

member aggrieved by an Exchange Official's ruling could then appeal the Exchange Official's ruling to a Floor Governor. The third appeal would be to a three-Governor panel. The proposed appeal process thus provides three levels of prompt review of a Floor Official's ruling. The Exchange believes that the several levels of review would assure that Floor Officials' decisions are fair and impartial as well as prompt.

There would be a slightly different appeal process for the limited number of situations where a Floor Official and a Senior Floor Official must rule together.¹⁹ In these situations, the appeal would go directly to a three Governor panel since a Senior Floor Official either is a Floor Governor or is the equivalent of a Floor Governor in his or her authority to make rulings.

The proposed rule change, as amended, would eliminate the right of appeal to the Board which the Exchange believes only facilitates pointless appeals due to the time required to convene the Amex Adjudicatory Council to review matters.²⁰ The proposed rule change, as amended, however, would leave unchanged any right that a member or its customer may have to submit a market dispute to arbitration. The rule filing does not seek in any way to define the matters that may be brought to arbitration, and the arbitrability of claims would remain a matter to be determined by arbitrators or the courts.

2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is consistent with Section 6(b) of the Act²¹ in general, and furthers the objectives of Section 6(b)(5) of the Act²² in particular, in that it is designed to promote just and equitable principles of trade and to protect investors and the public interest by providing for the prompt and fair resolution of a Floor Official's market decision.

¹⁹ See Amendment No. 2, *supra* note . An example of a situation where a Floor Official must act jointly with a Senior Floor Official is found in Commentary .02 to Amex Rule 1. This rule provides that if an option trading rotation is in progress prior to 4:02 p.m., and a Senior Floor Official and a Floor Official determine that a final trading rotation is needed to assure a fair and orderly market, the rotation in progress shall be halted and the final rotation begun as promptly as possible after 4:02 p.m.

²⁰ The Board has delegated to the Amex Adjudicatory Council, a board level committee, the responsibility for reviewing appeals to the Board.

²¹ 15 U.S.C. 78f(b).

²² 15 U.S.C. 78f(b)(5).

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

The Exchange does not believe that the proposed rule change, as amended, 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

The Exchange neither solicited nor received written comments with respect to the proposed rule change, as amended.

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 Exchange 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, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 Room. 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-2001-07 and should be submitted by December 6, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²³

J. Lynn Taylor,

Assistant Secretary.

[FR Doc. 02-28991 Filed 11-14-02; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46792; File No. SR-CME-2002-01]

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Amendment No. 1 Thereto, and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 2 Thereto, by Chicago Mercantile Exchange, Inc. Relating to Customer Margin Requirements for Security Futures

November 8, 2002.

On September 27, 2002, Chicago Mercantile Exchange, Inc. ("CME" or "Exchange") submitted to the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change relating to customer margin requirements for security futures. On October 7, 2002, CME submitted Amendment No. 1 to the proposed rule change.³ The proposed rule change was published for comment in the **Federal Register** on October 21, 2002.⁴ On November 7, 2002, CME submitted Amendment No. 2 to the proposed rule change.⁵ The Commission received no comment letters directly addressing the proposed rule change. However, the Commission received nine comment letters from ten commenters regarding a proposed rule change submitted by OneChicago, LLC ("OneChicago"), which is substantially similar to CME's proposed rule change.⁶ Accordingly, the Commission has considered those comments in its review of the proposed

²³ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See letter from Phupinder S. Gill, Managing Director and President, Clearing House Division, CME, to Office of Market Supervision, Division of Market Regulation, Commission, dated October 4, 2002 ("Amendment No. 1"). In Amendment No. 1, the Exchange replaced in its entirety the Form 19b-4 filed on September 27, 2002.

⁴ Securities Exchange Act Release No. 46637 (October 10, 2002), 67 FR 64672.

⁵ In Amendment No. 2, CME modified certain aspects of its exclusion for market making activity.

