

Pursuant to the proposed interpretations, once the system malfunction has been corrected and the market quotes have been updated, either the senior person then in charge of the Exchange's Control Room, or the Order Book Official, or the RAES Supervisor may re-start RAES.

Conclusion

CBOE believes that the proposed rule change is consistent with and further the objectives of Section 6(b)(5) of the Act, in that the rules change is designed to perfect the mechanisms of a free and open market and to protect investors and the public interest by enabling the Control Room to turn off RAES to prevent trades based on inaccurate market quotes.

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

CBOE 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

No written comments were solicited or received with respect to the proposed rule change.

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, 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 CBOE. All submissions should refer to file number SR-CBOE-95-06 and should be submitted by March 16, 1995.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-4401 Filed 2-22-95; 8:45 am]

BILLING CODE 8010-01-M

[Release No. 34-35389; File No. SR-NASD-94-78]

Self-Regulatory Organizations; Order Granting Accelerated Approval of a Proposed Rule Change by the National Association of Securities Dealers, Inc., Relating to Exercise Cut-Off Procedures for Expiring Equity Options Contracts

February 16, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² on December 23, 1994, the National Association of Securities Dealers, Inc. ("NASD") submitted to the securities and Exchange Commission ("Commission") a proposed rule change relating to the exercise procedures for expiring equity options contracts. The proposal was published for comment in the **Federal Register** on January 25, 1995.³ No comments were received on the proposed rule change. This order approves the proposed rule change.

Currently, with regard to expiring standardized equity options, Section 63 of the NASD's Uniform Practice Code ("Practice Code") provides that NASD members and their customers are required to indicate their exercise decisions to clearing members no later than 5:30 p.m. (E.S.T.) on the business day immediately prior to the expiration date of the options ("Exercise Cut-Off

Time").⁴ This is the latest time by which an exercise instruction⁵ may be: (1) Prepared by a clearing member for positions in its proprietary trading account; (2) accepted by a clearing member from a non-clearing member; or (3) accepted by a member from any customer.⁶

The only exceptions to the Exercise Cut-Off Times contained in Section 63 of the Practice Code are: (1) To remedy mistakes or errors made in good faith; (2) to take appropriate action as the result of a failure to reconcile an unmatched option transaction; (3) where exceptional circumstances relating to a customer's or member's ability to communicate exercise instructions to a member (or a member's ability to receive such exercise instructions) prior to the Exercise Cut-Off Time warrant such action; and (4) with respect to options contracts in an account maintained for another member in which only positions of customers of such other member are carried. Members are required to prepare a memorandum of every exercise instruction received from a customer stating the time when such instruction was received. In addition, in the event a member receives and acts on an exercise instruction pursuant to one of the exceptions noted above, the member must prepare a memorandum setting forth the circumstances giving rise to the exception. If the member is relying on either the first or the third exception described above, the member must promptly file a copy of the memorandum with the NASD.

Thus, it is presently a violation of Section 63 of the Practice Code for clearing members to accept exercise instructions after the Exercise Cut-Off Time, except in reliance on one of the exceptions noted above. Because

⁴ Generally, the rules of the options exchanges provide that equity options may be traded up until the close of business on the last business day before expiration, which is generally the third Friday of the expiration month ("Expiration Friday"). See, e.g. CBOE Rule 11.1 and Phlx Rule 1042.

⁵ For customers, an exercise instruction is a notice delivered to a member to exercise an option. For a clearing member of The Options Clearing Corporation ("OCC") or a market maker or floor broker on a national options exchange, an exercise instruction is a notice to OCC to exercise an option that would not be automatically exercised pursuant to OCC's exercise-by-exception procedure ("OCC Rule 805"), or not to exercise an option that would otherwise be automatically exercised pursuant to OCC Rule 805. See *infra* note 9. The OCC has separate rules regarding the cut-off time by which exercise notices must be delivered to OCC by OCC clearing members. The proposed rule change does not in any way affect OCC rules.

