

connection with the proposed disclosure requirements.

General comments may be directed to the OMB Clearance Officer for the Securities and Exchange Commission at the address below. Comments concerning the accuracy of the estimated average burden hours for compliance with Commission rules and forms should be directed to Michael E. Bartell, Associate Executive Director, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549, and to the Securities and Exchange Commission's Clearance Officer, Office of Information and Regulatory Affairs, Paperwork Reduction Act number 3235-0307, Office of Management and Budget, Room 3228, New Executive Office Building, Washington, DC 20543.

Dated: September 5, 1995.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-24095 Filed 9-27-95; 8:45 am]

BILLING CODE 8010-01-M

[Release No. 34-36270]

Order Extending Exemption for Certain Brokers and Dealers From Broker-Dealer Registration

September 22, 1995.

AGENCY: Securities and Exchange Commission.

ACTION: Extension of exemption.

SUMMARY: The Securities and Exchange Commission is extending the exemption for persons acting as brokers or dealers with respect to certain categories of over-the-counter derivative instruments, to the extent that such instruments are securities, from the broker-dealer registration requirement under Section 15(a) of the Securities Exchange Act of 1934. As extended, the exemption is retroactive to June 6, 1934, the date of the enactment of the Securities Exchange Act of 1934, and will expire September 30, 1996.

EFFECTIVE DATE: September 22, 1995.

FOR FURTHER INFORMATION CONTACT: Catherine McGuire, Chief Counsel, Patrice Gliniecki, Senior Counsel, or Glenn Jessee, Senior Counsel, (202) 942-0073, Office of Chief Counsel, Division of Market Regulation, Mail Stop 5-10, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION:

I. Background

On December 22, 1994, the Securities and Exchange Commission

("Commission") issued an order under Section 15(a)(2) of the Securities Exchange Act of 1934 ("Exchange Act") exempting persons acting as brokers or dealers with regard to certain categories of over-the-counter ("OTC") derivative instruments, to the extent such instruments are securities, from the broker-dealer registration requirement under Section 15(a) ("Exemptive Order").¹ In issuing the Exemptive Order, the Commission recognized the importance of derivative instruments as financial management tools, and sought to provide assurance to market participants in light of questions regarding the proper statutory and regulatory designation of certain OTC contracts. Such concerns, it was noted, are compounded by the trend among dealers to conduct a range of OTC derivatives activities in unregistered entities, either here or abroad, or in separately capitalized derivative product companies.

Market participants have indicated to the Commission staff that the exemption set forth in the Exemptive Order has proved useful in addressing concerns regarding the status of various OTC derivative instruments.² Therefore, in order to continue to provide certainty to participants in the OTC derivatives market with respect to their registration obligations under the Exchange Act, the Commission is exercising its authority under Section 15(a)(2) of the Exchange Act to extend the exemption covering persons acting as brokers or dealers regarding certain categories of OTC derivative instruments, to the extent such instruments are securities, from the broker-dealer registration requirement under Section 15(a).

II. Discussion

A. Scope of Order

This order extends the exemption for persons acting as brokers or dealers with regard to transactions in certain classes of OTC options, to the extent such options are securities, from the broker-dealer registration requirement under

¹ Exchange Act Release No. 35135 (Dec. 22, 1994), 59 FR 67358 (Dec. 29, 1994). The Exemptive Order was issued concurrently with the issuance of an order instituting proceedings pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b) and 21C of the Exchange Act, and findings and other imposing remedial sanctions in the Matter of BT Securities Corporation. Exchange Act Release No. 35136 (Dec. 22, 1994).

² See Letter from Zachary Snow, Chairman, OTC Derivative Products Committee, Securities Industry Association ("SIA"), to Brandon Becker, Director, Division of Market Regulation, dated July 31, 1995; Letter from Brandon Becker, Director, Division of Market Regulation, to Zachary Snow, Chairman, SIA OTC Derivative Products Committee, dated June 28, 1995.

Section 15(a) of the Exchange Act. This exemption only applies to transactions involving individually negotiated, cash-settlement OTC options on debt securities or groups or indexes of such securities that (1) are documented as swap agreements, and (2) satisfy the terms of the exemption from regulation under the Commodity Exchange Act adopted by the Commodity Futures Trading Commission ("CFTC"), which is set forth at 17 CFR Part 35 ("Part 35 Rules").³ In addition, to the extent any person satisfies the conditions of the exemption, the Division of Market Regulation has indicated that it would not recommend enforcement action if such persons do not comply with the various statutory and regulatory requirements otherwise imposed on a "broker" or "dealer" as defined in Sections 3(a)(4) and 3(a)(5) of the Exchange Act.⁴ Such persons, however, remain subject to the antifraud provisions under the federal securities laws including, but not limited to, the provisions of Section 17(a) of the Securities Act of 1933, Sections 10(b) and 15(c) of the Exchange Act, and Rules 10b-5 and 15c1-2 thereunder.

B. Clarification

The Commission notes that questions have arisen regarding the specific application of the requirements set forth above. For example, certain persons seeking to avail themselves of the exemption have asked whether transactions within the scope of the exemption must be documented using master agreements formulated by the International Swaps and Derivatives Association ("ISDA"). Some market participants prefer to use their own documentation for these transactions rather than standardized agreements. Also, certain OTC derivatives transactions based on foreign debt securities or documented using non-U.S. master agreements developed specifically for foreign domestic markets. Accordingly, the requirement

³ Individually negotiated, cash-settled OTC options on debt securities that may satisfy these criteria could include (1) options on prices of debt securities; (2) options on yields of debt securities; (3) options on the difference, or spread, between the yields of two or more debt securities, the spread between the prices (or other value) of two or more debt securities, or the spread between yields and prices involving two or more debt securities; and (4) options on the spread between the price (or other value) or yield on one or more debt securities and the price (or other value) or yield of any other asset or index (other than a equity security or a group or index of equity securities).

⁴ In addition, the Commission staff will respond promptly to no-action, exemptive, or other requests submitted by brokers or dealers that require relief from specific provisions of the federal securities laws.

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

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

C. Public Interest

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

D. Effective Date; Future Regulatory Action

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

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

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

By the Commission.
Margaret H. McFarland,
Deputy Secretary.
[FR Doc. 95-24097 Filed 9-27-95; 8:45 am]

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

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

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

September 21, 1995.

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

I. Description

The proposed rule change modifies NSCC's Procedures, Section VII.H.4(b), to allow the processing of voluntary reorganizations (*i.e.*, tender or exchange offers) with protect periods³ of three days or greater through NSCC's Continuous Net Settlement ("CNS") system. Previously, only voluntary reorganizations with protect periods of five days or greater were eligible for NSCC's CNS system. All other voluntary reorganizations with protect periods of four days or less had to be settled on a trade by trade basis through NSCC's balance order system. On June 7, 1995, Rule 15c6-1⁴ adopted under the Act became effective requiring that most broker-dealer securities transactions be settled in three business days ("T+3"). Since the implementation of T+3, some voluntary reorganizations have had protect periods of three days rather than five days.

II. Discussion

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

¹ 15 U.S.C. 78s(b) (1988).

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

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

⁴ 17 CFR 240.15c6-1 (1994).

⁵ 15 U.S.C. 78q-1 (1988).

⁶ 15 U.S.C. 78q-1(b)(3)(F) (1988).