⁶ See Securities Exchange Act Release No. 46555 (September 26, 2002), 67 FR 61707.

rule change.⁷ On November 7, 2002, CME submitted a letter in response to those comments.⁸ This order approves the proposed rule change and Amendment No. 1 thereto, accelerates approval of Amendment No. 2, and solicits comments from interested persons on Amendment No. 2.

I. Description of the Proposed Rule Change

Introduction

On August 1, 2002, the Commodity Futures Trading Commission (CFTC) and SEC (collectively, the Commissions) jointly adopted customer margin requirements for security futures.⁹ Under the Commissions' "account specific" approach, the Commissions' margin rules apply certain core requirements to all security futures, and direct that the more specific requirements depend on the type of account in which the security futures are held (*i.e.*, a futures account or securities account).

Proposal

The proposed rule change sets forth margin requirements for security futures traded on CME that are held in futures accounts.¹⁰ Specifically, the proposed rule change sets the minimum initial and maintenance customer margin rates for such security futures and provides for lower margin levels for permitted strategy-based offset positions. The proposed rules exclude certain financial relations to which the Commissions'

margin rules do not apply. The proposed rule change also establishes standards under which members may qualify as Security Futures Dealers and therefore be excluded from CME's margin rules.

Margin Levels

The Commissions' margin rules require that customers deposit in their accounts minimum margin of 20 percent of the current market value of security futures.¹¹ In addition, the Commissions' rules permit national securities exchanges to set margin levels below 20 percent of the current market value of security futures for certain offsetting positions in security futures and other securities or futures. The proposed rule change establishes a minimum margin rate of 20 percent for both long and short positions in security futures, except with respect to specified, permitted offsetting positions. Under the proposed rule change, CME permits reduced margin levels for eighteen specific offsetting positions.¹²

Security Futures Dealers

As noted above, the proposed rule change provides an exclusion from CME's margin rules for market makers. Under the proposed rule change, CME's market maker exclusion provides that in order to qualify for the exclusion from the margin rules, a person must (1) be a CME member that is registered with the Exchange as a dealer in security futures; (2) be registered as a floor trader or a floor broker with the CFTC under section 4f(a)(1) of the CEA or as a dealer with the Commission under section 15(b) of the Act; (3) maintain records sufficient to prove compliance with the requirements of CME Rule 930 and Rule 41.42(c)(2)(v) under the CEA and Rule 400(c)(2)(v) under the Act, as applicable, including without limitation trading account statements and other financial records sufficient to detail activity; and (4) hold itself out as being willing to buy and sell security futures

for its own account on a regular or continuous basis. In addition, the market maker exclusion provides that any market maker that fails to comply with the applicable rules of the exchange or the margin rules adopted by the Commission and the CFTC shall be subject to disciplinary action in accordance with Chapter 4 of CME's rules, and that appropriate sanctions in the case of any such failure shall include, without limitation, a revocation of such market maker's registration as a dealer in security futures.

The CME's proposal, as amended by Amendment No. 1, provided that a market maker would be considered to be holding itself out as being willing to buy and sell security futures for its own account on a regular or continuous basis if either (1) At least 75% of its gross revenue on an annual basis is derived from business activities or occupations from trading listed financial derivatives and the instruments underlying those derivatives, including security futures, stock index futures and options, stock and index options, stocks, foreign currency futures and options, foreign currencies, interest rate futures and options, fixed income instruments and commodity futures and options; or (2) except for unusual circumstances, at least fifty percent (50%) of its trading activity on CME in any calendar quarter is in classes of security futures contracts to which it is assigned by CME.