⁶ In most cases, exercise instructions are electronically transmitted to OCC clearing members through the Clearing Management and Control System ("C/MACS").

² 17 CFR 200.30-3(a)(12) (1994).

¹ 15 U.S.C. 78s(b)(1) (1988).

² 17 CFR 240.19b-4 (1993).

³ See Securities Exchange Act Release No. 35235 (January 18, 1995), 60 FR 4936 (January 25, 1995).

exercise instructions are submitted to the clearing members, without having the audit trail pass directly through the NASD or the particular options exchange(s) trading the expiring option, it is difficult for the NASD to surveil for violations of Section 63. In fact, there have been some situations where members have either delayed making exercise decisions until after the Exercise Cut-Off Time in anticipation of the release of significant news concerning a particular underlying company or, having made exercise decisions prior to the Exercise Cut-Off Time, changed these decisions based upon such news. In one notable situation, certain firms that anticipated the release of material news regarding a particular company allegedly delayed making their exercise decisions until after the Exercise Cut-Off Time, causing firms who claimed to have been disadvantaged by such conduct to commence a series of highly publicized arbitration proceedings and lawsuits.⁷

Accordingly, in order to enable the options exchanges and the NASD to determine whether options holders have made their final exercise decisions no later than the prescribed Exercise Cut-Off Time and not on the basis of market developments occurring after the Exercise Cut-Off Time, the NASD proposes to amend Section 63 of the Practice Code to provide for an exercise advice procedure. Specifically, the proposed rule change will alter the existing exercise instruction procedures by requiring the final exercise decisions also be submitted to the relevant options exchange(s) trading a particular equity option. The clearing members will still be responsible for delivering exercise notices to OCC, however, the proposed rule change will allow the NASD, in conjunction with the options exchanges, to accurately document when each exercise instruction was received by a member or clearing member or delivered by a clearing member to OCC.⁸ The Exercise Cut-Off Time will still be 5:30 p.m. (E.S.T.) on the business day immediately prior to the expiration date.

In particular, under the proposal, there will be two means of exercising an expiring equity option: (1) Take no action and allow exercise determinations to be made in

accordance with OCC Rule 805;⁹ or (2) members may submit a contrary exercise advice (*i.e.*, a notice committing an option holder either to exercise an option that would not otherwise be exercised automatically pursuant to OCC Rule 805, or not to exercise an option that otherwise would be exercised automatically pursuant to OCC Rule 805) ("Contrary Exercise Advice"). A Contrary Exercise Advice will be submitted by NASD members: (1) to a place designated for that purpose by any national options exchange of which they are a member and where the particular equity option is listed; (2) to a place designated for that purpose by any national options exchange that lists and trades that equity option via a member of such exchange if the member is not a member of such exchange; (3) to any national options exchange of which they are a member and where the equity option is listed via OCC in a form prescribed by OCC;¹⁰ or (4) to any national options exchange where the equity option is listed via OCC in a form prescribed by OCC, provided the member is a member of OCC. In those instances where OCC Rule 805 has been waived by OCC,¹¹ the proposal provides that a Contrary Exercise Advice must be submitted prior to the Exercise Cut-Off Time by members wanting to exercise an option that would not have been automatically exercised, or not to exercise an option that would have been automatically exercised, had OCC's exercise-by-exception procedure been in effect.¹² The applicable underlying security price in such instances will be as described in OCC Rule 805(1), which is normally the last sale price in the

⁹ OCC Rule 805 provides for the automatic exercise of in-the-money options at expiration without the submission of an exercise notice to OCC if the price of the security underlying the option is at or above a certain price for calls or at or below a certain price for puts; and the non-exercise of an option at expiration if the price of the security underlying the option does not satisfy such price levels. See OCC Rule 805.

