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For the Commission, by the Division of Investment Management, pursuant to delegated authority.

Margaret H. McFarland,  
Deputy Secretary.

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[Release No. 34-37988; File No. SR-CBOE-96-71]

**Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Incorporated Relating to the Closing Time for Equity and Narrow-Based Index Options**

November 26, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on November 20, 1996, the Chicago Board Options Exchange, Incorporated ("CBOE" 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 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 Exchange proposes to amend its rules governing the hours of trading in equity options and narrow-based index options. After the change, the Exchange will close trading in equity and narrow-based index options at 3:02 p.m. (Chicago time) instead of at 3:10 p.m. (Chicago time), as is the case now. The text of the proposed rule change is available at the Office of the Secretary, CBOE 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**

**1. Purpose**

The purpose of the proposed rule change is to change the close of the normal trading hours in equity and narrow-based index options from 3:10 p.m. (Chicago time) to 3:02 p.m. (Chicago time). After the change, the time of the close of trading in these CBOE options will more closely correspond to the normal time set for the close of trading on the primary exchanges listing the stocks underlying the CBOE options. The primary exchanges generally close at 3:00 p.m. (Chicago time).

When the Exchange determined to change its closing time for equity options and narrow-based index options, it determined that there were still reasons to continue trading options for some period of time after the close of trading of the primary markets for the underlying securities. Specifically, the extended period allows options traders to respond to late reports of closing prices over the consolidated tape. If the price of a late reported trade on an underlying security was substantially different from the previous reported price, the extended trading session would give options traders the opportunity to bring options quotes into line with the closing price of the underlying security. However, because of improvements in the processing and reporting of transactions, there are usually no significant delays in the reporting of closing prices. Therefore, a ten minute session is no longer needed to trade options after the underlying securities close trading.

The Exchange believes the need to continue trading options for some period of time after the close of trading on the primary markets for the underlying securities outweighs the obvious problems with continuing to trade options while stocks are longer traded. The Exchange has learned through experience with a 3:10 close that pricing aberrations can occur if an option is traded when the underlying stock is no longer trading. There is

obviously a close relationship in the price of the underlying stock and the overlying option. As a result, it is difficult for the market to price options accurately when the underlying security is not trading. It is for this reason that the halt of trading in an underlying security is a factor to be considered in determining whether to halt trading in the overlying option under CBOE Rule 6.3.

In recent weeks, the Exchange has become particularly cognizant of the pricing problems that result when the Exchange remains open after the close of the primary exchange for the underlying stocks. A number of issuers have adopted the practice of disseminating important corporate news after the close of trading on the primary exchange. Issuers often wait until after 3:00 p.m. Chicago time to release the news because they realize that the news might have a short-term disruptive effect on the market price of the stock that can be minimized if investors are able to digest the significance of the news after the markets have closed and overnight. However, despite efforts of the Exchange to remind issuers that most Exchange products trade until 3:10 p.m., important corporate news is often disseminated between 3:00 p.m. and 3:10 p.m. As a result, the Exchange is often deluged with option orders after a significant news announcement after 3:00 p.m., most often between 3:02 p.m. and 3:10 p.m. These orders have a disruptive effect on the market at a time when the Exchange is attempting to close in a fair and orderly fashion.<sup>3</sup> Among the possible deleterious effects is that customer orders might not be filled as quickly as they might otherwise be filled in more normal conditions. In addition, orders regularly are routed through the Exchange's Retail Automatic Execution System ("RAES") and are executed in rapid succession on markets that have not had a chance to be updated to reflect the significant news.<sup>4</sup> Weighing the benefits to be

<sup>3</sup> Although the Exchange has the ability to call a "fast" market under current Exchange Rule 6.6 in an effort to deal with the problems caused by news announcements after 3:00 p.m., this procedure requires the assessment of the situation by two Floor Officials. As a result, the Rule 6.6 procedure does not permit the Exchange to act quickly enough to prevent the possible deleterious effects of an unexpected news announcement.

<sup>4</sup> Orders routed through the RAES system are assigned execution prices instantaneously as determined by the prevailing market quotes that exist at the time of the order's entry into the system. As a result, these orders might be assigned a price before the market-makers will have had the chance to update the quotes based upon the unexpected news announcement. To respond to the problem presented when issuers make significant news

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<sup>1</sup> 15 U.S.C. § 78s(b)(1).

