

III. Date of Effectiveness of the Proposed Rule Changes 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 DTC or NSCC consents, the Commission will:

(A) By order approve such proposed rule changes or

(B) Institute proceedings to determine whether the proposed rules 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 changes are 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 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 in the Commission's Public Reference Section, 450 Fifth Street, NW., Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of DTC and NSCC. All submissions should refer to File Nos. SR-DTC-98-09 and SR-NSCC-98-05 and should be submitted by June 25, 1998.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁹

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40042; File No. SR-OCC-98-03]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change Relating to the Stock Loan/Hedge Program

May 28, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on April 13, 1998, 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 from interested persons on the proposed rule change.

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

The purpose of the proposed rule change is to amend OCC's By-Laws and Rules governing OCC's stock loan/hedge program ("hedge program") under which OCC operates a centralized facility for administering stock loan and stock borrow transactions between OCC clearing members.

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.²

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Overall Purpose

In general, the purpose of the proposed rule change is to make comprehensive amendments to OCC's By-Laws and Rules that govern the hedge program. Clearing members that are approved to participate in the hedge

program are referred to as "hedge clearing members." A clearing member that lends stock through the hedge program is referred to as a "lending clearing member," and a clearing member that borrows stock is referred to as a "borrowing clearing member." Stocks that are eligible for the hedge program are referred to as "eligible stocks."

2. Summary of Primary Changes in Program

(i) *Stock Loan Initiation.* Currently under the hedge program, a stock loan is initiated when two hedge clearing members agree on the terms of the loan, the lending clearing member transfers the stock to OCC's account at a "correspondent depository" (i.e., a securities depository at which OCC has an account), OCC directs the correspondent depository to redeliver the stock to the borrowing clearing member against payment of the required collateral amount to OCC, and OCC pays over the required collateral amount to the lending clearing member.

Under the revised hedge program, OCC will have no involvement in a stock loan until after the clearing members that are parties to the stock loan have completed the transaction between themselves through the facilities of The Depository Trust Company ("DTC"). Upon receiving notice of the stock loan from DTC, OCC will verify the accuracy of the clearing members' account numbers and the information supplied to OCC with respect to the transaction. If this information is verified, OCC will accept the loan into the hedge program. Upon acceptance (and only upon acceptance) by OCC, the stock loan contract between the stock lender and the stock borrower will be replaced by two parallel contracts with congruent terms: one between the stock lender and OCC as stock borrower and one between the stock borrower and OCC as stock lender. If OCC rejects a transaction, the transaction will remain in effect between the lending clearing member and the borrowing clearing member but outside the hedge program.

(ii) *Universe of Eligible Stocks.* Currently, the only stocks eligible for the hedge program are stock that are the underlying stocks for stock option contracts. Under the proposed rule change, all equity securities that are eligible for deposit at DTC will be eligible for the hedge program (other than any stock as to which OCC has made a determination pursuant to Section 2(c) of Article XXI of its By-Laws to terminate all outstanding stock loans relating to that stock).

¹ 15 U.S.C. 78s(b)(1).

² The Commission has modified the text of the summaries prepared by OCC.

⁹ 17 CFR 200.30-3(a)(12).

(iii) *Margin-Ineligible Stock Loan and Borrow Positions.* Under the current hedge program, all stock loan and stock borrow positions are taken into account in calculating each clearing member's obligation to deposit "additional margin" with OCC³ and may generate either an increased additional margin requirement (if the stock loan or borrow positions do not hedge other positions of the clearing member) or a reduced additional margin requirement (if the stock loan or borrow positions do hedge other positions of the clearing member).

Under the proposed rule change, a clearing member will be able to designate one or more of its accounts with OCC as "margin-ineligible." If an account is designated as margin-ineligible, OCC will not include any stock loan and stock borrow positions carried in that account in the calculation of the clearing member's additional margin obligations. Instead, OCC will rely on the other elements of its protection and back-up systems (primarily its clearing fund and its concentration monitoring surveillance system) to mitigate the risk to OCC created by those positions.⁴

(iv) *Stock Loan and Borrow Baskets.* Under the proposed rule change, a clearing member will be able to instruct OCC to treat specified stock loan positions in an account as constituting a "stock loan basket" and may instruct OCC to treat specified stock borrow positions in an account as constituting a "stock borrow basket." Stock loan baskets and stock borrow baskets will be subject to margin under OCC's Rule

602.⁵ The current hedge program has no provisions for stock loan and borrow baskets.

