

customer's account is approved for BOUNDS trading.

As discussed above, the Exchanges propose to have BOUNDS issued, cleared and settled by OCC. In this regard, on December 27, 1995, OCC filed with the Commission a proposed rule change to enable it to issue, clear, and settle BOUNDS.<sup>36</sup> The OCC proposal, when approved, should allow OCC to process BOUNDS transactions in accordance with procedures that are substantially similar to its existing well-established systems and procedures for the clearance and settlement of exchange-traded options.<sup>37</sup> In this respect, the Commission notes that the initiation of trading of BOUNDS is conditioned upon Commission approval of OCC's proposal to issue, clear and settle BOUNDS, as well as a Commission order approving the BOUNDS ODD supplement.

The Commission finds good cause for approving the Amendments to the proposed rule changes prior to the thirtieth day after the date of publication of notice of filing thereof in the Federal Register.<sup>38</sup> The Commission notes that the Amendments bring the BOUNDS margin rules applicable to spread positions into conformity with the margin treatment currently applicable to other standardized options. Furthermore, the Amendments also bring the Exchanges' rules into conformity with those of OCC which, the Commission notes, reduces the potential for conflict between an Exchanges' and OCC's rules.<sup>39</sup> Also, the Commission believes it is appropriate for Amex and CBOE to not apply their "ten-up" rules to BOUNDS transactions (*i.e.*, the minimum size guarantee for BOUNDS quotes). In the absence of trading experience or other indication of adequate market liquidity, the Commission believes it is reasonable for the Amex and CBOE to determine that specialists or market makers should not be required to make ten-up markets for transactions in BOUNDS. The Amendments also eliminate the use of escrow receipts and letters of guarantee

as adequate margin cover for BOUNDS. The Commission notes that because it is unknown whether BOUNDS will be settled in cash of the underlying stock until expiration of the BOUNDS position, this raises issues as to whether such instruments serve as adequate cover for short BOUNDS positions. Accordingly, the Commission believes this issue is better addressed in the context of a separate OCC filing. Finally, the Commission notes that PSE's designation of BOUNDS as a Tier I security is consistent with the treatment afforded standardized equity options and, therefore, does not raise any new or unique issues. Accordingly, the Commission believes it is consistent with Sections 6(b)(5) and 19(b)(2) of the Act to approve the Amendment on an accelerated basis.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the Amendments. 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. Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organization. All submissions should refer to the file numbers in the caption above and should be submitted by February 13, 1996.

Based upon the aforementioned factors, the Commission finds that the proposed rule changes relating to the listing and trading of BOUNDS are consistent with the requirements of Section 6(b)(5) and the rules and regulations thereunder. The initiation of BOUNDS trading, however, is conditioned upon the issuance of an order approving the OCC's proposed rule change to issue, clear, and settle BOUNDS and also upon the Commission's review and approval of an ODD BOUNDS supplement, pursuant to Rule 9b-1 of the Act.

It therefore is ordered, pursuant to Section 19(b)(2) of the Act,<sup>40</sup> that the proposed rule changes (SR-Amex-94-56, SR-CBOE-05-14, and SR-PSE-95-01) are approved, as amended.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>41</sup>

Margaret H. McFarland,

*Deputy Secretary.*

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[Release No. 34-36715; File No. SR-Amex-95-53]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the American Stock Exchange, Inc. Relating to Options on the Morgan Stanley Healthcare Product Companies Index, the Morgan Stanley Healthcare Providers Index and the Morgan Stanley Healthcare Payors Index

January 16, 1996.

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 December 19, 1995, the American Stock Exchange, Inc. ("Amex" or "Exchange") 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 by the Amex. On January 2, 1996, the Amex filed Amendment No. 1 to its proposal.<sup>1</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The Exchange proposes to approve for listing and trading options on three new indexes developed by Morgan Stanley & Co. Incorporated ("Morgan Stanley") relating to three different subsectors within the healthcare sector: the Morgan Stanley Healthcare Providers Index ("Providers Index"); the Morgan Stanley

<sup>40</sup> 15 U.S.C. § 78s(b)(2) (1988).

<sup>41</sup> 17 CFR 200.30-3(a)(12) (1994).

<sup>1</sup> In Amendment No. 1, the Amex states that for each of the healthcare sector indexes, if at any time between annual rebalancings, the top five stocks in an Index by weight represent in the aggregate more than 60% of the Index's value, the Exchange will rebalance the Index after the close of trading on Expiration Friday in the next month in the March cycle. See Letter from Claire P. McGrath, Managing Director and Special Counsel, Derivatives Securities, Amex, to Michael Walinskas, Branch Chief, Office of Market Supervision, Division of Market Regulation, Commission, dated January 2, 1996 ("Amendment No. 1").

<sup>36</sup> See SR-OCC-95-20.