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

obtained by a brief extended trading session against the difficulties presented when options trade after the underlying securities have closed, the Exchange has determined that a two minute extended session is the correct balance.

The Exchange also proposes to change the closing time for narrow-based indexes under Rule 24.6 because these indexes are subject to the same pricing problems as options on individual stocks. A significant news announcement on one component of a narrow-based index could have a significant effect on that index. The Exchange is not at this time proposing to change the closing time of 3:15 p.m. for broad-based index options because it is unlikely that a significant news announcement by the issuer of one component stock of a broad-based index is likely to have a significant effect on the price of that broad-based index.

The Exchange is also proposing to amend Interpretations .02 and .03 of its trading rotation rule, Rule 6.2, to reflect the changes in the closing time for stock options and narrow-based index options from 3:10 p.m. to 3:02 p.m. Chicago time. A change would also be made to allow a closing rotation in non-expiring options to be held five minutes after news of such rotation is disseminated. Currently, the rule requires notice of ten minutes before a closing rotation may be held.

Finally, the Exchange is proposing to amend Interpretation .01 to Rule 6.1 to make it clear that the Board may designate a person or persons to change the hours for the trading of options when unusual conditions exist. This change is consistent with the Exchange's current Rule 24.6.

## 2. Statutory Basis

The proposed rule changes further the objectives of Section 6(b)(5) of the Act, in that they are designed to promote just and equitable principles of trade, 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 Exchange states that it believes that the proposed rule change will impose no burden on competition.

announcements during the ten minute period after the close of trading in stocks, the Exchange filed a rule with the Commission which permits the Exchange to employ a system to suspend the operation of the RAES system in the event of news announcements near the close of trading. See Securities Exchange Act Release No. 37885 (October 29, 1996), 61 FR 56724 (approving CBOE-96-55).

### *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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Exchange. All submissions should refer to File No. SR-CBOE-96-71 and should be submitted by December 26, 1996.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>5</sup>

Margaret H. McFarland,

*Deputy Secretary.*

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<sup>5</sup> 17 CFR 200.30-3(a)(12).

[Release No. 34-37985; File No. SR-OCC-96-16]

### **Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Order Granting Permanent Approval on an Accelerated Basis of a Proposed Rule Change Concerning Equity TIMS**

November 25, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on November 8, 1996, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared primarily by OCC. The Commission is publishing this notice and order to solicit comments from interested persons and to grant permanent approval of the proposed rule change on an accelerated basis.

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

The proposed rule change seeks permanent approval of OCC's use of its Theoretical Intermarket Margin System ("TIMS") for calculating clearing margin positions in equity options.<sup>2</sup> Since its initial temporary approval of Equity TIMS in 1991, the Commission has extended the temporary approval five times.<sup>3</sup>

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

<sup>2</sup> Equity TIMS is a modified version of OCC's Non-Equity TIMS, which is OCC's margin system used to calculate requirements on options for which the underlying asset is anything but an equity security. Securities Exchange Act Release No. 23167 (April 22, 1986), 51 FR 16127 [File No. SR-OCC-85-21] (order approving Non-Equity TIMS). On March 1, 1991, the Commission temporarily approved a proposed rule change that authorized OCC to use TIMS to calculate clearing member margin requirements on equity options. At that time, OCC phased out its previous margin system, known as the "production system," and since then has used Equity TIMS to calculate its clearing members' margin requirements on equity option positions. For a complete description of Equity TIMS, refer to Securities Exchange Act Release No. 28928 (March 1, 1991), 56 FR 9995 [File No. SR-OCC-89-12] (order approving the use of Equity TIMS to calculate margin on equity options on a temporary basis through May 31, 1992).

<sup>3</sup> Securities Exchange Act Release Nos. 30761 (May 29, 1992), 57 FR 24286 [File No. SR-OCC-92-15] (order extending the approval of Equity TIMS through May 31, 1993); 32388 (May 28, 1993), 58 FR 31989 [File No. SR-OCC-93-06] (order extending the approval of Equity TIMS through May 31, 1994); 34065 (May 13, 1994), 59 FR 26534 [File No. SR-OCC-94-03] (order extending the approval of Equity TIMS through May 31, 1995); 36003 (July 21, 1995), 60 FR 38880 [File No. SR-OCC-95-07] (order extending the approval of Equity TIMS through May 31, 1996) and 37449 (July 17, 1996), 61 FR 38498 [File No. SR-OCC-96-06] (order extending the approval of Equity TIMS through November 30, 1996).