¹⁰ Even through this may be accomplished by submitting exercise decisions directly to the relevant options exchange, the more likely manner of accomplishing this will be to submit the exercise decisions to the options exchanges through C/MACS. The OCC has represented that all necessary systems modifications have been made and fully tested in order for the proposed exercise procedures described herein to be implemented for the next Expiration Friday on February 17, 1995. See Letter from James Young, First Vice President and General Counsel, OCC, to Brad Ritter, Senior Counsel, Office of Market Supervision, Division of Market Regulation, Commission, dated February 13, 1995.

¹¹ This could happen when an underlying security is not traded on its primary market on the trading day immediately preceding an expiration date and, as a result, OCC determines not to fix a closing price for that security. See OCC Rule 805(l).

¹² See *supra* note 9.

primary market for the underlying security.

The proposal also requires that members maintaining proprietary or public customer positions in expiring options take necessary steps to ensure that final exercise decisions are properly indicated to the relevant national options exchange with respect to such positions. In addition, the proposal provides that members who have accepted the responsibility of indicating final exercise decisions on behalf of another member also shall take necessary steps to ensure that such decisions are properly indicated to the relevant national options exchange. In this regard, the proposal also provides that members may establish an internal processing cut-off time prior to 5:30 p.m. (E.S.T.), at which time the member will no longer accept final exercise decisions from its customers in expiring options.

With certain minor modifications,¹³ the proposal maintains the current exceptions to Section 63 of the Practice Code. The proposal, however, does add language to Section 63(b)(3) to expressly state that the burden of establishing an exception to the Exercise Cut-Off Time for a proprietary or customer account of a member rests solely on the member seeking to rely on such exception.

In the event a member does not timely submit a Contrary Exercise Advice pursuant to an exception, the responsible member must prepare a written memorandum describing the circumstances surrounding the late submission of the Contrary Exercise Advice and stating the time when such final exercise decision was made or, in the case of customer, was received. The member must also file a copy of the memorandum with the market surveillance department of the national options exchange trading the option, if it is a member of such exchange, or the NASD's Market Surveillance Department, if it is not a member of such exchange, no later than 12:00 p.m. (E.S.T.) on the business day following that expiration.

Furthermore, in order to highlight the seriousness of violating Section 63 of the Practice Code, the proposed rule language expressly states that submitting or preparing an exercise instruction after the Exercise Cut-Off Time in any expiring equity option on the basis of material information

¹³ Specifically, in order to conform the NASD's proposed rule with the rules of the options exchanges, the NASD proposes to delete the exemption that applies to "option contracts carried in an account maintained for another member in which only positions of customers of such other member are carried."

⁷ See, *e.g.*, *In re Farmers Group Stock Options Litigation*, Master File No. 88-4994 (E.D.Pa.).

⁸ Because OCC's rules are not affected by this rule proposal, the reporting of final exercise decisions as contemplated by the revised rule does not serve to substitute as the effective exercise notice to OCC for the exercise or nonexercise of expiring options.

released after the Exercise Cut-Off Time is activity inconsistent with just and equitable principles of trade. The proposal also states that the requirements specified in Section 63(b) will not apply to standardized foreign currency options or standardized index option products.

The NASD represents that the proposed rule change reflects a coordinated effort among all the options exchanges, the NASD, and OCC. In particular, the NASD represents that the proposed exercise advice procedure has been reviewed and endorsed by the Intermarket Surveillance Group ("ISG"),¹⁴ which has approved the issuance by the options exchanges of a circular explaining the operation of the new exercise cut-off provisions. The NASD notes that the Commission has already approved similar rule proposals from each of the national options exchanges.¹⁵

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 15A(b)(6) of the Act.¹⁶ Specifically, the Commission believes that the NASD's proposal is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to protect investors and the public interest.