<sup>37</sup> The Commission has not yet approved OCC's proposed rule filing to issue, clear, and settle BOUNDS (SR-OCC-95-20).

<sup>38</sup> Amex Amendment No. 1 was noticed and published for comment with the original filing. The Commission, therefore, is not seeking comment on Amex Amendment No. 1.

<sup>39</sup> For example, one of the changes alters the timing of the payment of the BOUNDS dividends equivalent. The Commission notes that this change, which brings the Exchanges' rules into conformity with the rules of OCC, will harmonize the payment date for BOUNDS with that of the underlying stock, and that this should make trading strategies involving both the BOUNDS and underlying stock more efficient.

Healthcare Payors Index ("Payors Index"); and the Morgan Stanley Healthcare Product Companies Index ("Product Companies Index") (collectively the "Indexes"). Each Index is comprised of stocks which are traded on the Amex, the New York Stock Exchange ("NYSE"), or are National Market securities traded through the facilities of the National Association of Securities Dealers Automated Quotation system ("NASDAQ"). In addition, the Amex proposes to amend Rule 902C(d) to include the Indexes in the disclaimer provisions of the rule.

The text of the proposed rule change is available at the Office of the Secretary, the Amex, 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 Exchange 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 Amex 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

The Amex proposes to trade standardized index options on the Indexes. The Indexes are equal-dollar weighted indexes developed by Morgan Stanley, each representing a portfolio of large, actively traded stocks.<sup>2</sup>

<sup>2</sup> As of December 1, 1995, the Providers Index was comprised of 15 stocks of companies engaged in the hospital management and medical/nursing services industries, with market capitalizations ranging from \$494 million to \$23 billion, and six month average daily trading volumes ranging from 95,000 to 995,000 shares. The Payor's Index, as of December 1, 1995, was comprised of 12 stocks of companies conducting business in the managed health care and health industry services industries, with market capitalizations ranging from \$622 million to \$10 billion and six month average daily trading volumes ranging from 170,000 to 1,700,000 shares. Finally, as of this same date, the Product Companies Index was comprised of 25 equity issues of companies engaged in the major pharmaceuticals, biotechnology, medical specialties, medical electronics, and medical/dental distributors industries. The market capitalizations of these 25 companies range from \$1.6 billion to \$56.1 billion and the six month average daily trading volumes range from 124,000 to 2,800,000 shares.

#### (a) Eligibility Standards for Index Components

The Amex represents that the Indexes conform with Exchange Rule 901C which specifies criteria for inclusion of stocks in an index on which standardized options will be traded. In addition, for each of the Indexes, Morgan Stanley will include in the Index only those stocks that meet the following standards: (1) A minimum price of \$7.50 at the time of announcement of entry into the Index; (2) a minimum market capitalization of \$75 million; (3) average monthly trading volume in the component security of at least one million shares during the preceding six months; (4) each component security must be traded on the Amex, NYSE or must be a National Market Security traded through the facilities of NASDAQ; and (5) upon annual rebalancing, at least 90% of the Index numerical value and at least 80% of the total number of component securities must meet the then current criteria for standardized option trading set forth in Exchange Rule 915. Also, because the Indexes are equal-dollar weighted, no component security will represent more than 25% of the weight of any of the Indexes, nor will the five highest weighted component securities in any of the Indexes, in the aggregate, account for more than 60% of the weight of that Index upon annual rebalancing. The criteria set forth above are the same as or exceed many of the criteria established for the expedited listing of options on stock industry indexes pursuant to Exchange Rule 901C Commentary .02.

#### (b) Index Calculation

The Indexes are calculated using an "equal-dollar weighting" methodology designed to ensure that each of the component securities is represented in an approximately "equal" dollar amount in each Index. The following is a description of how the equal-dollar weighting calculation method works. As of the market close on December 16, 1994, a portfolio of stocks was established for each of the Indexes representing an investment of \$300,000 in the stock (rounded to the nearest whole share) of each of the companies in each Index. The value of each Index equals the current market value (*i.e.*, based on U.S. primary market prices) of the sum of the assigned number of shares of each of the stocks in the Index portfolio divided by the Index divisor. The Index divisors were initially determined for each Index to yield benchmark values of 200.00 at the close of trading on December 16, 1994.

Annually thereafter, following the close of trading on the third Friday of December, each Index portfolio will be adjusted by changing the number of whole shares of each component stock in that Index so that each company is again represented in "equal" dollar amounts. If necessary, a divisor adjustment is made at the rebalancing to ensure continuity of the Index's value. The newly adjusted portfolio becomes the basis for the Index's value on the first trading day following the annual adjustment.

