

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 Section, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such filing also will be available for inspection and copying at the principal office of the New York Stock Exchange. All submissions should refer to File No. SR-NYSE-95-46 and should be submitted by January 26, 1996.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁶

Jonathan G. Katz,

Secretary.

[FR Doc. 96-171 Filed 1-4-96; 8:45 am]

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[Release No. 36649; File No. SR-NASD-95-50]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by National Association of Securities Dealers, Inc. Amending the Buy-in Procedures in Section 59 of the Uniform Practice Code to Clarify the Appropriate Delivery Deadlines for Buy-in Notices

December 28, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² on November 15, 1995, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change that amends Section 59 of the Uniform Practice Code ("UPC" or "Code") to revise the buy-in procedures to clarify the appropriate delivery deadlines for buy-in notices.

⁶ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. § 78s(b)(1).

² 17 CFR 240.19b-4.

Notice of the proposed rule change, together with the substance of the proposal, was issued by Commission release (Securities Exchange Act Release No. 36496, November 20, 1995) and by publication in the Federal Register (60 FR 58695, November 28, 1995).³ No comment letters were received. The Commission is approving the proposed rule change.

I. Background

Under Section 59 of the Code, when the seller has not completed a contract of sale of securities by delivering the securities called for in the contract on settlement day, the buyer may close the contract by purchasing the subject securities in the open market ("buying-in"). When securities are bought-in to complete a contract, the seller is liable for any difference between the contract price and the buy-in price.

Pursuant to subsection 59(a) of the Code, a buy-in is initiated by the buyer delivering a notice of buy-in to the seller at his office not later than 12 noon, the seller's time, two business days preceding the execution of the proposed buy-in. Subsection 59(b) provides that the notice must include the terms of the contract to be closed and must state that unless delivery is effected at or before a certain specified time not earlier than 11:30 a.m., the buyer's local time, the security may be bought-in for the account of the seller (meaning the seller assumes the liability for the market price of the security bought-in). Subsection 59(b) also provides that if the originator of the buy-in notice is a participant in a registered securities depository and the security to be bought-in is a depository eligible security, the buy-in may not be executed before 2:30 p.m., Eastern Time.

The NASD has identified an inconsistency in subsection 59(b) in that the provisions permit a buy-in notice to specify the seller's delivery deadline at a time no earlier than 11:30 a.m., the buyer's local time, yet the buy-in may not be executed before 2:30 p.m., Eastern Time. If the seller obtained securities and tendered them for delivery after the notice deadline but before the buy-in was executed, the provisions of the rule and the notice could permit the buyer to refuse delivery and subject the seller to the risk of an execution at a price higher than the original contract price. To resolve

³ The proposal was originally filed with the Commission on October 26, 1995. The NASD subsequently submitted Amendment No. 1 to the filing. Letter from Elliot R. Curzon, Assistant General Counsel, NASD, to Karl J. Varner, Over-the-Counter Regulation, Division of Market Regulation, SEC, dated November 15, 1995.

this anomaly, the rule change amends subsection 59(b) of the UPC to notify the delivery times permitted to be specified in the buy-in notice.

II. The Terms of Substance of the Proposed Rule Change

The rule change amends Section 59 of the UPC to modify the delivery times permitted to be specified in the buy-in notice. With respect to buy-in notices for depository eligible securities where the originator is a depository participant, the notice may not specify a delivery time earlier than 3:00 p.m., Eastern Time.

In addition, the rule change amends UPC subsection 59(b)(2), which permits the recipient of a buy-in notice to retransmit the notice to another broker-dealer from whom the subject securities are due. A retransmitted buy-in notice must be delivered to the recipient not later than 12 noon, the seller's local time, on the business day preceding the buy-in date and the specified delivery time in the original notice.

III. Discussion

The Commission believes that the rule change is consistent with the provisions of Section 15A(b)(6) of the Act⁴ in that the rule change will refine the buy-in provisions of the code to recognize new developments in the clearance and settlement system.⁵ Furthermore, the rule change will facilitate the clearance and settlement of securities by eliminating an inconsistency in subsection 59(b) that permitted a buy-in notice to specify the seller's delivery deadline at a time no earlier than 11:30 a.m., the buyer's local time, yet the buy-in could not be executed before 2:30 p.m., Eastern Time. For depository eligible securities where the originator is a depository participant, the rule change precludes the buy-in notice from requiring the seller to deliver the securities before 3:00 p.m., the seller's time. The provision will reduce the risk of the buyer exposing the seller to an execution at a price higher than the original contract price. However, the rule change permits broker-to-broker buy-ins in nondepository eligible securities that specify an earlier delivery time (no earlier than 11:30 a.m. local time).

In addition, the rule change amends UPC subsection 59(b)(2) to require the recipient of a buy-in notice to retransmit

⁴ 15 U.S.C. § 78o-3.