Although, as noted by the NASD, all options exchanges currently have a uniform 5:30 p.m. (E.S.T.) Exercise Cut-Off Time on Expiration Fridays for expiring equity options, OCC's rules permit OCC to accept exercise notices

for expiring equity options from clearing firms until 12:00 a.m. (E.S.T.) on the expiration date (*i.e.*, the Saturday after an Expiration Friday). This additional time within which to receive exercise notices from clearing members was provided to accommodate corrections of mistakes made in good faith, trade reconciliations, and certain exceptional circumstances that affected a customer's ability to inform its brokerage firm or affected a firm's ability to receive final exercise decisions before the Exercise Cut-Off Time. Nevertheless, in order to prevent situations such as the one cited by the NASD,¹⁷ the Commission believes that it is appropriate for the Exchange to make it clear in its rules that the submission of a Contrary Exercise Advice on the basis of material information released after the Exercise Cut-Off Time will be activity deemed inconsistent with just and equitable principles of trade.¹⁸

The Commission believes that the proposed exercise procedures should enhance the NASD's ability to surveil for violations of Section 63 of the Practice Code by providing an enhanced audit trail for identifying late exercises. Specifically, every time an exercise decision is made contrary to OCC Rule 805, a Contrary Exercise Advice must be filed as discussed above, in addition to submitting an exercise instruction to a clearing member as is currently required by either the rules of the options exchanges or by exchange clearing members.¹⁹ Similarly, the proposal requires that documentation must be prepared and submitted either to the proper options exchange or to the NASD whenever a late exercise decision is made in reliance on one of the exceptions to Section 63, with the burden of establishing the existence of the exception on the party submitting the Contrary Exercise Advice. The proposed rule change, therefore, should facilitate the Exchange's ability to monitor and enforce compliance with Section 63. Accordingly, because the proposed rule change significantly bolsters the NASD's existing procedures

regarding the exercise of expiring equity options and helps to ensure compliance with their rules, the Commission believes that the proposal is consistent with the Act.²⁰

Even though the proposed rule change significantly improves the NASD's audit trail with respect to late exercises, the Commission believes that the NASD should continue to examine ways of ensuring compliance with the Exercise Cut-Off Time and the other requirements of Section 63.²¹ Furthermore, the Commission also encourages the NASD to review the permitted exceptions to Section 63 and consider ways of establishing parameters as to the extent of the exceptions.²²

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. Specifically, the Commission notes that the proposed rule change is substantively similar to proposals submitted by the national options exchanges and recently approved by the Commission.²³ Additionally, the proposals by the other options exchanges are being implemented in time for the next Expiration Friday on February 17, 1995.²⁴ Accelerated approval of the NASD's proposal is therefore necessary in order to ensure that the options exchanges and their members as well as the NASD and its members are operating under uniform procedures for exercising expiring equity options. Finally, the proposal was noticed for the full 21-day comment period without any comments being received by the Commission. Accordingly, the Commission believes that it is consistent with Section 15A(b)(6) of the Act to approve the proposed rule change on an accelerated basis.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,²⁵ that the

²⁰The Commission notes that the NASD has distributed a notice to member organizations describing the new procedures set forth above and notifying member organizations as to the scheduled implementation of those procedures in time for the next Expiration Friday on February 17, 1995. See NASD Notice to Members 94-102, "New Exercise Advice Procedures for Expiring Equity Options," dated December 23, 1994.

²¹For example, the NASD may wish to consider adopting additional penalties in those situations where a member organization is unable to establish the existence of one of the exceptions to Section 63 of the Practice Code for a particular trade or trades.

²²For example, the NASD may want to define expressly in the rule the circumstances that qualify for a good faith exception.

²³See *supra* note 15.

²⁴See *supra* note 10.

²⁵15 U.S.C. 78s(b)(2). (1982).

