

Asian 25 Index immediately. The Commission is accelerating approval of the proposed rule change, as amended by Amendment No. 1, prior to the expiration of the comment period because these proposed Indexes are similar the other broad-based index options that CBOE currently trades, and CBOE has addressed the relevant regulatory issues, especially pertaining to comprehensive surveillance agreements. Because Amendment No. 2 does not change the proposed rule change but only request acceleration prior to the expiration of the comment period, the Commission is noticing and approving this amendment on an accelerated basis. Accordingly, the Commission believes that it is consistent with Section 6(b)(5) and 19(b)(2) of the Act to approve the proposed rule change, and Amendment Nos. 1 and 2 thereto, on an accelerated basis.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether Amendment No. 2 to the proposed rule change 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, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of such filing will also be available for inspection and copying at the principal office of CBOE. All submissions should refer to the File No. SR-CBOE-2002-40 and should be submitted by March 25, 2003.

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹⁹ that the proposed rule change (SR-CBOE-2002-40), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²⁰

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03-4953 Filed 3-3-03; 8:45 am]

BILLING CODE 8010-01-P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47402; File No. SR-OCC-2002-11]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change To Modify the Stock/Loan Hedge Program

February 25, 2003.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on May 21, 2002, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") and on July 16 and September 26, 2002, amended the proposed rule change as described in Items I, II, and III below, which items have been prepared primarily by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested parties.

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

The proposed rule change would modify OCC's Stock/Loan Hedge Program ("Hedge Program") to establish: (i) Heightened financial requirements as a condition for clearing members to designate accounts as margin-ineligible; (ii) additional eligibility requirements for eligible securities; and (iii) limits on the notional value of the stock loan/borrow position that a clearing member may maintain in a single stock in a margin-ineligible account.

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

In its filing with the Commission, OCC 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. OCC has 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 Change

The purpose of the proposed rule change is to modify OCC's Hedge Program, under which OCC operates a centralized facility for clearing stock loan/borrow transactions between OCC clearing members. In order to provide enhanced risk management while maintaining the flexibility of the current program, OCC proposes to establish: (i) Heightened financial requirements as a condition for clearing members to designate accounts as margin-ineligible; (ii) additional eligibility requirements for eligible securities; and (iii) limits on the notional value of the stock loan/borrow position that a clearing member may maintain in a single stock in a margin-ineligible account.

OCC's Hedge Program is intended to facilitate stock lending transactions among OCC's clearing members. Clearing members effecting stock loan/borrow transactions through the Hedge Program obtain the advantages of centralized clearing of those transactions as well as reduced credit risk through the substitution of OCC as the counterparty in all transactions. Unless a clearing member has designated an account as margin-ineligible for purposes of the Hedge Program, stock loan and borrow positions are margined by OCC's TIMS³ margin system using the same basic risk assessment procedures that are used for positions in options or futures. For many clearing members, this results in an important advantage of the Hedge Program. By taking into consideration the reduction in risk where stock loan/borrow positions are on the opposite side of the market from option positions on the same underlying stock, the margin system will calculate a reduced margin requirement for the account containing the offsetting positions.⁴

² The Commission has modified the text of the summaries prepared by OCC.

³ The Theoretical Intermarket Margin System, known as TIMS, uses advanced portfolio theory to recognize economically and statistically reasonable hedges among various positions and to correctly assess the dollar risk of those positions.

⁴ While similar offsets may exist between positions in index options, on the one hand, and a group of stock loan/borrow positions that are identified as baskets comprised of constituent securities in the index, the stock borrow basket/stock loan basket feature of the Hedge Program, although provided for in the OCC By-Laws and Rules, has not been placed into operation for systems reasons. OCC is proposing in this filing to add an interpretation following Section 2 of Article

Continued

¹⁹ 15 U.S.C. 78s(b)(2).

