

that transactions under the exemption be documented as swaps may be satisfied by the use of ISDA master agreements, individually tailored agreements negotiated between specific counterparties that contain terms that are substantially equivalent to those terms contained in the ISDA master agreements, or non-U.S. master agreements developed specifically for documenting transactions effected in foreign domestic markets. Conventional option agreements or conventional forward agreements that are documented using ISDA master agreements or other forms of agreement are not included within the scope of this exemption.

Questions also have arisen regarding the requirement that swap agreements covered by this exemption satisfy the terms of the exemption in the Part 35 Rules. Specifically, questions have arisen whether swap agreements covered by this exemption also must be exempt under the Part 35 Rules. The Commission's intention in requiring that transactions eligible for the exemption satisfy the Part 35 Rules was to ensure that the exemption be available only to swap agreements that meet the terms and conditions set forth in the Part 35 Rules, specifically in Part 35.2 (17 CFR 35.2). Therefore, it is not necessary that swap agreements subject to the exemption also be exempt under the Part 35 Rules; rather, such swap agreements must satisfy the specified criteria set forth in the Part 35 Rules.

### C. Public Interest

The Commission finds that extending the exemption is consistent with the public interest and the protection of investors. When used properly, OTC derivative instruments provide significant benefits to corporations, financial institutions, and institutional investors in managing the risks of their business exposures or financial assets. Derivatives also permit investors to lower their funding costs and, in many instances, can be a cheaper and more liquid way of attaining desired exposure than a position in the cash market. This exemption is intended to reduce or eliminate any legal risk arising from conducting certain OTC derivatives transactions in unregistered broker-dealers, and thus to reduce any financial risk within the securities markets. Legal certainty contributes to the preservation of the financial integrity and stability of OTC derivatives markets.

### D. Effective Date; Future Regulatory Action

The exemption being extended by this order is retroactive and effective as of

June 6, 1934, the date of the enactment of the Exchange Act, and will expire September 30, 1996. The Commission staff will continue its review of the OTC derivatives activities of U.S. broker-dealers and their affiliates, and prior to September 30, 1996, the Commission will consider whether to modify, condition, extend, or withdraw the exemption in whole or in part. Furthermore, this exemption is subject to modification or revocation at any time the Commission determines that such modification or revocation is consistent with the public interest or the protection of investors.<sup>5</sup>

It is therefore ordered, pursuant to Section 15(a)(2) of the Exchange Act, that to the extent brokers or dealers engage in transactions involving individually negotiated, cash-settled OTC options on debt securities or groups or indexes of such securities that (1) are documented as swap agreements, and (2) satisfy the terms of the exemption from regulation under the Commodity Exchange Act adopted by the Commodity Futures Trading Commission, which is set forth at 17 CFR Part 35, to the extent such instruments are securities, such brokers and dealers are exempt from the registration requirements of Section 15(a)(1) of the Exchange Act.

By the Commission.  
Margaret H. McFarland,  
*Deputy Secretary.*  
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<sup>5</sup> The extension of the exemption is intended to avoid any dislocation of existing OTC derivatives markets and to allow those broker-dealers who have not already done so time to move existing business covered by this exemption into entities that do not rely on this exemption. The extension of the exemption is not intended to permit registered broker-dealers conducting transactions in cash-settled OTC options on debt securities to move their activities involving such transactions to unregistered affiliates. The extension of the exemption also is not designed to facilitate the creation of new types of options on debt securities to be written, purchased, or sold by an unregistered broker-dealer, if such instruments are of the type that are written, purchased, or sold by registered broker-dealers or are similar to conventional option contracts. Indeed, were such conduct to occur, the Commission would move quickly to revise or withdraw this order to constrain such conduct prior to September 30, 1996. In this regard, it is the Commission's intent to continue monitoring developments in the OTC derivatives market during the period in which the exemption is effective and to take prompt action to protect investors and maintain fair and orderly markets.

[Release No. 34-36258; File No. SR-NSCC-95-09]

## Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change Relating to a Modification to its Procedures to Allow the Processing of Voluntary Reorganizations with Protect Periods of Three Days or Greater

September 21, 1995.

On July 27, 1995, National Securities Clearing Corporation ("NSCC") filed a proposed rule change (File No. SR-NSCC-95-09) with the Securities and Exchange Commission ("Commission") pursuant to Section 19(b) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposal was published in the Federal Register on August 22, 1995, to solicit comments from interested persons.<sup>2</sup> The Commission did not receive any comments. As discussed below, this order approves the proposed rule change.

### I. Description

The proposed rule change modifies NSCC's Procedures, Section VII.H.4(b), to allow the processing of voluntary reorganizations (*i.e.*, tender or exchange offers) with protect periods<sup>3</sup> of three days or greater through NSCC's Continuous Net Settlement ("CNS") system. Previously, only voluntary reorganizations with protect periods of five days or greater were eligible for NSCC's CNS system. All other voluntary reorganizations with protect periods of four days or less had to be settled on a trade by trade basis through NSCC's balance order system. On June 7, 1995, Rule 15c6-1<sup>4</sup> adopted under the Act became effective requiring that most broker-dealer securities transactions be settled in three business days ("T+3"). Since the implementation of T+3, some voluntary reorganizations have had protect periods of three days rather than five days.

### II. Discussion

The Commission believes that NSCC's proposed rule change is consistent with Section 17A of the Act.<sup>5</sup> Specifically, Section 17A(b)(3)(F)<sup>6</sup> states that the

<sup>1</sup> 15 U.S.C. 78s(b) (1988).