(v) *Stock Loan Termination.* Under the proposed rule change, the process for terminating stock loans will parallel the changes to the process for initiating stock loans. Under the current hedge program, a stock loan is terminated when the borrowing clearing member transfers the stock to OCC's account at the correspondent depository, OCC directs the correspondent depository to redeliver the stock to the lending clearing member against payment of the collateral amount to OCC, and OCC pays the collateral amount over to the borrowing clearing member. Under the proposed rule change, a stock loan will be terminated when the borrowing clearing member transfers the stock directly to the account of the lending clearing member at DTC against payment of the collateral amount to the DTC account of the borrowing clearing member.

3. Section-by-Section Discussion

In Article I of OCC's By-Laws, the definition of the term "eligible stock" will be revised to include all equity securities that are eligible for deposit at DTC. The terms "margin-eligible," "margin-ineligible," "stock borrow basket," and "stock loan basket" will be defined for the purposes described above.

Article VIII of OCC's By-Laws will be amended to include the stock loan basket and stock borrow basket concepts in OCC's clearing fund. OCC's clearing fund is comprised of a "stock clearing fund" and a "non-equity securities clearing fund." Clearing members' contributions to each are based upon the members' equity option margin requirements under rule 601 and members' NEO margin requirements under Rule 602. As discussed above, stock loan and borrow baskets will be subject to margin in OCC's NEO margin system. Therefore, stock loan and borrow baskets will be taken into account in determining clearing members' contributions to the non-equity securities clearing fund. If OCC were ever to suffer a loss attributable to stock loan or borrow baskets, OCC's first recourse to the clearing fund would be to the non-equity securities clearing fund.

The definitions in Article XXI, Section 1 of the By-Laws will be revised

primarily to accommodate the revisions to the manner in which stock loans are initiated. The definitions of the terms "collateral" and "loaned stock" will be revised to reflect that the loaned stock and collateral will no longer be passed through OCC's account at DTC. The definition of "correspondent depository" will be deleted and replaced with the new term "depository." The term "stock loan business day" will be defined as a day on which OCC and DTC are both open for business, and this term will be used in the Rules describing stock loan settlement procedures.

Article XXI, Section 2 of the By-Laws will be amended to reflect the revised manner in which stock loans are initiated, as described above. An interpretation will be added to section 2 to address certain situations in which the termination of a stock loan is reported to OCC at a settlement price (i.e., reflecting payment by the lending clearing member of an amount of collateral) which is not consistent with OCC's records. A similar interpretation will be added to Rule 2209 (currently Rule 2208) to address situations in which OCC receives a report of the termination either of a purported stock loan which does not exist on OCC's records or of a stock loan on OCC's records in a quantity which does not match the quantity in the termination report. OCC anticipates that both of these types of situations will be extremely unusual. However, they are theoretically possible because OCC will receive reports of terminations of stock loans only after the transactions are final on DTC's books. OCC's records will be dispositive in both of these types of situations, and OCC will not accept any responsibility for reconciling the discrepancy between its records and those of the affected clearing members.

Paragraph (d) in Article XXI, Section 5 will be deleted. This paragraph currently limits the stock loan and borrow positions that may be maintained in a stock market-maker's or stock specialist's account to positions relating to the stock for which the stock market-maker or stock specialist acts as stock market-maker or stock specialist. Article VI, Section 3(f) of OCC's By-Laws restricts the options transactions which may be conducted in a stock market-maker's or stock specialist's account to those in options on underlying stocks for which the stock market-maker or specialist acts as market-maker or specialist. Section 5(d) of Article XXI was intended to extend that restriction to stock loan and borrow positions. However, the purpose of the Article VI, Section 3(f) restriction is to

³ Under the current hedge program, a hedge clearing member is required to deposit margin with OCC to cover OCC's risk that the market will move against the member's stock loan and borrow positions during a day and that the member will fail before making the required mark-to-market payment on the next business day. Under the proposed rule change, a hedge clearing member will continue to be required to deposit margin with OCC but only with respect to "margin-eligible" stock loan and borrow positions. This margin is analogous to the "additional margin" that OCC requires with respect to short stock option positions, and therefore it is referred to in OCC's rules and in this notice as "additional margin."

