

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁷

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39856; File No. SR-Phlx-97-63]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the Philadelphia Stock Exchange, Inc. to Amend its Method of Calculating Initial and Maintenance Margin Requirements for Foreign Currency Options

April 13, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on December 22, 1997, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. On February 20, 1998, the Phlx filed a Letter Amendment to the proposed rule change.³ The Phlx filed Amendment No. 1 to the proposed rule change on April 6, 1998.⁴ The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Phlx proposes to amend Phlx Rule 722 to codify its method of calculating initial and maintenance customer margin requirements for foreign currency options. Under proposed new Commentary .16 to Rule 722, the Exchange would calculate the margin requirements for each foreign currency separately, rather than determining one margin level for all foreign currencies based upon the historical pricing information for all foreign currencies together.

The complete text of the proposed rule change is available at the Office of the Secretary, Phlx and at the Commission.

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

In its filing with the Commission, the Phlx 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 Phlx 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, the Exchange calculates the margin requirement for customers that assume short foreign currency option positions by adding 4% of the current market value of the underlying foreign currency contract to the option premium price less an adjustment for the out-of-the-money amount of the option contract.⁵ The 4% add-on percentage was adopted in 1986 and provided for initial margin which would cover the aggregate underlying foreign currencies' historical volatility over a seven day period with a 95% confidence level over the latest nine month period.⁶ This add-on percentage

⁵ This 4% "add-on" percentage is applicable to the following foreign currencies: Australian dollar, British pound, Canadian dollar, German mark, European Currency Unit, French franc, Japanese yen and Swiss franc. The Spanish peseta and the Italian lira currently have a 7% add-on percentage and the Mexican peso has an add-on percentage of 17%.

⁶ See Securities Exchange Act Release No. 22469 (September 26, 1985) 50 FR 40663 (October 4, 1985) (order approving File Nos. SR-Amex-84-29, SR-

is now reviewed by the Exchange every quarter to assure that it provides for a 97.5% confidence level over a five day period. Recently, the Exchange has listed new foreign currency options such as the Spanish peseta and the Italian lira⁷ and has received approval to trade options on the Mexican peso.⁸ In determining the appropriate margin levels for these new currencies, the Commission has indicated that it believes that the Exchange should set margin levels for each foreign currency option independently and that it should state its specific procedure for setting these levels in its rules. The purpose of this proposal is to address this issue by adopting new foreign currency options margin procedures as proposed in Commentary .16 to Rule 722.

The Exchange is proposing to determine the applicable add-on percentage by reviewing, on a quarterly calendar basis,⁹ five-day price changes over the preceding three-year period for each underlying currency and set the add-on percentage at a level which would have covered those price changes at least 97.5% of the time ("confidence level"). If the results of subsequent reviews show that the current margin level provides a confidence level below 97%, the Exchange will increase the margin requirement for that individual currency up to a 98% confidence level. If the confidence level is between 97% and 97.5%, the margin level will remain the same but will be subject to monthly follow-up reviews until the confidence level exceeds 97.5% for two consecutive months.¹⁰ If during the course of the monthly follow-up reviews, the confidence level drops below 97%, the margin level will be increased to a 98% level and if it exceeds 97.5% for two consecutive months, the currency will be taken off monthly reviews and will

CBOE-84-27, SR-NASD-85-15, SR-PSE-84-20, SR-Phlx-84-32 and SR-Phlx-85-18 and establishing a uniform margin system for options products).

⁷ See Securities Exchange Act Release No. 36255 (September 20, 1995) 60 FR 50229 (September 28, 1995) (order approving File Nos. SR-Phlx-95-20 and SR-Phlx-95-21).

⁸ See Securities Exchange Act Release No. 39460 (December 17, 1997) 62 FR 67425 (December 24, 1997) (order approving File No. SR-Phlx-97-22).

⁹ Although the Phlx initially proposed semi-annual margin reviews, in Amendment No. 1, the Phlx proposes to amend Commentary .16(b) of Rule 722 to require margin reviews to be conducted quarterly, on the 15th of January, April, July and October of each year. See Amendment No. 1, *supra* note 4.

¹⁰ As initially proposed, it was unclear whether monthly margin reviews would be required once the confidence level equaled 97.5%. Amendment No. 1 makes clear that the confidence level must exceed 97.5% for two consecutive months before the currency will no longer be reviewed monthly. See Amendment No. 1, *supra* note 4.