⁵ The NASD noted that with the advent of same day funds settlement (SDFS) in early 1996 and the new settlement time frames associated with the Depository Trust Company's SDFS System, the appropriate buy-in execution time in subsection 59(b) should not be prior to 3:00 P.M. Eastern Time.

the notice to another broker-dealer from whom the securities are due not later than 12 noon, the seller's local time, on the business day preceding the date of execution of the buy-in. The specified delivery time in the retransmitted notice must not be earlier than the time specified in the original notice. The rule change modifies the existing language to provide the seller with 23½ hours to deliver the securities to the recipient that retransmitted the buy-in notice and is an improvement to the current procedures that arguably permit retransmittal to occur at the end of the previous business day, which provided the recipient with as little as 18½ hours notice.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change SR-NASD-95-50 be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Jonathan G. Katz,

Secretary.

[FR Doc. 96-168 Filed 1-4-96; 8:45 am]

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[Release No. 34-36657; File No. SR-NASD-95-56]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the National Association of Securities Dealers, Inc., Relating to an Extension and Expansion of the NASD's Equity Option Position Limit Hedge Exemption Pilot Program

December 29, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on November 21, 1995, the National Association of Securities Dealers, Inc. ("NASD") 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 by the self-regulatory organization. The NASD has requested accelerated approval for the proposal. This order approves the NASD's proposal on an accelerated basis and solicits comments from interested persons.

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

The NASD is proposing to amend Article III, Section 33(b)(3)(A)(5) of the NASD Rules of Fair Practice to extend, until December 31, 1997, the NASD's equity option position limit hedge exemption pilot program. The NASD is also proposing to expand the hedge exemption pilot program to permit the establishment of hedged positions up to three times the applicable basic position limit.

In addition, the NASD is requesting that the Commission find good cause, pursuant to Section 19(b)(2) of the Act, to approve the proposed rule change prior to the thirtieth day after publication in the Federal Register.

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 NASD 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 III below. The NASD 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

On February 9, 1990, the Commission approved a NASD proposal³ to implement a two-year pilot program during which certain fully hedged equity option positions would be automatically exempt from established position⁴ and exercise limits.⁵ On

³ See Securities Exchange Act Release No. 27697 (February 9, 1990), 55 FR 5535 (February 15, 1990).

⁴ Position limits impose a ceiling on the number of option contracts in each class on the same side of the market (*i.e.*, aggregating long calls and short puts and long puts and short calls) that can be held or written by an investor or group of investors acting in concert. Article III, Section 33(b)(3)(A) of the NASD Rules of Fair Practice currently provides that equity option position limits are 4,500, 7,500, or 10,500 contracts, depending upon the trading volume and number of outstanding shares of the underlying stock. In addition, the NASD has recently submitted to the Commission a rule proposal that would add a 20,000-contract position limit tier and a 25,000-contract position limit tier. See File No. SR-NASD-95-55.

⁵ Exercise limits restrict the number of options contracts which an investor or group of investors acting in concert can exercise within five consecutive business days. Under NASD Rules, exercise limits correspond to position limits, such

March 18, 1994, the Commission extended the NASD's hedge exemption pilot program through December 31, 1995.⁶

The NASD's hedge exemption provides for an automatic exemption from equity option position limits for accounts that have established one of the four most commonly used hedged positions⁷ and where each option contract is either (i) hedged by 100 shares of stock, (ii) hedged by securities that are readily convertible into, or economically equivalent to, such stock,⁸ or (iii) in the case of an adjusted options contract, hedged by the number of shares represented by the adjusted contract.

Under the NASD's current hedge exemption, the largest options position (combining hedged and unhedged positions) that may be established may not exceed twice the basic position limit (*i.e.*, 9,000, 15,000, or 21,000 contracts, respectively). In addition, the hedge exemption does not change the exercise limits contained in Article III, Section 33(b)(4) of the NASD Rules of Fair Practice. Therefore, market participants are allowed to exercise, during any five consecutive business days, the same number of options contracts as set forth in the position limit for that option, including those options positions that are hedged (*i.e.*, if the position limit for an option is 10,500 contracts and an investor has established a position of 21,000 contracts (10,500 unhedged and 10,500 hedged), the investor may exercise all 21,000 contracts during five consecutive business days).

The NASD is currently proposing two amendments to its hedge exemption pilot program. First, the NASD is

that investors in options classes on the same side of the market are allowed to exercise, during any five consecutive business days, only the number of options contracts set forth as the applicable position limit for those options classes. See Article III, Section 33(b)(4) of the NASD Rules of Fair Practice.

⁶ See Securities Exchange Act Release No. 33783 (March 18, 1994), 59 FR 14229 (March 25, 1994).

⁷ The four exempted hedge positions are: (1) Long stock and short calls; (2) long stock and long puts; (3) short stock and long calls; and (4) short stock and short puts.

⁸ The Commission notes that the NASD determines on a case-by-case basis whether an instrument that is being used as the basis for the underlying hedged positions is readily convertible into, or economically equivalent to, the security underlying the corresponding option position. In this regard, the NASD generally finds that an instrument that is not presently convertible into a security, but which will be at a future date, is not a "convertible" security for purposes of the hedge exemption. In addition, the NASD notes that if a convertible security used to hedge an option position is called for redemption by the issuer, the security would have to be converted into the underlying security immediately or the corresponding option position would have to be reduced accordingly.

¹ 15 U.S.C. § 78s(b)(1) (1988).

² 17 CFR 240.18b-4 (1994).