In Amendment No. 2, CME amended this aspect of its proposed rule change. Specifically, the market maker exclusion now provides three alternatives ways for a member to satisfy the requirement that a security futures dealer hold itself out as being willing to buy and sell security futures for its own account on a regular or continuous basis. Under the first alternative, the market maker must (1) Provide continuous two-sided quotations throughout the trading day for all delivery months of security futures representing a meaningful proportion of the total trading volume on the Exchange,¹³ subject to relaxation during unusual market conditions as determined by CME (such as a fast market in either a security future or underlying security) at which times the market maker must use its best efforts to quote continuously and competitively; and (2) when providing quotations, quote with a maximum bid/ask spread of no more than the greater of \$0.20 or 150% of the bid/ask spread in the

⁷ See letters to Jonathan Katz, Secretary, Commission, from: Philip D. DeFeo, Chairman and Chief Executive Officer, Pacific Stock Exchange, dated October 15, 2002 ("PCX Letter"); Marc Menchel, Senior Vice President and General Counsel, National Association of Securities Dealers, dated October 23, 2002 ("NASD Letter"); Richard Ketchum, Deputy Vice Chairman and President, The Nasdaq Stock Market, Inc., dated October 23, 2002 ("Nasdaq Letter"); Michael J. Simon, Senior Vice President and Secretary, International Securities Exchange, Inc., dated October 22, 2002 ("ISE Letter"); Michael J. Ryan, Jr., Executive Vice President and General Counsel, American Stock Exchange, Inc., dated October 22, 2002 ("Amex Letter"); John P. Davidson, Managing Director, Morgan Stanley & Co. Inc., and Mitchell J. Lieberman, Managing Director, Goldman, Sachs & Co., dated October 23, 2002 ("Morgan/Goldman Letter"); Kathleen M. Hamm, Senior Vice President, Nasdaq Liffe Markets, LLC, dated October 22, 2002 ("NQLX Letter"); Darla C. Stuckey, Corporate Secretary, New York Stock Exchange, Inc., dated October 24, 2002 ("NYSE Letter"); and Michael R. Schaefer, Managing Director, Salomon Smith Barney, dated October 25, 2002 ("SSB Letter").

⁸ Letter from CME to Office of Market Supervision, Division of Market Regulation, Commission, dated November 7, 2002 ("CME Letter").

⁹ Securities Exchange Act Release No. 46292, 67 FR 53146 (August 14, 2002).

¹⁰ The proposed rule change limits the scope of CME's customer margin rules to positions in futures accounts.

¹¹ Rule 403(b)(1) under the Act and Rule 41.45(b)(1) under the Commodity Exchange Act ("CEA") 17 CFR 240.403(b)(1) and 17 CFR 41.45(b)(1).

¹² In its release adopting the customer margin rules for security futures, the Commissions published a table of eighteen offsetting positions and corresponding margin levels that are consistent with comparable offsets permitted for positions involving exchange-traded options. The proposed rule change includes all of the offsetting positions that the Commissions included in their table. However, CME's customer margin rules only apply to positions held in futures accounts. Because any offset that includes a security (other than a security future) must be carried in a securities account, CME's rule applies only to those offsetting positions that may be carried in a futures account (*i.e.*, offsets that do not include securities other than security futures).

¹³ Beginning on the 181st calendar day after the commencement of trading on the Exchange, a "meaningful proportion of the total trading volume on the Exchange from time to time" shall mean a minimum of 20% of such trading volume.

primary market for the security underlying each security future.

Under the second alternative, the market maker must (1) respond to at least 75% of the requests for quotation for all delivery months of security futures representing a meaningful proportion of the total trading volume on the Exchange,¹⁴ subject to relaxation during unusual market conditions as determined by the CME (such as a fast market in either a security future or an underlying security) at which times such Market Maker must use its best efforts to quote competitively; and (2) when responding to requests for quotation, quote within five seconds with a maximum bid/ask spread of no more than the greater of \$0.20 or 150% of the bid/ask spread in the primary market for the security underlying each security future.