<sup>2</sup> Securities Exchange Act Release No. 36097 (August 11, 1995), 60 FR 43629.

<sup>3</sup> A protect period is generally understood to mean the amount of time after the expiration of a tender or exchange offer that the owner or record holder that has elected to participate in the offer has to submit the shares to the tender agent.

<sup>4</sup> 17 CFR 240.15c6-1 (1994).

<sup>5</sup> 15 U.S.C. 78q-1 (1988).

<sup>6</sup> 15 U.S.C. 78q-1(b)(3)(F) (1988).

rules of a clearing agency must be designed to promote the prompt and accurate clearance and settlement of securities transactions.

Currently, if an entity making a tender or exchange offer wants a protect period of three days, the entire reorganization must be settled on a trade-by-trade basis. By including these transactions within the CNS system, the rule change enhances the settlement procedure for such trades. Thus, the rule promotes the prompt and accurate clearance and settlement of securities transactions. Further, by including reorganizations with protect periods of three days within the CNS system, the proposed rule change may encourage the use of three day protect periods.<sup>7</sup> By limiting the time the tender or exchange offer remains unsettled, the goal of risk reduction contemplated by Rule 15c6-1 is furthered.

### III. Conclusion

For the reasons stated above, the Commission finds that NSCC's proposal is consistent with Section 17A of the Act.<sup>8</sup>

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>9</sup> that the proposed rule change (File No. SR-NSCC-95-09) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

Margaret H. McFarland,  
Deputy Secretary.

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[Release No. 34-36271; File No. SR-Phlx-95-66]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Philadelphia Stock Exchange, Inc. Relating to P/A Orders

September 22, 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 September 15, 1995, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange

<sup>7</sup> Buyers sometimes purchase securities on the last day of a tender offer and tender their shares that day. Such purchasers can not deliver the securities until their purchase transactions settle. Before the implementation of T+3, a three day protect period was not practical because purchasers would not receive their securities until the fifth business day after the trade date.

<sup>8</sup> 15 U.S.C. 78q-1 (1988).

<sup>9</sup> 15 U.S.C. 78s(b)(2) (1988).

<sup>10</sup> 17 CFR 200.30(a)(12) (1994).

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

The Phlx is proposing to amend: (i) Phlx Rule 1066<sup>1</sup> by adding new paragraph (h), P/A Orders (Principal Acting as Agent); and (ii) Phlx Rule 1015<sup>2</sup> by adding new paragraph (c). Below is the text of the proposed rule change. Proposed new language is in italics.

#### Options Rules

\* \* \* \* \*

#### Certain Types of Orders Defined

##### Rule 1066

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(h) *P/A Order ("Principal Acting as Agent")—A P/A order is an order received on the Exchange in the name ("give-up") of a registered floor trader on another national options exchange (i.e., an "N" account type) sent while that floor trader is holding a similar customer order in that same option series for the account of a public customer for which price improvement is sought on the basis that the PHLX is displaying a superior bid or offer.*

\* \* \* \* \*

#### Quotation Guarantees

##### Rule 1015

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(c) *P/A Orders—the P/A order type shall only exist with respect to those multiply traded equity options for which the originating options exchange affords reciprocal P/A treatment. P/A orders received on the PHLX must be provided with the customer volume guarantees of Rules 1015 and 1033, if the PHLX specialist agreement to accept P/A orders is reciprocated by the sending floor trader in the same option on another national options exchange. P/A orders may not be for more than the number of contracts on the customer's order and must be market or marketable limit orders. An order does not qualify as a P/A order if the customer's order on the other exchange was given an*

<sup>1</sup> Philadelphia Stock Exchange Guide, Options Rules, Rule 1066 (CCH) ¶3066.

<sup>2</sup> Philadelphia Stock Exchange Guide, Options Rules, Rule 1015 (CCH) ¶3015.

*execution prior to the time the P/A order is sent on its behalf.*

\* \* \* \* \*

#### 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 Phlx included statements concerning the purpose of and basis for the proposed rule change and discussed any comments if received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Phlx has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

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

The purpose of the proposed rule change is to create a new equity options order designator, the P/A order, to ensure that when a floor trader (i.e., Specialist, market maker, Registered Options Trader, Lead Market Maker or Designated Primary Market Maker) from another options exchange in possession of a public customer order sends a mirror-image order<sup>3</sup> to the Phlx to obtain price improvement for that customer, the customer will receive the benefit of that better execution price, notwithstanding that the mirror-image order has been sent in the name of floor trader. Similarly, the P/A order is intended to ensure that when a Phlx floor trader sends such an order to another options exchange, the customer for whom the Phlx order is sent receives the benefit of the better price available on that exchange.

The proposed rule change recognizes that orders received on national options exchanges in the name of public customers are provided firm quotes and volume guarantees not available to orders received in the name of broker-dealers. These volume guarantees are not insignificant, established by rule as a minimum of ten contracts and are frequently much higher.

Because orders emanating from the floor of one exchange and sent to another in multiply-listed options normally are sent in the name of the floor trader, they are often deprived of the opportunity to receive such guarantees. For example, a customer buy order may be "stopped" by a floor trader on the receiving exchange at that

<sup>3</sup> A mirror-image order is an order sent by the floor trader for the exact number of contracts specified in the customer order.