As noted above, for each Index the number of shares of each component stock in the Index portfolio remains fixed between annual reviews except in the event of certain types of corporate actions such as the payment of a dividend other than an ordinary cash dividend, stock distribution, stock split, reverse stock split, rights offering, distribution, reorganization, recapitalization, or similar event with respect to the component stocks. In a merger or consolidation of an issuer of a component stock, if the stock remains in the Index, the number of shares of that security in the portfolio will be adjusted, if necessary, to the nearest whole share, to maintain the component's relative weight in the Index at the level immediately prior to the corporate action. In the event of a stock replacement, the dollar value of the security being replaced will be calculated and that amount invested in the stock of the new component, to the nearest whole share. In all cases, the divisor will be adjusted, if necessary, to ensure Index continuity.

Additionally, for each of the Indexes, if at any time between annual rebalancings, the top five stocks in the Index by weight represent in the aggregate more than 60% of the Index's value, the Exchange will rebalance the Index after the close of trading on expiration Friday in the next month in the March cycle. For example, if in July it is determined that the top five components in the Morgan Stanley Healthcare Product Companies Index account for more than 60% of the Index's weight, then the Index will be rebalanced after the close of trading on expiration Friday in September.<sup>3</sup>

Similar to other stock index values published by the Exchange, the value of each Index will be calculated continuously and disseminated every 15 seconds over the Consolidated Tape Association's Network B.

<sup>3</sup> See Amendment No. 1, *supra* note 1.

## (c) Maintenance of the Indexes

The Indexes will be calculated and maintained by the Amex in consultation with Morgan Stanley who may, from time to time, suggest changes in the industry categories represented in any or all of the Indexes or changes in the number of component stocks in an industry category to properly reflect the changing conditions in the healthcare sector. In addition, the Amex will replace component securities in each Index that fails to meet the following maintenance criteria on quarterly review: (1) A minimum market capitalization of \$75 million; (2) average monthly trading volume in the component security of at least 500,000 shares during the preceding six months; (3) at least 90% of the Index's numerical value and at least 80% of the total number of component securities meet the then current criteria for standardized option trading set forth in Exchange Rule 915; and (4) a share price of \$5.00 or greater for a majority of business days during the three calendar months preceding the date of selection for inclusion in the Index.

At the beginning of each calendar quarter, Morgan Stanley will provide the Amex with a current list of replacement stocks for each Index on which to draw in the event that a component in an Index must be replaced due to merger, takeover or other similar event. The Exchange will make these lists publicly available. Stocks in the replacement lists will be selected and ranked by Morgan Stanley based on a number of criteria, including conformity to the eligibility standards described above and to Exchange Rules 915 and 916 which set forth the criteria for the initial and continued listing of standardized options of equity securities, trading liquidity, market capitalization, ability to borrow shares and share price. The replacement stocks will be categorized by industry within each healthcare subsector and ranked within their category based on the aforementioned criteria. The replacement stock for a security leaving the Index will be selected by the Amex from the replacement list based on industry category and liquidity. In the event no replacement stocks are available that meet the eligibility criteria and pass Morgan Stanley's selection process, then the security leaving the Index will be removed without replacement and the divisor adjusted to ensure Index continuity. It is expected that each Index will remain at the current number of components; however, if the number of components in an Index shall increase or decrease by

more than one third, the Exchange must obtain prior approval for such index from the Commission pursuant to Section 19(b) of the Act.

In addition, Morgan Stanley will advise the Exchange regarding the handling of unusual corporate actions which may arise from time to time. Routine corporate actions (e.g., stock splits, routine spin-offs, etc.) which require straightforward index divisor adjustments will be handled by Exchange staff without consultation with Morgan Stanley. All stock replacements and unusual divisor adjustments caused by the occurrence of extraordinary events such as dissolution, merger, bankruptcy, non-routine spin-offs or extraordinary dividends will be made by Exchange staff in consultation with Morgan Stanley. All stock replacements and the handling of non-routine corporate actions will be announced at least ten business days in advance of such effective change, whenever practicable. As with all options currently trading on the Amex, the Exchange will make this information available to the public through dissemination of an information circular.

## (d) Expiration and Settlement

The proposed options on the Indexes will be European style (*i.e.*, exercisable only at expiration), and cash settled. Standard option trading hours (9:30 a.m. to 4:10 p.m. New York time) will apply. The options on the Index will expire on the Saturday following the third Friday of the expiration month ("Expiration Friday"). The last trading day in an expiring option series will normally be the second to last business day preceding the Saturday following the third Friday of the expiration month (normally a Thursday). Trading in expiring options will cease at the close of trading on the last trading day.