Under the third alternative, the market maker is assigned to a group of security futures that is either unlimited in nature ("Unlimited Assignment") or is assigned to no more than 20% of the security futures listed on the Exchange ("Limited Assignment"). In addition, this alternative provides that: (a) At least 75% of the market maker's total trading activity in CME products is in its assigned security futures, measured on a quarterly basis; (b) during at least 50% of the trading day the market maker has bids or offers in the market that are at or near the best market, except in unusual market conditions (such as a fast market in either a security future or an underlying security), with respect to at least 25% (in the case of an Unlimited Assignment) or at least one (in the case of a Limited Assignment) of its assigned security futures; and (c) the first two requirements are satisfied on at least 90% (in the case of an Unlimited Assignment) or 80% (in the case of a Limited Assignment) or in the case where the Exchange is listing four or fewer security futures contracts) of the trading days in each calendar quarter. CME has requested approval of this alternative on a six-month pilot basis beginning on the date of this order.

II. Summary of Comments

As noted above, the Commission received no comment letters directly addressing the proposed rule change, but did receive nine comment letters from ten commenters regarding a similar proposed rule change submitted by OneChicago. Accordingly, the

¹⁴ Beginning on the 181st calendar day after the commencement of trading on the Exchange, a "meaningful proportion of the total trading volume on the Exchange from time to time" shall mean a minimum of 20% of such trading volume.

Commission has considered those comments in its review of the proposed rule change.¹⁵ CME submitted a letter in response to those comments.¹⁶

Market Maker Exclusion

All of the comments expressed concern with the proposed market maker exclusion. In particular, the commenters objected to the provision that would allow members to qualify for the market maker exclusion based on the amount of revenue they derive from trading listed financial derivatives and underlying instruments. Six comments expressed the view that this test was inconsistent with the guidelines provided by the Commission and the CFTC,¹⁷ and six comments maintained that the proposed revenue requirement was not consistent with the margin requirements for comparable exchange-traded options and therefore did not satisfy the requirements of section 7(c)(2) of the Act.¹⁸ Commenters argued that the revenue test would allow members to qualify for the market maker exclusion without actually providing liquidity to the market for security futures.¹⁹ Other commenters contended that the revenue test would increase systemic risk in the marketplace for security futures, and therefore did not satisfy section 7(c)(2) of the Act, by allowing an excessively high number of market professionals to trade security futures with reduced margin requirements.²⁰

In response to the commenters' concerns, CME stated that it had modified the tests that a CME member must satisfy in order to qualify for the market maker exclusion by eliminating the test based on revenue and revising the test based on trading activity. CME also stated that the futures industry tends to rely upon "local traders" acting as individual entrepreneurs as a primary source of liquidity, and that these local traders are typically not obligated to participate or otherwise be tied to a specific marketplace during the course of the trading day. In addition, CME stated that electronic trading systems

developed to support futures trading have been developed to parallel open outcry trading practices, under which local traders may be physically unable to voice a bid and an offer simultaneously or to voice either a bid or offer continuously throughout the entire trading day on each and every trading day. CME maintained that, as a result, electronic futures trading systems may not necessarily support features such as request for quotes or the entry of two-sided quotations.

CME expressed the view that the first and second revised tests are substantively identical to tests that the Commission approved for Nasdaq Liffe Markets.²¹ In addition, CME maintained that the third revised test is crafted to reflect the realities of the its electronic trading platform, as well as the fact that a number of CME's floor traders and floor brokers are individual entrepreneurs who cannot physically represent themselves in the market at all times on all trading days. Finally, CME stated that it requested that the third revised test of its market maker exclusion in proposed Rule 930.B.2.b.(3) be adopted on a six-month pilot basis, subject to public comment and subsequent approval by the Commission so that there would be an opportunity for the study of the effects and implications of the test before it is adopted on a permanent basis.