²⁰ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

For other clearing members, however, the margin offset or hedging aspect of the Hedge Program is of little or no benefit. For these clearing members, the nature of their business or the organization of their business within the firm is such that they rarely if ever have stock loan/borrow transactions that provide any significant offset against their options positions. These firms may nevertheless desire to use the Hedge Program because of its other benefits. The participation of these clearing members, which tend to be the larger clearing members, is desirable from OCC's perspective because they contribute liquidity to the program and facilitate inclusion in the program of the hedging activity of some of OCC's less well-capitalized clearing members. It reduces OCC's risk when a market maker clearing firm, for example, carries stock loan/borrow positions in the same OCC account as the positions that the loan/borrow positions hedge.⁵ However, in order to do that, the clearing firm must find a stock loan counterparty that is willing to submit the transaction to OCC for clearance. If the counterparty is not itself entering into the transaction for hedging purposes, it may be willing to clear the transaction through OCC only if it can do so on a margin-ineligible basis to avoid additional cost.

For those clearing members whose stock loan/borrow positions are not ordinarily offset by options positions, clearing stock loan/borrow activity through the Hedge Program increases rather than reduces their risk margin requirement at OCC. In the stock loan market, collateral (usually equal to 100% or 102% of the value of the loaned stock) is provided by the borrower to the lender to secure the lender's obligation to return the stock. Daily mark-to-market payments between the borrower and lender maintain the collateral at that level. The same is true when stock loan activity is cleared through the Hedge Program. However, in addition to the collateral that is passed by OCC between the borrowing and lending clearing members, OCC's TIMS system also assesses both the

borrower and the lender an amount of risk margin equal to one day's anticipated maximum market movement in order to protect OCC against a default by the borrower or the lender in its mark-to-market obligations. Because this risk margin is collected only for stock loan transactions that are submitted to OCC, clearing these transactions through OCC imposes additional costs on some clearing members.

In order to address this issue, the Hedge Program permits clearing members to elect to carry stock loan and borrow transactions on a margin-ineligible basis. If a clearing member designates an account as margin-ineligible, OCC will exclude any stock loan or borrow positions in that account when calculating the regular margin requirement for the account. OCC, however, relies on other elements of its protection systems⁶ to assess its potential exposure with respect to positions carried in a margin-ineligible account. Margin will be required for positions carried in a margin-ineligible account if predefined concentration monitoring parameters are exceeded.

OCC believes that permitting clearing members to carry stock loan and borrow positions on a margin-ineligible basis is appropriate, safe, and essential to the competitiveness of the Hedge Program. However, in recognition of the fact that this alternative does create uncollateralized risk for OCC, OCC has conducted a study of credit practices in the stock loan market generally and has determined to implement certain measures to reduce its risk.

Although OCC's current risk management practices are consistent with industry standards, OCC is nevertheless proposing elevated financial standards for clearing members wishing to designate accounts as margin-ineligible for purposes of the Hedge Program. Clearing members would be required to maintain excess net capital of at least \$75 million in order to carry margin-ineligible accounts with OCC.⁷ OCC believes this requirement is sufficient to ensure strong participant credit standing

without unduly hindering program participation.

The excess net capital requirement would be supplemented by a profitability standard. A clearing member would not be permitted to maintain a margin-ineligible account if it has: (i) Losses in one month equal to or exceeding 50 percent of its excess net capital; (ii) cumulative losses over two consecutive months equal to or exceeding 60 percent of its excess net capital; or (iii) cumulative losses over three consecutive months equal to or exceeding 70 percent of its excess net capital. These excess net capital and profitability standards would be ongoing tests and would have to be met at all times by a clearing member wishing to carry stock loan or borrow positions in any account on a margin-ineligible basis. Clearing members falling out of compliance with these standards would be precluded from clearing opening transactions in a margin-ineligible account while out of compliance.

The rationale for these requirements is that unlike a participant in the regular stock loan market, which has the ability to consider the impact of new transactions on counterparty credit limits before entering into them, OCC becomes a counterparty solely at the discretion of the lender and borrower without the ability to approve or disapprove individual loans on a credit basis before they are accepted for clearance. OCC's excess net capital and profitability standards should substitute for a transaction-by-transaction credit review. Using these straightforward requirements instead of a credit limit or activity cap makes it unnecessary for OCC to reserve the right to reject completed transactions in cases where acceptance would put one of the parties above its cap.

As an additional safety measure, OCC is proposing to amend the definition of "Eligible Stock" to exclude non-option stocks from the program subject to limited exceptions.⁸ Loans for non-option stocks will be permitted to be maintained (i) if the loan was accepted prior to the implementation of the restriction or (ii) if the stock is deliverable upon exercise of an

XXI of the By-Laws stating that OCC will provide notice to its clearing members when this feature becomes operative.