For each Index, the Exchange plans to list option series with expirations in the three near-term calendar months and in the two additional calendar months in the March cycle. In addition, longer term option series having up to thirty-six months to expiration may be traded. In lieu of such long-term options on a full value Index level, the Exchange may instead list long-term, reduced value put and call options based on one-tenth (1/10th) the Index's full value. In either event, the interval between expiration months for either a full value or reduced value long-term options will not be less than six months. The trading of any long term options would be subject to the same rules which govern the trading of all the Exchange's index options, including sales practice rules, margin

requirements and floor trading procedures and all options will have European style exercise. Position limits on reduced value long term Index options will be equivalent to the position limits for regular (full value) Index options and would be aggregated with such options (for example, if the position limit for the full value options is 12,000 contracts on the same side of the market, then the position limit for the reduced value options will be 120,000 contracts on the same side of the market).

For each Index, the exercise settlement value for all of the Index's expiring options will be calculated based upon the primary exchange regular way opening sale prices for the component stocks. In the case of securities traded through the NASDAQ system, the first reported regular way sale price will be used. If any component stock does not open for trading on its primary market on the last trading day before expiration, then the prior day's last sale price will be used in the calculation.

## (e) Exchange Rules Applicable to Stock Index Options

Amex Rules 900C through 980C will apply to the trading of option contracts based on the Indexes. These Rules cover issues such as surveillance, exercise prices, and position limits. Surveillance procedures currently used to monitor trading in each of the Exchange's other index options will also be used to monitor trading in options on the Indexes. The Indexes are deemed to be Stock Index Options under Rule 901C(a) and Stock Index Industry Groups under Rule 900C(b)(1). With respect to Rule 903C(b), the Exchange proposes to list near-the-money (*i.e.* strike prices within ten points above or below the current index value) option series on an Index at 2½ point strike price intervals when the value of that Index is below 200 points. In addition, the Exchange expects that the review required by Rule 904C(c) will result in position limits of 12,000 contracts with respect to options on each of the Indexes.

## 2. Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act, in general, and furthers the objectives of Section 6(b)(5) in particular, in that it 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 remove impediments to and perfect the

mechanism of a free and open market and a national market system.

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

The Amex 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 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, 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. Copies of such filing will also be available for inspection and copying at the principal office of the Amex. All submissions should refer to File No. SR-Amex-95-53 and should be submitted by February 13, 1996.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>4</sup>

Margaret H. McFarland,  
*Deputy Secretary.*

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[Release No. 34-36721; File No. SR-Amex-95-58]

#### **Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the American Stock Exchange, Inc., Relating to Listing and Trading of Warrants Based on the Undervalued Market Basket**

January 16, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 2, 1996, the American Stock Exchange, Inc. ("Amex" or "Exchange") 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 by the Amex. 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 Amex, pursuant to Rule 19b-4 of the Act, proposes to approve for listing and trading, under Section 106 of the Amex *Company Guide*, index warrants based on the undervalued market basket index ("Index"). The Index is an equal-dollar weighted broad-based index developed by the Exchange and is comprised of stocks which are traded on the Amex, the New York Stock Exchange, Inc. ("NYSE"), or through the facilities of the National Association of Securities Dealers Automated Quotation system and are reported national market system securities ("NASDAQ/NMS").

The text of the proposed rule change is available at the Office of the Secretary, the Amex, and 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 Amex 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 Amex 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

Under Section 106 of the Amex *Company Guide*, the Exchange may approve for listing index warrants based on foreign and domestic market indices. While the Exchange currently lists and trades warrants on a number of foreign market indices, it currently proposes to list and trade warrants on a domestic market index. The listing and trading of warrants on the undervalued market basket index will comply in all respects with Exchange Rules 1100 through 1110 for the trading of stock index and currency warrants.

Warrant issues on the Index will conform to the listing guidelines under Section 106, which provide, among other things, that: (1) the issuer shall have tangible net worth in excess of \$250,000,000 and otherwise substantially exceed size and earnings requirements in Section 101(A) of the *Company Guide* or meet the alternate guideline in paragraph (a); (2) the term of the warrants shall be for a period ranging from one to three years from the date of issuance; and (3) the minimum public distribution of such issues shall be 1,000,000 warrants, together with a minimum of 400 public holders, and have an aggregate market value of \$4,000,000.

Index warrants will be direct obligations of their issuer subject to cash-settlement during their term, and either exercisable throughout their life (*i.e.*, American style) or exercisable only on their expiration date (*i.e.*, European style). Upon exercise, or at the warrant expiration date (if not exercisable prior to such date), the holder of a warrant structured as a "put" would receive payment in U.S. dollars to the extent that the Index has declined below a pre-stated cash settlement value. Conversely, holders of a warrant structured as a "call" would, upon exercise or at expiration, receive payment in U.S. dollars to the extent that the Index has increased above the pre-stated cash settlement value. If "out-of-the-money" at the time of expiration, the warrants would expire worthless. In addition, the Amex, prior to the

<sup>4</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> 17 CFR 240.19b-4 (1994).