In addition, two comments expressed the view that the proposed market maker exclusion would encourage imprudent risk taking, speculation, and leverage because there would be no net capital requirements imposed either on a floor broker that qualifies for the market maker exclusion or on its carrying broker-dealer or FCM.²² The commenters' concern is that the regulatory capital requirements for certain security futures market participants is inadequate. Moreover, those commenters expressed concern that in the event of a bankruptcy of a carrying firm, a bankruptcy receiver or trustee would pay out to the floor broker a pro rata share of the available pool of assets on the same terms as customers, notwithstanding that the floor broker was not required to post customer margin.

The Commission believes that the determination of what amount of capital is sufficient for a market participant is within the purview of the participant's primary regulator and does not believe that it would be appropriate to require CME's margin rules to address these

¹⁵ PCX Letter, NASD Letter, Nasdaq Letter, ISE Letter, Amex Letter, Morgan/Goldman Letter, NQLX Letter, NYSE Letter, and SSB Letter. See *supra* note 7. The SSB Letter stated that it agreed generally with the comments expressed in the Morgan/Goldman Letter.

¹⁶ CME Letter, *supra* note 8.

¹⁷ NASD Letter, Morgan/Goldman Letter, NQLX Letter, NYSE Letter, Nasdaq Letter, SSB Letter, and Amex Letter.

¹⁸ PCX Letter, NASD Letter, ISE Letter, Amex Letter, Morgan/Goldman Letter, and SSB Letter.

¹⁹ PCX Letter, ISE Letter, and NQLX Letter, Morgan/Goldman Letter.

²⁰ Morgan/Goldman Letter, NASD Letter, SSB Letter.

²¹ See Securities Exchange Act Release No. 46771 (November 5, 2002).

²² Morgan/Goldman Letter and SSB Letter.

concerns indirectly. In addition, the Commission believes that any concerns regarding a market maker's share of a customer's estate in a bankruptcy proceeding would be more properly addressed by changes to the insolvency regime applicable to those market participants.

Finally, one commenter expressed concern with the fact that certain aspects of the margin rules would apply to positions carried in securities accounts. One commenter objected to the proposal to adopt margin levels for offsetting positions that only may be held in securities accounts even though its rules only apply to positions in futures accounts because the proposal gave the impression that those offsets were permitted to be carried in a futures account.²³ The Commission reiterates that because any offset that includes a security (other than a security future) must be carried in a securities account, CME's rule applies only to those offsetting positions that may be carried in a futures account (*i.e.*, offsets that do not include securities other than security futures). In addition, the Commission emphasizes that approval of the proposed rule change does not affect the applicability of the rules of another self-regulatory organization to its members.

III. Discussion

Under section 19(b)(2) of the Act, the Commission is directed to approve the proposed rule change if it finds that it is consistent with the requirements of the Act and the rules and the rules and regulations thereunder applicable to a national securities exchange.²⁴ Section 6(b)(5) of the Act²⁵ requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade and, in general, to protect investors and the public interest.²⁶ In addition, section 7(c)(2)(B) of the Act²⁷ provides, among other things, that the margin rules for security futures must preserve the financial integrity of markets trading security futures, prevent systemic risk, and be consistent with the margin requirements for comparable exchange-traded options. Section 7(c)(2)(B) also provides that the margin levels for security futures may be no lower than the lowest level of margin, exclusive of premium, required for any

comparable exchange-traded option. For the reasons discussed below, after careful review and consideration of the commenters' views, the Commission finds that the rule change is consistent with CME's obligations under the Act and the rules and regulations thereunder.

The Commission believes that the rule change is generally consistent with the customer margin rules for security futures adopted by the Commission and the CFTC. In particular, the Commission notes that, consistent with Rule 403 under the Act, CME's proposed rule provides for a minimum margin level of 20% of current market value for all positions in security futures. The Commission believes that 20% is the minimum margin level necessary to satisfy the requirements of section 7(c)(2)(B) of the Act. Rule 403 under the Act²⁸ also provides that a national securities exchange may set margin levels lower than 20% of the current market value of the security future for an offsetting position involving security futures and related positions, provided that an exchange's margin levels for offsetting positions meet the criteria set forth in section 7(c)(2)(B) of the Act. The offsets proposed by CME are consistent with the strategy-based offsets permitted for comparable offset positions involving exchange-traded options and therefore consistent with Section 7(c)(2)(B) of the Act.

