

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-38852; File No. SR-CBOE-97-30]

### Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the Chicago Board Options Exchange, Inc. Relating to a Change to a Modified Capitalization-Weighted Index for the Goldman Sachs Technology Composite Index

July 18, 1997.

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> notice is hereby given that on July 9, 1997, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Exchange subsequently filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The Exchange has requested accelerated approval for the proposal, as amended. This order approves the Exchange's proposal, as amended, on an accelerated basis and solicits comments from interested persons.

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

The Exchange is proposing, pursuant to a determination by Goldman, Sachs & Co. ("Goldman Sachs"), to change the weighting methodology of its Goldman Sachs Technology Composite Index ("Composite Index") from a capitalization-weighted index to a modified capitalization-weighted index, limiting components to a maximum of 8.5% of the Composite index weight.<sup>4</sup> The Exchange seeks continued approval

to list and trade options on these indexes after Goldman Sachs has instituted these changes.

#### 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 an 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 III 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

The Exchange currently lists and trades European-style, cash-settled options on the Composite Index pursuant to approval by the Commission.<sup>5</sup> The Composite Index is a capitalization-weighted index of the universe of technology-related company stocks which meet certain objective criteria.<sup>6</sup> The Composite Index is re-balanced semi-annually, in January and July.

The Exchange has been informed by Goldman Sachs that as of the July 1997 re-balancing (effective as of July 18, 1997), Goldman Sachs will be revising its weighting criteria for the Composite Index to a modified capitalization-weighted index. Under the new criteria, no stock can account for more than 8.5% of the weight of the Composite Index at each semi-annual re-balancing. This weighting methodology will be implemented in the same manner as the weighting methodology for the sub-indexes to the Composite Index which were previously approved for options trading by the Commission.<sup>7</sup> The Exchange is requesting that the Commission approve the continued listing and trading of options on the Composite Index after this change is instituted by Goldman Sachs.

###### 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with

and furthers the objectives of Section 6(b)(5) of the Act, in that it is designed to perfect the mechanisms of a free and open market, and to protect investors and the public interest.

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

The Exchange 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

The Exchange states that no written comments were solicited or received with respect to the proposed rule change.

#### III. 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 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 Room. Copies of such filings also will be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-CBOE-97-30 and should be submitted by August 14, 1997.

#### IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 6(b)(5) thereunder.<sup>8</sup> Specifically, the Commission finds that the Exchange's proposal to modify the weighting methodology of the Composite Index from a capitalization-weighted index to a modified capitalization-weighted

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

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

<sup>3</sup> See letter from Eileen Smith, Exchange, to Janice Mitnick, Commission, dated July 18, 1997 ("Amendment No. 1").

In Amendment No. 1, the Exchange amended its proposal to clarify how the Exchange would notify market participants of the change and also states that the impact of the change should be limited because as of July 14, 1997, there were only seven contracts of open interest expiring after the July expiration date. amendment No. 1 also makes a technical correction to the rule filing regarding the basis of summary effectiveness of the proposal.

<sup>4</sup> The Composite Index is a capitalization-weighted index designed to measure the performance of the universe of high capitalization technology stocks. See Release No. 34-37693 (September 17, 1996), 61 FR 50362 (September 25, 1996) (order approving the Exchange's proposal to trade options on the Composite Index (SR-CBOE-96-43)).

<sup>5</sup> See *id.*, *supra* n. 4.

<sup>6</sup> See *id.*, *supra* n. 4.

<sup>7</sup> See Release No. 34-37696 (September 17, 1996), 61 FR 50358 (September 25, 1996) (order approving the Exchange's proposal to trade options on six sub-indexes to the Composite Index (SR-CBOE-96-44)).

<sup>8</sup> In approving this proposal, the Commission notes that it has considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

index, which will limit components to a maximum of 8.5% of the Composite Index weight, will contribute to the maintenance of fair and orderly markets consistent with investor protection by ensuring that no one stock or group of stocks dominate the Composite Index.

The Exchange states that approving the proposed change will allow the continued listing and trading of options on the Composite Index without interruption. As noted above, the change will alter the weighting methodology for the Composite Index from a capitalization-weighted index to a modified capitalization-weighted index, limiting components to a maximum weight of 8.5% of the Composite Index.<sup>9</sup> Currently, two components each comprise more than 8.5% of the Composite Index.<sup>10</sup> The revision to a modified capitalization-weighted index will reduce the impact that those two components have on the index, thereby reducing the opportunity for the Composite Index to be dominated by a few component stocks.