⁴ Under the proposed rule change, lending and borrowing clearing members will continue to be required to pay or be entitled to daily mark-to-market payments to adjust the collateral held by lending clearing members with respect to all stock loans. The purpose of additional margin is to protect OCC from the risk of an adverse market move between mark-to-market payments. OCC has concluded that the other elements of its protection and back-up systems should be adequate to protect it against this risk with respect to margin-ineligible stock loan and borrow positions. Margin-ineligible stock loan and borrow positions will be taken into account in determining the clearing fund contributions of hedge clearing members even though they will not be taken into account in margin calculations.

⁵ OCC Rule 602 describes the calculation of margin requirements for securities which are neither equity securities nor based on equity securities. This margin system is sometimes referred to as OCC's "NEO" or "non-equity option" margin system.

facilitate surveillance of stock market-makers' and specialists' trading activity conducted in those accounts.⁶ Stock loan and borrow positions are created by hedge clearing members and not by the stock market-maker or specialist for which a stock-market maker's or specialist's account is established. Therefore, the paragraph (d) restriction is irrelevant to the surveillance purpose of the Article VI, Section 3(f) restriction. OCC believes that a hedge clearing member should be permitted to carry a stock loan or borrow position relating to a particular stock in a stock-market maker's or specialist's account that is restricted to options transactions in a different stock if the clearing member wishes to do so.

A new paragraph (b)(12) will be added to Rule 601 to state that margin-ineligible stock loan and borrow positions will not be taken into account in determining a clearing member's margin requirements. Rule 601(c) will be revised to state that additional margin on margin-eligible stock loan and borrow positions will be based only on the "net" stock loan or borrow position in an account in a manner analogous to the method that OCC uses for options.⁷ Interpretation .06 to Rule 601 will be deleted because OCC has determined that it is unnecessary to have a special rule for the "margin interval"⁸ to be used for stock loan and borrow positions maintained in an account in which no options in the same class group are being maintained.

Rule 602 will be amended to incorporate references to stock loan baskets and stock borrow baskets. The definition of "class group" in paragraph (b)(2) will be amended to state that OCC will treat any stock loan basket or stock borrow basket defined by a clearing member as within the class group identified by the clearing member even if the stock loan or borrow positions comprising the basket do not replicate the composition or weighting of the index group for the class group and even if the stocks underlying the identified stock loan or borrow positions are not even included in the

index group. However, a stock loan or borrow basket that does not meaningfully replicate the composition and weighting of the index group for a class group will be subject to a very large haircut when OCC takes the basket into account in determining the additional margin requirement for the class group.⁹ OCC has developed the systems capacity to be able to analyze customized portfolios and assign appropriate haircuts to them on a large-volume, overnight basis. OCC believes that enabling hedge clearing members to use stock loan and borrow positions in OCC's NEO margin system will offer OCC additional margin in a desirable form because the assets, unlike cash, government securities, and letters of credit, will "co-vary" to some degree with the clearing members' short option positions on the opposite side of the market. In addition, including stock loan and borrow positions as offsets in the NEO system will allow clearing members to reduce their net additional margin requirements.

Changes will be made to the definitions of "marking price" in Rule 602(b)(6) and "margin interval" in Rule 602(b)(8) to extend these concepts to stock loan and borrow baskets. A new sentence will be added to Rule 602(c)(1)(ii)(A) to state that if a clearing member defines two or more stock loan baskets or two or more stock borrow baskets in an account as within the same class group, OCC will take each basket into account separately, and calculate a "haircut" for each separately in determining additional margin for the class group.