Finally, the Commission believes that the standards for CME's market maker exclusion, as amended by Amendment No. 2, are consistent with the Act, and Rule 400(c)(2)(v) thereunder.²⁹ Specifically, the Commission's margin rules do not apply to a member of a national securities exchange that is registered with such exchange as a "security futures dealer" pursuant to exchange rules that must meet several criteria, including a requirement that a security futures dealer be required "to hold itself out as being willing to buy and sell security futures for its own account on a regular or continuous basis." The Commission believes that the affirmative obligations required by CME Rule 930.B.2.b satisfy this requirement.

IV. Accelerated Approval of Amendment No. 2

CME has asked the Commission to approve Amendment No. 2 to the proposed rule change prior to the thirtieth day after the date of publication of notice of the filing. Amendment No. 2 modifies CME's

market maker exclusion. Specifically, Amendment No. 2 modifies the trading obligations that market maker must meet to qualify for the exclusion. The amendments to the trading obligations are in response to the commenters' concerns, and clarify the minimum trading requirements imposed on market makers in order to satisfy the requirement of the exclusion that a market maker hold itself out as being willing to buy and sell security futures for its own account on a regular or continuous basis. CME has also requested that the Commission approve the revised test in CME Rule 930.B.2.b.(3) as a pilot program for six months beginning on the date of this order.

The Commission finds good cause for approving the proposed rule change, as amended, prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. The Commission believes that accelerated approval of the proposed rule change should enable CME to begin trading security futures from the outset of security futures trading.³⁰ In addition, the Commission believes that granting accelerated approval to Amendment No. 2 thereto should clarify the obligations that CME members must meet in order to qualify for the market maker exclusion from the margin requirements. In addition, the Commission notes that certain of the modifications to the trading obligations of the market maker exclusion set forth in Amendment No. 2 will take effect as a temporary pilot to give members of the public an opportunity to comment on the substance of those aspects of Amendment No. 2 before CME requests permanent approval. Accordingly, the Commission believes that there is good cause, consistent with section 19(b) of the Act, to approve Amendment No. 2 to the proposed rule change on an accelerated basis.

V. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether Amendment No. 2 is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the

²³ NQLX Letter.

²⁴ 15 U.S.C. 78s(b)(2).

²⁵ 15 U.S.C. 78f(b)(5).

²⁶ In approving this rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78o-3(b)(9).

²⁷ 15 U.S.C. 78g(c)(2)(v).

²⁸ 17 CFR 240.403(b)(2).

²⁹ 17 CFR 200.400(c)(2)(v).

³⁰ The Commission understands that trading in security futures is scheduled to begin on November 8, 2002.

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 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-CME-2002-01 and should be submitted by December 6, 2002.

VI. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,³¹ that the proposed rule change, as amended, (File No. SR-CME-2002-01) be, and hereby is, approved, *provided, however*, that CME Rule 930.B.2.b.(3) is approved until May 7, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.³²

J. Lynn Taylor,

Assistant Secretary.

[FR Doc. 02-28988 Filed 11-14-02; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46790; File Nos. SR-GSCC-2002-09 and SR-MBSCC-2002-01]

Self-Regulatory Organizations; Government Securities Clearing Corporation and MBS Clearing Corporation; Notice of Filing of Proposed Rule Changes Relating to the Merger of MBS Clearing Corporation into the Government Securities Clearing Corporation to Form the Fixed Income Clearing Corporation

November 7, 2002.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on October 7, 2002, the Government Securities Clearing Corporation ("GSCC") and the MBS Clearing Corporation ("MBSCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule changes (File Nos. SR-GSCC-2002-09 and SR-MBSCC-2002-01). On October 31, 2002, and on November 5, 2002, GSCC and MBSCC amended the proposed rule changes. The proposed rule changes are described in Items I, II,

and III below, which items have been prepared primarily by GSCC and MBSCC. The Commission is publishing this notice to solicit comments on the proposed rule changes from interested parties.