The Commission believes that the proposed weighting method does not present any new or novel regulatory issues as the Exchange's proposal adopts a weighting method which was previously approved by the Commission for sub-indices to the Composite Index.<sup>11</sup> The Composite Index will be calculated through a modified capitalization-weighted method, which is a hybrid between equal weighting (which may impose liquidity concerns for smaller-cap stocks) and capitalization weighting (which may result in two or three stocks dominating an index's performance). Under the method, the maximum weight for each component in the Composite Index will be capped at 8.5%, as of the semiannual rebalancing date. The weight of each component below 8.5% will be market capitalization weighted, and therefore will not be capped. At the time of semi-annual rebalancing, component stocks with weights in excess of their capped weight in the Composite Index will be

restored to the appropriate capped weight. In approving this change, the Commission believes that the new methodology should be beneficial by preventing one or a few stocks from dominating the index and having an undue effect on the index value.

The Exchange proposes to implement the change in calculating the Composite Index after the July expiration, at the close on July 18, 1997. This coincides with the semi-annual rebalancing of the Composite Index. The Commission notes that as of July 14, there were only seven contracts of open interest which expired after the July expiration. While the change to a modified capitalization-weighted index will be applied to these open contracts, the Commission believes that the potential impact on those seven contracts is de minimis and that, in any case, any impact will be outweighed by the anticipated benefits from the alteration of the weighting mechanism.

The Exchange has notified market participants of its proposal to alter the weighting methodology through a notice to members and member firms.<sup>12</sup> The Exchange has also stated it will inform its members and member firms upon approval of the proposal by the Commission.<sup>13</sup> The Commission believes that this will ensure investors have been adequately notified about the impending change prior to its implementation, and should provide them with sufficient time to make any desired adjustments to their positions.

The Commission finds good cause to approve the proposal prior to the thirtieth day after the date of publication of notice of filing in the **Federal Register**. By accelerating the effectiveness of the Exchange's rule proposal, the Commission will enable the new weighting methodology to become effective concurrent with the effective date for the semi-annual rebalancing, subsequent to the July expiration. In addition, the Commission believes that the proposed weighting method does not present any new or novel regulatory issues as the Exchange's proposal adopts a weighting method which will assist in ensuring that one or a few components will not dominate the Composite Index. Further, as noted above, the modified-capitalization weighted method being adopted for the Composite Index is the same method approved by the Commission for the sub-indices to the

Composite Index.<sup>14</sup> Accordingly, the Commission believes that it is consistent with Sections 6(b)(5) and 19(b)(2) of the Act to approve the proposed rule change on an accelerated basis.

## V. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-CBOE-97-30), as amended, is hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 38847; File No. SR-GSCC-97-01]

### Self-Regulatory Organizations; Government Securities Clearing Corporation; Order Approving Proposed Rule Change Regarding Off-The-Market Transactions

July 17, 1997.

On March 11, 1997, the Government Securities Clearing Corporation ("GSCC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR-GSCC-97-01) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposal was published in the **Federal Register** on May 16, 1997.<sup>2</sup> No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

## I. Description

The modifications to GSCC's rules revise the loss allocation provisions and margining process relating to the netting and guaranteed settlement of transactions that have a price that differs significantly from the prevailing market price for the underlying security ("off-the-market transactions"). More specifically, GSCC is defining an off-the-market transaction as any of the following: (1) An options exercise; (2) a single transaction that is (i) greater than \$1 million in par value and (ii) either one percentage point higher than the

<sup>9</sup> Under a modified capitalization-weighted index, the number of index shares of a component stock which is not capped will equal the company's outstanding common shares. The number of index shares for a stock which is capped will equal its maximum weight, multiplied by the adjusted total market capitalization of the Composite Index, and divided by the component stock's closing price on the rebalancing date. The Composite Index's adjusted total market capitalization is the total outstanding market capitalization, adjusted to reflect the number of capped stocks.

<sup>10</sup> As of July 2, 1997, Intel comprised 10.06% of the Composite Index, and Microsoft comprised 13.05% of the Composite Index. Phone conversation between Eileen Smith, Exchange and Janice Mitnick, Commission, on July 11, 1997.

<sup>11</sup> See *supra* n. 7.

<sup>12</sup> See Amendment No. 1. *supra* n.3.

<sup>13</sup> Phone conversation between Eileen Smith, Exchange and Janice Mitnick, Commission, on July 16, 1997.

<sup>14</sup> See *supra* n.7.

<sup>15</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> Securities Exchange Act Release No. 38601 (May 9, 1997), 62 FR 27089.