

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, 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 at the Commission's Public Reference Section, 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 Phlx. All submissions should refer to SR-Phlx-95-22 and should be submitted by June 6, 1995.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34-35694; File No. SR-PHLX-95-16]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Relating to Modifications of the Position and Exercise Limits for Narrow-Based Index Options

May 9, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on March 6, 1995, 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 self-regulatory organization. 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

Currently, PHLX Rule 1001A, "Position Limits,"¹ establishes the following position limits for industry (or narrow-based) index options (i) 5,500 contracts for an index where a single component stock accounted, on average, for 30% or more of the index value during the 30-day period immediately preceding the review; (ii) 7,500 contracts for an index where a single component stock accounted, on average, for 20% or more of the index value or any five component stocks together accounted, on average, for more than 50% of the index value but no single component stock accounted, on average, for 30% or more of the index value during the 30-day period immediately preceding the review; or (iii) 10,500 contracts where the conditions requiring a limit of 5,500 contracts or 7,500 contracts have not occurred. The PHLX proposes to amend Exchange Rule 1001A(b)(1) and Exchange Rule 1002A, "Exercise Limits,"² to increase the position and exercise limits for industry index options from 5,500, 7,500, or 10,500 contracts to 6,000, 9,000, or 12,000 contracts.

¹ Position limits impose a ceiling on the number of option contracts which an investor or group of investors acting in concert may hold or write in each class of options on the same side of the market (i.e., aggregating long calls and short puts or long puts and short calls).

² Exercise limits prohibit an investor or group of investors acting in concert from exercising more than a specified number of puts or calls in a particular class within five consecutive business days.

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

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

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of 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 self-regulatory organization has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.

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

The PHLX proposes to amend PHLX Rule 1001A to raise the position limits for its narrow-based index options. Specifically, the PHLX proposes to amend PHLX Rule 1001A(b)(1) to establish narrow-based index option position limits of 6,000, 9,000, or 12,000 contracts. In addition, the PHLX proposes to amend PHLX Rule 1002A to establish a corresponding increase in exercise limits for industry index options.

Currently, the PHLX trades options on the following narrow-based indexes:

- (1) Gold/Silver Index ("XAU"): 5,500 contracts
- (2) Utility Index ("UTY"): 10,500 contracts
- (3) PHLX/KBW Bank Index ("KBX"): 10,500 contracts
- (4) Phone Index ("PNX"): 5,500 contracts
- (5) Semiconductor Index ("SOX"): 7,500 contracts
- (6) Airline Sector Index ("PLN"): 10,500 contracts

These position limits, which are standard among all of the options exchanges for narrow-based index options, are based on the degree of concentration of a component stock of the index.³ Currently, under PHLX Rule 1001A, the three-tiered levels of position and exercise limits are 5,500, 7,500, or 10,500 contracts. For the reasons stated below, the PHLX proposes to increase these limits to 6,000, 9,000, or 12,000 contracts.

First, the Exchange notes that the current levels have been in place since

¹⁰ 17 CFR 200.30-3(a)(12).

³ See PHLX Rule 1001A.

1993.⁴ However, there have been no further increases in position limits since 1993, despite substantial changes in the marketplace. Most notable among these changes, according to the PHLX, is an appreciable growth in index options trading. This marked increase in index options volume has significantly increased liquidity in PHLX-traded index options, as open interest has similarly increased.⁵

Second, the Exchange believes that the proposed increases are reasonable. The PHLX states that in prior releases approving increased position limits, the Commission acknowledged that a gradual, evolutionary approach has been adopted by the Commission and the various options exchanges in increasing position and exercise limits. Accordingly, the PHLX proposes a 33% increase in the lowest tier (from 5,000 to 6,000 contracts); a 31% increase for options currently at the 7,500 contract limit; and a 20% increase in the highest tier, which is currently at 10,500 contracts. The Exchange believes that these proposed increases are consistent with the gradual evolution cited by the Commission, because the proposed levels represent reasonable increases which are in line with prior changes.⁶

Third, the Exchange believes that the proposed increases are needed by traders and investors. According to the PHLX, Exchange members and customers have asked the Exchange to propose an increase in position limits. The PHLX states that the requests have focused on the inability of interested trading participants to meet their investment needs at current position limit levels and the deleterious effect this inability is having on these products. Based on such member and customer requests, the Exchange has realized that the current position limit levels discourage market participation by large investors and the institutions that compete to facilitate the trading interests of large investors.

Accordingly, the PHLX proposes to raise position limits to accommodate the liquidity and hedging needs of large investors and the facilitators of those investors. Specifically, certain institutional traders handling industry funds deal in securities valued many

times higher than the maximum permissible position under PHLX rules.

In addition, the Exchange believes that the proposed limit of 6,000, 9,000, and 12,000 contracts should increase the depth and liquidity of the markets for index options. The PHLX also believes that higher position limits would further accommodate the hedging needs of Exchange market makers and specialists, who are also restricted by current levels.

The Exchange has considered the effects of increased position limits on the marketplace, recognizing the purposes of these limits in preventing manipulation and protecting against disruption of the markets for both the option as well as the underlying security. The PHLX notes that it nevertheless continues to monitor the markets for evidence of manipulation or disruption caused by investors with positions at or near current position or exercise limits and that the new limits will not diminish the surveillance function in this regard. Additionally, surveillance procedures have become increasingly sophisticated and automated.

For these reasons, the Exchange believes that the proposal to increase narrow-based index option position limits is consistent with Section 6 of the Act, in general, and, in particular, with Section 6(b)(5), in that it is designed to promote just and equitable principles of trade and to prevent fraudulent and manipulative acts and practices, as well as to protect investors and the public interest. The Exchange believes that the proposal should remove impediments to and perfect the mechanism of a free and open market by providing market opportunity to investors constricted by current position limit levels. The PHLX also believes that by stimulating market participation and thereby increasing option market depth and liquidity, the proposed rule change should promote just and equitable principles of trade. At the same time, the PHLX believes that the proposed position limits should continue to prevent fraudulent and manipulative acts and practices as well as protect investors and the public interest by limiting the ability to disrupt and manipulate the markets for options as well as the underlying securities.

(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 received or requested.

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For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland,
Deputy Secretary.

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⁴ See Securities Exchange Act Release No. 33288 (Dec. 3, 1993), 58 FR 65221 (Dec. 13, 1993) (order approving File No. SR-PHLX-93-07).

⁵ The PHLX states that index options volume increased 450% (from 354,614 contracts to 1,957,171 contracts) in 1994 as compared to 1993.

⁶ According to the PHLX, the most recent position limit changes in 1993 represented changes of 38% (from 4,000 to 5,500 contracts); 25% (from 6,000 to 7,500 contracts); and 31% (from 8,000 to 10,500 contracts).

⁷ 17 CFR 200.30-3(a)(12) (1994).