

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39941; File No. SR-Amex-98-11]

Self-Regulatory Organizations; American Stock Exchange, Inc.; Order Granting Approval of Proposed Rule Change and Amendment No. 1 Thereto and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 2 to Proposed Rule Change Relating to a Reduction in the Value of the de Jager Year 2000 and Amex Airline Indices

May 1, 1998.

I. Introduction

On February 23, 1997, the American Stock Exchange, Inc. ("Amex" or "Exchange") submitted to the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² a proposed rule change to split the de Jager Year 2000 ("de Jager Index"), Amex Securities Broker/Dealer Index ("Broker/Dealer Index") and Amex Airline ("Airline Index") Indices to one-half of their current values. On March 11, 1998, the Amex filed Amendment No. 1 to the proposed rule change.³ On March 20, 1998, the Amex filed Amendment No. 2 to the proposed rule change.⁴

On March 26, 1998, the proposed rule change and Amendment No. 1 were

published for comment in the **Federal Register**⁵ and the Commission granted accelerated approval to the portion of the proposal relating to the Broker/Dealer Index. No comments were received on the proposal. This order approves the portions of the proposed rule change relating to the de Jager Index and Airline Index (collectively, "de Jager and Airline Indices") and approves Amendment No. 2 on an accelerated basis.

II. Description of the Proposal

The Commission granted the Exchange approval to list and trade options on the de Jager⁶ and the Airline⁷ Indices on February 19, 1997 and December 12, 1994, respectively. Initially, the aggregate value of the stocks contained in the de Jager and Airline Indices was reduced by divisors to establish index benchmark values of 250 and 200, respectively. Over the past two years, the index value of the Airline Index has more than tripled in value from 200 to 728. Moreover, since its creation, the index value of the de Jager Index has nearly doubled in value from 250⁸ to 413.

As a consequence of the rising values of the Indices, premium levels for options on the de Jager and Airline Indices have also risen. According to the Exchange, these higher premium levels have been cited as the principal factor that has discourage retail investors and some small market professionals from trading these index options. As a result, the Exchange is proposing to decrease the de Jager and Airline Indices to one-half of their respective present values.

To decrease the values of the Indices, the Exchange will double the divisor used in calculating the de Jager and Airline Indices. The Amex proposes no other changes to the components of the Indices, their methods of calculation (other than the change in the divisor), expiration style of the options or any other Index specification.

The Amex believes that lower values Indices will result in substantial lowering of the dollar values of options premiums for options contracts on the de Jager and Airline Indices. The Exchange plans to adjust outstanding

series similar to the manner in which equity options are adjusted for a 2-for-1 stock split. On the effective date of the split "ex-date," the number of outstanding options contracts on the de Jager and Airline Indices will be doubled and the associated strike prices halved.

Position and Exercise Limits

Currently, position and exercise limits for the de Jager Index equal 12,000 contracts, while position and exercise limits for the Airline Index equal 15,000 contracts, on the same side of the market. The Exchange proposes to double the position and exercise limits to 24,000 contracts for the de Jager Index and to 30,000 contracts for the Airline Index on the same side of the market. This change will be made simultaneously with the proposed reduction of the Indices' values and the doubling of the number of contracts.

Since the new position and exercise limits will be equivalent to the Indices' present limits, the Exchange believes there is no additional potential for manipulation of the Indices or the underlying securities. Further, an investor who is currently at the de Jager (12,000) or Airline (15,000) Indices' contract limit will, as a result of the Index value reductions, automatically hold 24,000 or 30,000 contracts, respectively, to correspond with the lowered Index values. These increased position and exercise limits will revert to their original limits at the expiration of the furthest expiration month for non-LEAPs as established on the date of the split.

III. Discussion

The Commission finds that the proposed rule change, as amended, relating to the de Jager and Airline Indices is consistent with the requirements of Section 6 of the Act⁹ and the rules and regulations thereunder applicable to a national securities exchange.¹⁰ Specifically, the Commission believes that the provisions of the proposed rule change pertaining to the de Jager and Airline Indices are consistent with and further the objectives of Section 6(b)(5) of the Act¹¹ in that the proposed reduction in value of the de Jager and Airline Indices and the associated temporary increases in the position and exercise limits should remove impediments to and perfect the mechanism of a free and open market in

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Letter from Scott G. Van Hatten, Legal Counsel, Derivative Securities, Amex, to Sharon Lawson, Assistant Director, Division of Market Regulation ("Division"), Commission, dated March 10, 1998 ("Amendment No. 1"). In Amendment No. 1, the Amex requests expedited review and accelerated effectiveness of the proposed rule change with respect to the provisions concerning the Broker/Dealer Index. In addition to correcting a clerical error, Amendment No. 1 also makes clear that the position and exercise limits, which are proposed to be initially doubled, will revert to their original limits at the expiration of the furthest expiration month for non-long term options series ("LEAPs") as established on the date of the split.

⁴ See Letter from Scott G. Van Hatten, Legal Counsel, Derivative Securities, Amex, to Sharon Lawson, Assistant Director, Division, Commission, dated March 19, 1998 ("Amendment No. 2"). In Amendment No. 2, the Amex represents that, in connection with the splitting of the Airline, Broker/Dealer and de Jager Indices, it will issue: (1) a circular to its members at least two weeks prior to the split, disclosing the pre- and post-reduction values, the doubling of the number of contracts, and the temporary doubling of the position limits for the options overlying such Indices; (2) a second notice to its members just prior to implementing the index reductions setting forth the new divisor and other relevant information; and (3) a circular at least one month prior to the expiration of the furthest non-LEAP options reminding members that the position limits are scheduled to revert to the original levels.

