and should be submitted by April 29, 1996.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁵

Margaret H. McFarland,
Deputy Secretary.

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Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by Chicago Board Options Exchange, Incorporated Relating to FLEX Equity Options

March 29, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934, 15 U.S.C. 78s(b)(1), notice is hereby given that on March 18, 1996, the Chicago Board Options Exchange, Incorporated ("CBOE" or "Exchange") 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 by the CBOE. 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 CBOE proposes to amend certain rules pertaining to FLEX Equity Options. The text of the proposed rule change is available at the Office of the Secretary, CBOE 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, CBOE 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 CBOE 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

The Exchange proposes to amend two rules pertaining to FLEX Equity Options. First, the Exchange proposes to amend Interpretation and Policy .05 under Exchange Rule 5.5 in order to provide that new series of FLEX Equity options may be opened during the month in which they will expire, so long as options of that series expire no earlier than the day following the day the series is added. The Exchange believes that this will provide maximum flexibility to users of FLEX Equity Options, while avoiding the administrative costs that would be

associated with options that expire on the day they are issued.

Second, the Exchange proposes to amend Rule 24A.5(e) in order to provide a minimum right of participation to Exchange members who initiate Requests for Quotes in respect of FLEX Equity Options and indicate an intention to cross or act as principal on the trade, similar to the right of participation that applies under existing Exchange rules in respect of FLEX Index Options. Under existing Rule 24A.5(e)(iii), a member who submits a Request for Quotes in respect of a FLEX Index Option and indicates an intention to cross or act as principal on the trade, and who matches the current best bid or offer ("BBO") during the BBO Improvement Interval, has priority to execute the contra side of the trade up to the greater of (i) one-half of the trade, (ii) \$1 million Underlying Equivalent Value, or (iii) the remaining Underlying Equivalent Value on a closing transaction valued at less than \$1 million. If the member improves the BBO and any other FLEX-participating member matches the improved BBO, the submitting member has priority to execute the contra side of the trade up to the greater of (i) two-thirds of the trade, (ii) \$1 million Underlying Equivalent Value, or (iii) the remaining Underlying Equivalent Value on a closing transaction valued at less than \$1 million. By contrast, under current Exchange rules no priority right of participation in a principal or agency cross is given to a member who submits a Request for Quotes in respect of a FLEX Equity Option, even if the submitting member matches or improves the BBO.

The proposed rule change would provide that a member who submits a Request for Quotes in respect of a FLEX Equity Option and indicates an intention to cross or act as principal on the trade, and who matches or improves the BBO during the BBO Improvement Interval, has a priority right to execute the contra side of the trade for at least twenty-five percent (25%) of the trade.¹ The Exchange believes that the proposed rule change will encourage members to bring FLEX Equity Option orders to CBOE and to commit their capital to the FLEX Equity Options market on CBOE, and thereby contribute to the liquidity of that market, by

¹ The proposed rule change amends the language of Rule 24A.5(e) to state that a submitting member will "have priority" to execute the specified share of a trade, instead of that he will "be permitted" to execute that share, in order to clarify that a member may cross more than the designated share as to which he has priority if no one else is willing to trade at the same or a better price.

⁵ 17 CFR 200.30-3(a)(12) (1994).