¹⁴ISG was formed on July 14, 1983 to, among other things, coordinate more effectively surveillance information sharing arrangements in the stock and options markets. See Intermarket Surveillance Sharing Group Agreement, July 14, 1983. The members of ISG are the American Stock Exchange, Inc., the Boston Stock Exchange, Inc., the Chicago Board Options Exchange, Inc., the Chicago Stock Exchange, Inc., the Cincinnati Stock Exchange, Inc., the NASD, the New York Stock Exchange, Inc., the Pacific Stock Exchange, Inc., and the Philadelphia Stock Exchange, Inc.

¹⁵See Securities Exchange Act Release Nos. 34806 (October 7, 1994), 59 FR 52339 (October 17, 1994) (order approving File No. SR-PHLX-93-37); 34807 (October 7, 1994), 59 FR 52329 (October 17, 1994) (order approving File No. SR-CBOE-94-06); 34808 (October 7, 1994), 59 FR 52324 (October 17, 1994) (order approving File No. SR-AMEX-94-01); 34810 (October 7, 1994), 59 FR 52334 (October 17, 1994) (order approving File No. SR-PSE-94-12); and 34818 (October 11, 1994), 59 FR 52331 (October 17, 1994) (order approving File No. SR-NYSE-94-12).

¹⁶15 U.S.C. 78o(b)(6) (1982).

¹⁷See *supra* note 7.

¹⁸The Commission believes that the Exercise Cut-Off Time serves an important investor protection function. Specifically, the Exercise Cut-Off Time protects holders of short positions in equity options from unanticipated events occurring after the close of the market. As the Commission has previously stated, if expiring equity options were allowed to be exercised after the Exercise Cut-Off Time for reasons other than the exceptions set forth above, the Commission believes that options writers could be unfairly disadvantaged with respect to options holders by not having the same opportunity to react to such unanticipated events. See Securities Exchange Act Release No. 19589 (March 10, 1983), 48 FR 11196 (March 16, 1983).

¹⁹See *supra* note 5.

proposed rule change (File No. SR-NASD-94-78) is hereby approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁶

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-4400 Filed 2-22-95; 8:45 am]

BILLING CODE 8010-01-M

DEPARTMENT OF STATE

Bureau of Political-Military Affairs

[Public Notice 2168]

Policy on Munitions Export Licenses to Ecuador and Peru

AGENCY: Department of State.

ACTION: Public notice.

SUMMARY: Notice is hereby given that all licenses and other approvals to export or otherwise transfer defense articles or defense services to Ecuador or Peru are suspended until further notice pursuant to Sections 38, and 42 of the Arms Export Control Act.

EFFECTIVE DATE: February 9, 1995.

FOR FURTHER INFORMATION CONTACT: Christopher Kavanagh, Office of Export Control Policy, Bureau of Political-Military Affairs, Department of State (202-647-4231).

SUPPLEMENTARY INFORMATION: Effective immediately, it is the policy of the U.S. Government to deny all requests for licenses and other approvals to export or otherwise transfer defense articles and defense services to Ecuador or Peru. In addition, the Department of State has suspended all previously issued licenses and approvals authorizing the export or other transfer of defense articles or defense services to Ecuador or Peru. This action has been taken in response to the continuing conflict on the border between Ecuador and Peru.

The licenses and approvals subject to this policy include manufacturing licenses, technical assistance agreements, technical data, and commercial military exports of any kind involving Ecuador or Peru and which are subject to controls under the Arms Export Control Act. This policy also prohibits the use in connection with Ecuador or Peru of any exemptions from licensing or other approval requirements included in the International Traffic in Arms Regulations (ITAR) (22 CFR Parts 120-130), with the exception of those exemptions specified in Section 126.1(a), unless a specific written

exception is provided by the Office of Defense Trade Controls.

Exceptions to this policy will be made for certain U.S. Munitions List Category XIII(B)(1) items from banking and financial institutions.

This action has been taken pursuant to Sections 38 and 42 of the Arms Export Control Act (22 U.S.C. §§ 2778, 2791) and § 126.7 of the ITAR in furtherance of the foreign policy of the United States.

Dated: February 9, 1995.