⁵ As an economic matter, option and security futures positions are hedged not by a clearing member's stock loan or borrow positions, but by its related long or short positions in the underlying stock. However, it is the stock loan/borrow positions that generate cash mark-to-market payments when the market moves against the member's options or futures positions. When the loan/borrow positions are carried in the Hedge Program, OCC is able to capture those payments. This is what enables OCC to reduce its margin requirements for the account in which the positions are carried.

⁶ OCC especially relies on its concentration monitoring system, known as ConMon, which provides a comparison of the capital and net worth of each OCC clearing member to the market risk associated with the clearing member's positions. Securities Exchange Act Release No. 40083 (June 11, 1998), 63 FR 33424 (June 18, 1998) [File No. SR-OCC-98-3].

⁷ Clearing members currently maintaining margin-ineligible accounts would be given a one-year grace period in which to conform to the minimum excess net capital requirement. If a clearing member is not in compliance at the end of that period, OCC would thereafter treat all of the clearing member's accounts as margin-eligible.

⁸ As originally filed, the proposed rule change sought to amend the definition of "Eligible Stock" to require that non-option stocks that are the subject of program transactions have a price per share of at least \$10.00 at the time the transaction is submitted to clearance. The September 26, 2002, amendment proposes to exclude non-option stocks from the program subject to limited exceptions in order to more closely align the use of the Hedge Program with its primary objective of recognizing the intermarket hedges between a participant's stock and options positions.

outstanding option (e.g., where a stock ceases to be an option stock but options on that stock remain outstanding or where a non-option stock is distributed to holders of an option stock and options on the latter are adjusted to require delivery of both stocks). The restriction applies only to non-option stocks because OCC does not want to limit clearing members' ability to include option hedging transactions in their accounts.

Finally, no lender or borrower would be allowed to maintain a stock loan or borrow position in a single issue in a margin-ineligible account if the notional value of the position exceeded the clearing member's excess net capital. This restriction is intended to address concentration risk. Where the positions are carried in a margin-eligible account, the restriction is deemed unnecessary because OCC will hold collateral sufficient to cover the risk.

OCC believes that the proposed rule change is consistent with the requirements of section 17A of the Act⁹ and the rules and regulations thereunder applicable to OCC because it will promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds in the custody and control of OCC by providing for enhanced risk management while maintaining the flexibility of the current Hedge Program.

(B) Self-Regulatory Organization's Statement on Burden on Competition

OCC does not believe that the proposed rule change would impose any burden on competition.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments were not and are not intended to be solicited with respect to the proposed rule change and none have been received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within thirty-five 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 ninety 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, including whether the proposed rule change 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. Comments may also be submitted electronically at the following e-mail address: *rule-comments@sec.gov*. All comment letters should refer to File No. SR-OCC-2002-11. This file number should be included on the subject line if e-mail is used. To help us process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. 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, NW., Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of OCC.

All submissions should refer to File No. SR-OCC-2002-11 and should be submitted by March 25, 2003.

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

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03-4951 Filed 3-3-03; 8:45 am]

BILLING CODE 8010-01-P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47396; File No. SR-OCC-2002-14]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of a Proposed Rule Change Relating to Procedures for Processing Late and Supplementary Exercise Instructions

February 24, 2003.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on June 28, 2002, The Options Clearing Corporation ("OCC") 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 primarily by OCC. 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 proposed rule change would amend OCC Rules 801 and 805 to modify the existing fees for processing late instructions and supplementary exercise notices and would amend Rule 801 to establish a specific cut-off time for accepting late exercise notices after the start of critical processing and to eliminate OCC's ability to accept instructions to modify a previously submitted exercise after the start of critical processing.

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

In its filing with the Commission, OCC 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. OCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.²

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

The purpose of this rule change is to amend Rules 801(e) and 805(g) to

¹ 15 U.S.C. 78s(b)(1).

² The Commission has modified parts of these statements.

⁹ 15 U.S.C. 78q-1.

¹⁰ 17 CFR 200.30-3(a)(12).