A new sentence will be added to Rule 602(c)(1)(ii)(B) to reflect that the daily mark-to-market payments between lending and borrowing clearing members that are described in Rule 2204 (currently Rule 2203) are the functional equivalent of premium margin deposited with OCC with respect to short option positions. Changes to Rule 602(c)(1)(C) will extend the description of the calculation of additional margin in the NEO margin system to stock loan and borrow baskets. Changes to Rules 602(d) and (e) will extend those provisions to stock loan and borrow baskets. A new Rule 602(f)(8) will describe the way that OCC will proceed in certain special circumstances in which a hedge clearing member reduces or terminates a stock loan or borrow position which is completely or partly included in a stock loan basket or stock borrow basket. Interpretations .06 and .07 to Rule 602

will be modified to extend them to stock loan and borrow baskets.

Rule 1001 will be amended to describe the way that stock loan and borrow baskets will be taken into account in determining hedge clearing members' contributions to the stock clearing fund and the non-equity securities clearing fund. These changes will parallel the changes to Article VIII of the By-Laws.

Rule 1104 will be amended to delete a phrase that currently states that if a hedge clearing member is suspended the proceeds from the closing out of stock loan positions and stock borrow positions in the clearing member's customers' account will be subject to the special accounting for customer funds that is described in the Rule. Proceeds from the closing out of stock loan positions and stock borrow positions are correctly characterized as funds of the clearing member and not funds of the clearing member's customers because stock loan and borrow positions (even those that are carried in a customers' account so that they can provide additional margin offsets in that account) are correctly characterized as positions of the clearing member and not positions of the clearing member's customers.¹⁰

A new Rule 2201 will be added to OCC's rules. Rule 2201(a) will describe the standing instructions regarding the hedge program that a hedge clearing member will be expected to maintain with OCC. Rule 2201(b) will describe situations under which a hedge clearing member may provide OCC specific instructions that override the clearing member's standing instructions.

Rule 2201(a)(iv) will require a hedge clearing member to provide OCC with a standing instruction as to the account from and to which the clearing member wishes its net daily mark-to-market payments to be made. The rule will state that the clearing member may specify either its firm account or its combined market-makers' or specialists' account for this purpose. OCC believes that funds deposited as collateral by a borrowing clearing member with a lending clearing member to secure its obligation to return the loaned stock do not constitute funds of the customers of

⁶ Securities Exchange Act Release No. 22692 (December 6, 1985), 50 FR 50882 [File No. SR-OCC-85-15].

⁷ Rule 601 currently provides that additional margin calculations are based in part on the "gross" stock loan and borrow positions of a hedge clearing member (i.e., without regard to whether a position on the other side of the market was carried in the account). OCC has concluded that requiring additional margin on the gross positions leads to over-margining and is an unnecessary disincentive for clearing members to use the hedge program.

⁸ "Margin interval" is the maximum daily change in the marking price of the underlying security, upwards or downwards, assumed by OCC for purposes of calculating additional margin.

⁹ OCC's authority to determine haircuts is set forth in OCC Rule 602(c)(1)(ii)(C)(1).

¹⁰ The interests of the clearing member's customers are nonetheless protected because the clearing member is required under Rule 15c3-3 of the Act, 17 CFR 240.15c3-3, to include in its calculations of the amount which it is required to maintain on deposit in its Reserve Bank Account "Monies borrowed collateralized by securities carried for the account of customers" (Item 2) and "Monies payable against customers' securities loaned" (Item 3). This subject is discussed in Securities Exchange Act Release No. 39738 (March 10, 1998), 63 FR 13082 [File No. SR-OCC-97-11].

either the lending clearing member or the borrowing clearing member regardless of the accounts in which stock loan and stock borrow positions are carried. OCC believes that funds paid to adjust the collateral also do not constitute customer funds and therefore that cross-account netting of mark-to-market payments is appropriate and permissible.