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

The proposed rule changes propose arrangements for the combination of GSCC with MBSCC. The subject proposal provides the following:

- MBSCC will merge into GSCC.
- GSCC will be renamed the Fixed Income Clearing Corporation ("FICC").
- FICC will provide services currently offered by GSCC and MBSCC through separate divisions of FICC ("Government Securities Division" and "Mortgage-Backed Securities Division" collectively referred to as "Divisions"). FICC will adopt the current rules of GSCC, as amended and described herein, as rules of the Government Securities Division and the current rules of MBSCC, as amended and described herein, as rules of the Mortgage-Backed Securities Division.

• After the merger, current GSCC members will receive the services they currently receive from GSCC from the Government Securities Division, and current MBSCC participants, limited purpose participants, and Electronic Pool Notification ("EPN") users will receive the services they currently receive from MBSCC from the Mortgage-Backed Securities Division. The membership agreements between GSCC and its members and between MBSCC and its participants, limited purpose participants, and EPN users will be modified to reflect the merger.

- The rules of GSCC and MBSCC will be modified to reflect that the formerly separate clearing corporations will be separate divisions of FICC.

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

In their filings with the Commission, GSCC and MBSCC included statements concerning the purpose of and basis for the proposed rule changes and discussed any comments they received on the proposed rule changes. The text of these statements may be examined at the places specified in Item IV below. GSCC and MBSCC have prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.²

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

GSCC and MBSCC became wholly-owned, indirect subsidiaries of The Depository Trust and Clearing Corporation ("DTCC") as a result of merger and exchange offer transactions that took place in late 2001 ("DTCC Integration").³ GSCC and MBSCC provide clearing and certain ancillary services for government securities and mortgage-backed securities, respectively. The clearing and other services for these different types of fixed-income products have many common elements. The handling of such products by different clearing corporations hinders development of uniform standards for the fixed-income services industry. The combination of GSCC and MBSCC will lead to development of uniform standards for messaging, reporting, netting and settlement mechanisms, standardized settlement practices, and coordinated cash and mark-to-market flows for fixed-income products. Moreover, combining GSCC and MBSCC will help the clearing corporations achieve important membership and risk management goals, such as building a consolidated risk management platform, optimizing cross-margining among various fixed-income products, and establishing uniform membership standards. Furthermore, redundant facilities, services, and operational aspects⁴ will be eliminated as a result of the merger thereby reducing the costs of processing transactions in fixed-income products over time.

To effect the merger, MBSCC will be merged into GSCC under New York law. At the time of the merger, GSCC Acquisition Company LLC ("GSCC Parent"), the sole shareholder of GSCC, will pay MBSCC Holding Company, Inc., the sole shareholder of MBSCC, a nominal amount of money in consideration for canceling its shares of capital stock of MBSCC, and shares of capital stock of MBSCC will be cancelled. GSCC will be the surviving corporation of the merger and will be renamed FICC. GSCC Parent will be the sole direct shareholder of FICC. The current Certificate of Incorporation and Bylaws of GSCC will be amended to be the Certificate of Incorporation and

³ Securities Exchange Act Release Nos. 44988 (October 25, 2001), 66 FR 55222 [SR-MBSCC-2001-01] and 44989 (October 25, 2001), 66 FR 55220 [SR-GSCC-2001-11].

⁴ Operational aspects include such things as separate annual reports, regulatory reports, audits, financial statements, and regulatory examinations.

³¹ 15 U.S.C. 78s(b)(2).

³² 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² The Commission has modified the text of the summaries prepared by GSCC and MBSCC.