Eric D. Newsom,

Acting Assistant Secretary, Bureau of Political-Military Affairs, Department of State.

[FR Doc. 95-4346 Filed 2-22-95; 8:45 am]

BILLING CODE 4710-25-M

DEPARTMENT OF TRANSPORTATION

Coast Guard

[CGD 95-017]

In the Matter of Shanghai Hai Xing Shipping Company: Proposed Assessment of Class II Administrative Penalty

AGENCY: Coast Guard, DOT.

ACTION: Notice of proposed penalty; opportunity to comment.

SUMMARY: The Coast Guard gives notice of and provides an opportunity to comment on the proposed assessment of a Class II administrative penalty to Shanghai Hai Xing Shipping Company for violations of the Federal Water Pollution Control Act (FWPCA). The alleged violations involved the spill of approximately 3,000 gallons of intermediate fuel oil from the M/V AN PING 6 on January 10, 1994 into the Columbia River in the vicinity of Longview, Washington. Interested persons may submit written comments on the proceeding, including comments on the amount of the proposed penalty, or written notice of intent to present evidence at any hearing held in the proceeding. If no hearing is held, an interested person may, within 30 days after issuance of an order, petition to set aside the order and to provide a hearing.

DATES: Comments or notice of intent to present evidence at a hearing must be received not later than March 27, 1995.

ADDRESSES: Comments and requests for a hearing may be mailed to the Hearing Docket Clerk, Office of the Chief Administrative Law Judge, Commandant (G-CJ), U.S. Coast Guard, 2100 Second Street SW., Washington, DC 20593-0001, or may be delivered to

room 6302 at the same address between 8 a.m. and 3 p.m., Monday through Friday, except Federal holidays. Filings should reference docket number 95-0001-CIV. The administrative record for this proceeding is available for inspection at the same address and times.

FOR FURTHER INFORMATION CONTACT:

Mr. George J. Jordan, Judicial Administrator, Office of the Chief Administrative Law Judge, Commandant (G-CJ), U.S. Coast Guard, 2100 Second Street SW., Washington, DC 20593-0001, telephone (202) 267-2940.

SUPPLEMENTARY INFORMATION: Notice of this proceeding is given pursuant to the Federal Water Pollution Control Act (33 U.S.C. 1251 et seq.), as amended by the Oil Pollution Act of 1990. The proceeding is initiated under Section 311(b) of the FWPCA (33 U.S.C. 1321(b)).

This proceeding results from an alleged spill of approximately 3,000 gallons of intermediate fuel oil from the M/V AN PING 6 on January 10, 1994 into the Columbia River in the vicinity of Longview, Washington. Under the Coast Guard's Class II Civil Penalty regulations in 33 CFR Part 20, the Coast Guard publishes notice of the proposed issuance of an order assessing a Class II penalty in the Federal Register (33 CFR § 20.402). A person who wishes to be an interested person must file written comment on the proceeding or written notice of intent to present evidence at any hearing held in the proceeding with the Hearing Docket Clerk not later than March 27, 1995 (33 CFR § 20.404). Interested persons will be given notice of any hearing, a reasonable opportunity to be heard and to present evidence during any hearing, and notice of the decision. Although a hearing is not yet scheduled, the Coast Guard has asked that any hearing be held in Seattle, WA. If no hearing is held, an interested person may, within 30 days after issuance of an order, petition the Commandant of the Coast Guard to set aside the order and to provide a hearing (33 CFR § 20.1102).

The following additional information is provided:

Respondent: Shanghai Hai Xing Shipping Co., 20 Canton Rd., Shanghai, China 200002; M/V AN PING 6 (L8301929)

Complaint Filed: February 2, 1995; Seattle, WA

Docket Number: 95-0001-CIV

Amount of Proposed Penalty: \$120,000

Charges:

Count 1—Improper Discharge of Oil

²⁶ 17 CFR 200.30-3(a)(12) (1994).