Rule 2202 (currently rule 2201) will be rewritten to describe the new stock loan initiation process, and in particular to reflect the elimination of any role of an OCC account at DTC in the stock loan initiation process. Rule 2202(c) (currently Rule 2201(e)) will be revised to state that the sole obligation of the lending clearing member with respect to the collateral which it holds shall be to "act as agent for [OCC] in repaying an amount equal to the Collateral * * *, or in otherwise disposing of the Collateral in such other manner as the Corporation may direct in the event that the Borrowing Clearing Member has been suspended pursuant to Chapter XI of the Rules, if and when the Stock Loan is terminated as provided in the Rules." This language parallels new language in Rule 2208(c) which says that the actions of the borrowing clearing member to terminate a stock loan "shall be undertaken as [OCC's] agent, and [OCC] shall have the authority to instruct the Borrowing Clearing Member to proceed in another manner in the event that the Lending Clearing Member has been suspended pursuant to Chapter XI of the Rules."

In each case, this language is intended to give OCC, if it must suspend a hedge clearing member, the express authority to instruct each hedge clearing member on the other side of the suspended clearing member's stock loans not to use the ordinary stock loan termination procedures but instead to use the collateral to buy in the loaned stock (if the suspended clearing member is the borrowing clearing member) or to sell out the loaned stock and apply the proceeds to the repayment of the collateral (if the suspended clearing member is the lending clearing member). These statements of express authority are necessary because under the revised process for terminating stock loans when neither hedge clearing member has been suspended, the borrowing clearing member and the lending clearing member will return the loaned stock and the collateral directly to each other's DTC account rather than to OCC's DTC account. In the absence of this expressly stated authority to instruct hedge clearing members that have not been suspended to proceed in another manner, it might be difficult

under the revised hedge program for OCC to control the disposition of assets held by clearing members on the other side of stock loans from the suspended clearing member.

Changes will be made to Rule 2203 (currently Rule 2202) to reflect the fact that a hedge clearing member may declare its stock loan and borrow positions margin-ineligible. The calculation of margin deposited with OCC margin for stock loan and borrow baskets will be described in Rule 602.

Rule 2204 (currently Rule 2203) will be amended to provide for the netting across all of a hedge clearing member's accounts of the mark-to-market payments due to and from the clearing member with respect to the clearing member's stock loan and stock borrow positions on each business day. OCC believes that the changes in Rule 2204 are appropriate for the same reason that underlies the changes in Rule 1104 described above. Namely, that funds deposited as collateral by a borrowing clearing member with a lending clearing member to secure its obligation to return the loaned stock do not constitute funds of the customers of either the lending clearing member or the borrowing clearing member regardless of the accounts in which stock loan and stock borrow positions are carried. OCC believes that funds paid to adjust the collateral also do not constitute customer funds and therefore that cross-account netting of mark-to-market payments is appropriate and permissible.

OCC will specify in Rule 2201(a)(iv) that a hedge clearing member may process the net daily payment to or from the hedge clearing member only through its firm account or its combined market-makers' or specialists' account. This requirement will eliminate any possibility that a net mark-to-market payment due from a hedge clearing member to OCC (which does not constitute customer funds) will be netted against funds such as premiums being paid to writers of options which are due from OCC to the hedge clearing member's customers' account (and which do constitute customer funds).

Rules 2208 and 2209 (currently Rules 2207 and 2208, respectively) will be rewritten to reflect the changes in the procedures for terminating stock loans that are described above.

Rule 2210(a) [currently Rule 2209(a)] will be rewritten to state that if DTC suspends one of the parties to a stock loan prior to the time at which OCC would have otherwise accepted a stock loan into the hedge program, OCC will not accept the stock loan. The rule also will state that OCC will accept any stock

loan which complies with the completeness and accuracy requirements of Rule 2202(b) even if OCC suspends one of the hedge clearing members which is a party to the stock loan prior to the time at which OCC accepts the stock loan.