⁵ See Securities Exchange Act Release No. 39775 (March 20, 1998) 63 FR 14741.

⁶ See Securities Exchange Act Release No. 38307 62 FR 8469 (February 25, 1997) (order approving File No. SR-Amex-97-04).

⁷ See Securities Exchange Act Release No. 35084 59 FR 65419 (December 19, 1994) (order approving File No. SR-Amex-94-54).

⁸ As originally filed, the proposal incorrectly listed the de Jager's benchmark Index value as 200. This clerical error was corrected by the Exchange in Amendment No. 1. See Amendment No. 1, *supra* note 3.

⁹ 15 U.S.C. 78f.

¹⁰ In approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹¹ 15 U.S.C. 78f(b)(5).

a manner consistent with the protection of investors and the public interest.

By reducing the value of the de Jager and Airline Indices, the Commission believes that a broader range of investors will be provided with a means to hedge their exposure to the market risk associated with the stocks underlying the Indices. Similarly, the Commission believes that reducing the value of the de Jager and Airline Indices may attract additional investors, thus creating a more active and liquid trading market.

The Commission also believes that Amex's proposed adjustments to its position and exercise limits applicable to the de Jager and Airline Indices are appropriate and consistent with the Act. In particular, the Commission believes that the temporary doubling of the position and exercise limits are reasonable in light of the fact that the size of the options contracts on the de Jager and Airline Indices will be halved and that, as a result, the number of outstanding options contracts an investor holds will be doubled. The temporary doubling of the position and exercise limits, therefore, will ensure that investors will not potentially be in violation of the lower existing position and exercise limits while permitting market participants to maintain, after the split of the de Jager and Airline Indices, their current level of investment in the de Jager and Airline Index options contracts. As noted above, the increased position and exercise limits of 24,000 and 30,000 contracts will revert to their original limits of 12,000 and 15,000 contracts, respectively, at the expiration of the furthest expiration month for non-LEAPs as established on the date of the split.¹²

The Commission further believes that doubling the de Jager and Airline Indices' divisors will not have an adverse market impact on the trading in these options. After the split, the de Jager and Airline Indices will continue to be composed of the same stocks with the same weightings and will be calculated in the same manner, except for the proposed change in the divisors. The Commission notes that the Amex's

surveillance procedures also will remain the same.

Finally, the Commission notes that, prior to implementing the proposed changes, the Exchange will provide advance notice of the proposed changes to the de Jager and Airline Indices to its membership.¹³ The de Jager and Airline Indices are expected to be reduced by one-half immediately following the May 15, 1998 expiration.¹⁴ The Amex has committed to provide notice to its membership at least two weeks prior to the implementation of the proposed changes to the values of the de Jager and Airline Indices and the resulting adjustments to the outstanding options contracts on the de Jager and Airline Indices.¹⁵ In addition, the Commission notes that the Exchange has agreed to issue a second notice to its members just prior to implementing the Index reductions setting forth the new divisor and other relevant information.¹⁶ Finally, the Exchange has agreed to issue a circular to its members at least one month prior to the expiration of the furthest non-LEAP options on the de Jager and Airline Indices reminding its member firms that the respective position and exercise limits will revert to their original levels.¹⁷ The Commission believes that the proposed time frames should allow for adequate notice to be provided to the holders of all open positions in options on the de Jager and Airline Indices and other market participants.

The Commission finds good cause for approving Amendment No. 2 to the proposed rule change prior to the thirtieth day after publication in the **Federal Register**. The Commission notes that Amendment No. 2 merely codifies the notification procedures that the Amex had agreed to verbally prior to the Commission's grant of partial accelerated approval to the reduction in value of the Broker/Dealer Index. The Commission believes that Amendment No. 2 should ensure that market participants will receive adequate notice prior to the implementation of the adjustments to the values of the de Jager and Airline Indices and the eventual reversion to the original position and exercise limits. Accordingly, the Commission finds that good cause

exists, consistent with Section 6(b)(5) of the Act,¹⁸ to accelerate approval of Amendment No. 2 to the proposed rule change.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning Amendment No. 2, including whether Amendment No. 2 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, D.C. 20549. Copies of the submissions, 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 Room, 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 Amex. All submissions should refer to File Number SR-Amex-98-11 and should be submitted by May 28, 1998.

V. Conclusion

For the foregoing reasons, the Commission finds that the Amex's proposal, as amended, to reduce the value of the de Jager and Airline Indices by one-half and to temporarily double the corresponding position and exercise limits, is consistent with the requirements of the Act and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹⁹ that the portions of the amended proposed rule change (SR-Amex-98-11) relating to the de Jager and Airline Indices are approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁰

Jonathan G. Katz,
Secretary.

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¹² According to the Amex, January 1999 and February 1999 will be the furthest expiration months for non-LEAPs on the Airline and de Jager Indices, respectively, for purposes of the reversion of position and exercise limits to their original levels. Per telephone conversation between Scott Hatten, Legal Counsel, Derivative Securities, Amex, and Deborah Flynn, Division, Commission, on April 29, 1998.

¹³ See Amendment No. 2, *supra* note 5.

¹⁴ Per telephone conversation between Scott Van Hatten, Legal Counsel, Derivative Securities, Amex, and Deborah Flynn, Division, Commission, on May 1, 1998.

¹⁵ See Amendment No. 2, *supra* note 5.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ 15 U.S.C. 78f(b)(5).

¹⁹ 15 U.S.C. 78s(b)(2).

²⁰ 17 CFR 200.30-3(a)(12).