²⁷ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Letter from Michele R. Weisbaum, Vice President and Associate General Counsel, Phlx, to Sharon Lawson, Senior Special Counsel, Division of Market Regulation ("Division"), Commission, dated February 19, 1998 ("Letter Amendment"). In the Letter Amendment, the Phlx proposes to amend its proposed rule change to: (1) conduct margin reviews quarterly rather than semi-annually; (2) monitor currencies monthly when the confidence level falls to between 97% and 97.5% until the confidence level exceeds 97.5% for two consecutive months, rather than just one month; and (3) revise Rule 722 to exclude the actual margin level for each currency and to note that instead, the Phlx will distribute membership circulars announcing the margin levels that are derived pursuant to Commentary .16 of Rule 722.

⁴ See Letter from Nandita Yagnik, Counsel, Phlx, to Sharon Lawson, Senior Special Counsel, Division, Commission, dated April 3, 1998 ("Amendment No. 1"). Amendment No. 1 incorporates the original proposed rule change and Letter Amendment into a Rule 19b-4 notice.

be put back on the quarterly review cycle. If the currency exceeds 98.5%, the margin level will be reduced to a 98% confidence level. Finally, in order to account for large price movements outside the margin level, if the review shows that the currency had a price movement, either positive or negative, greater than two times the margin level, the margin requirement would be set at a level to meet a 99% confidence level ("extreme outlier test").

The quarterly reviews will be conducted promptly following the 15th of January, April, July and October of each year. In addition to the routine reviews described above, the Exchange continues to have authority to impose a higher margin level at any time in between reviews if market conditions so warrant.¹¹ At this time, the margin levels for Tier I, II, and III customized cross rate options will remain the same.

Finally, the Phlx proposes to revise Rule 722 so that while the calculation methodology will be outlined in Commentary .16, the actual margin level for each currency will not be stated. Instead, the Exchange will distribute circulars to the membership announcing the margin levels that are derived pursuant to the methodology in Commentary .16 to Rule 722. In addition, any time that a particular margin level changes based on a review or otherwise pursuant to Rule 722, the new margin requirement will be announced via circular to the membership.¹²

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6 of the Act¹³ in general, and in particular, with Section 6(b)(5),¹⁴ in that it is designed to promote just and equitable principles of trade, prevent fraudulent and manipulative acts and practices, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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 by establishing margin levels for foreign currency options which reflect the specific risks associated with each individual currency.

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

The Phlx does not believe that the proposed rule change will impose any inappropriate burden on competition.

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

No written comments were either solicited or 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 or such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Phlx 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, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, 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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-Phlx-97-63

and should be submitted by May 11, 1998.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Margaret H. McFarland,
Deputy Secretary.

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DEPARTMENT OF STATE

[Public Notice #2789]

Advisory Committee on International Communications and Information Policy; Meeting Notice

The Department of State is holding the next meeting of its Advisory Committee on International Communications and Information Policy. The Committee provides a formal channel for regular consultation and coordination on major economic, social and legal issues and problems in international communications and information policy, especially as these issues and problems involve users of information and communication services, providers of such services, technology research and development, foreign industrial and regulatory policy, the activities of international organizations with regard to communications and information, and developing country interests.

The meeting will be devoted to discussion of issues of interest to members, particularly as to the work of the State Department on telecommunications policy involving both bilateral and multilateral fora.

In addition, the purpose of this meeting will be to hear reports from the working groups on various issues that chart the future direction and work plan of the committee. The members will look at the substantive issues on which the committee should focus, as well as specific countries and regions of interest to the committee.

This meeting will be held on Thursday, April 30, 1998, from 9:30 a.m.—12:30 p.m. in Room 1107 of the Main Building of the U.S. Department of State, located at 2201 "C" Street, NW., Washington, DC 20520. Members of the public may attend these meetings up to the seating capacity of the room. While the meeting is open to the public, admittance to the State Department Building is only by means of a pre-arranged clearance list. In order to be placed on the pre-clearance list, please provide your name, title, company,

¹¹ See Phlx Rule 772(i)(8).

¹² As initially proposed, all changes to the add-on percentages for individual currencies set forth in Phlx Rule 722 would have required a proposed rule change to be filed with the Commission pursuant to Section 19(b)(3)(A) of the Act. As changes to the margin levels for individual currencies will not require changes to Phlx Rule 722 and instead, will be announced to the Phlx membership via circular, such changes will not trigger a requirement to subject a 19(b)(3)(A) filing to the Commission. Telephone conversation between Nandita Yagnik, Counsel, Phlx, and Deborah Flynn, Division, Commission, on April 13, 1998.

¹³ 15 U.S.C. 78f.

¹⁴ 15 U.S.C. 78f(b)(5).

¹⁵ 17 CFR 200.30-3(a)(12).