Rule 2210(b) [currently Rule 2209(b)] will be rewritten for two purposes: (1) To clarify that OCC contemplates that the buy-in and sell-out procedures described in Rule 2211 (currently rule 2210) generally will be used to close out the stock loan and borrow positions of a suspended clearing member unless OCC determines that another manner of proceeding is more appropriate in the circumstances and (2) to eliminate language that states that proceeds of stock loan and borrow positions carried in market-maker and specialist accounts will be accounted for separately. The reason for these changes is the same as the reason for the changes in Rule 1104 described above. Namely, that stock loan and borrow positions, regardless of the account in which they are carried, are properly characterized as position of the hedge clearing member and not positions of the market-maker or specialist for whom the account is established.

Old Rule 2210(c) [currently rule 2209(c)] will be deleted because OCC has concluded that it would be unlikely ever to match up stock, loan and borrow positions of hedge clearing members that were formerly counter-parties of a suspended clearing member in the manner described in the rule.

The only substantive change in Rule 2221 (currently Rule 2210) will be to eliminate references to the separate treatment of stock loan and borrow positions carried in market-maker and specialist accounts. The reason for eliminating this separate treatment is described above in the discussion of Rule 2210(b).

4. Statutory Basis for the Proposed Rule Change

OCC believes that the proposed rule change provides for the enhancement of the hedge program in a number of ways that should increase the attractiveness of the hedge program to the stock lending community and thereby lead to increased use of the hedge program. Because OCC believes that its hedge program facilitates the prompt and accurate clearance and settlement of stock loans and provides enhanced safeguarding of related securities and funds, OCC believes that the proposed rule change is consistent with the requirements of the Section 17A of the

Act¹¹ and the rules and regulations thereunder. In addition, OCC believes that the hedge program reduces exposure to counterparty default by allowing for the substitution of OCC's AAA credit rating for that of each stock loan counterparty, by using increased payment netting, by reducing duplicative collateralization requirements, and by applying advanced clearing and risk management systems to the stock loan market. OCC therefore believes that the proposed changes are consistent with the purposes and requirements of the Act.

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

OCC does not believe that the proposed rule change would 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, including whether the proposed rule change 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 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-98-03 and should be submitted by June 25, 1998.

For the Commission by the Division of Market Regulations, pursuant to delegated authority.¹²

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40044; File No. SR-PCX-98-24]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Pacific Exchange, Inc. Relating to the Elimination of Suffixes Designating Tier II Equity Securities

May 29, 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 May 11, 1998, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. 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 PCX is proposing to eliminate its current practice of affixing a suffix to the ticker symbol for certain PCX equity securities. This practice is currently performed for the purpose of designating equity securities that are listed pursuant to the Exchange's Tier II requirements.

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

In its filing with the Commission, PCX 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. PCX 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

On July 22, 1994, the Commission approved an Exchange proposal to modify its equity listing and maintenance criteria by adopting a "two-tiered" structure. While the creation of two tiers resulted in a new higher tier (Tier I), the Exchange did not change its existing listing standards (which became Tier II) or otherwise create a lower tier of listing standards. In its approval order, the Commission reiterated a statement from the Exchange's filing regarding Tier II securities (*i.e.*, securities of smaller companies with limited commercial operations, lower capitalization, and a lack of demonstrated earnings history) that:

"Transactions in Tier II [securities] will be identified by a special suffix to the ticker symbol so that these securities can be distinguished from other securities traded on the Exchange. The suffix will not be applied, however, to a security listed on either the NYSE, Amex, or NASDAQ/NMS even though it is designated by the Exchange as a Tier II security." (Exchange Act Release No. 34429 (July 22, 1994), 59 FR 38998, 38999 (August 1, 1994)).

The Exchange currently complies with this requirement by disseminating a ticker symbol with a "TT" suffix for Tier II securities. This is sent to vendors so that they can identify quotes and transactions in Tier II securities. But the Exchange now believes that it would be appropriate and expedient to discontinue this practice and to eliminate the use of the "TT" suffix for Tier II securities for the following reasons:

- Different data vendors are currently using different practices in displaying the Exchange's "TT" suffix. Some display them in reporting quotes and trades. Others include them only in their symbol books, and do not include

¹² 17 CAR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

¹¹ 15 U.S.C. 78q-1.