[Release No. 34–35149; File No. SR–OCC–94–08]

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving a Proposed Rule Change Relating to Flexibly Structured Index Options Denominated in a Foreign Currency

December 23, 1994.

On August 19, 1994, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR–OCC–94–08) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act).¹ Notice of the proposal was published in the **Federal Register** on October 19, 1994.² No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description of the Proposal

On September 23, 1993, the Commission approved a proposed rule change filed by OCC to accommodate the clearance and settlement of flexibly structured index options.3 Flexibly structured index options exhibit virtually the same characteristics as regular index options; therefore, OCC establishes long and short flexibly structured index option positions in clearing member accounts in precisely the same way it currently does for regular index options. OCC incorporates flexibly structured index options in its premium settlement, margin collection, exercise notice, exercise assignment, and exercise/expiration statement processes without significant changes to those processes. Premiums and exercise prices for the flexibly structured index options that currently are being traded are denominated in United States dollars. Parties to a transaction in such an option may customize certain terms of the option including the expiration date, the exercise style, the exercise price, the cap interval in the case of capped-style options, and the method to be used for establishing the current index value for purposes of settling expiration date exercises.

Recently, the Chicago Board Options Exchange ("CBOE") amended its rules regarding flexibly structured index options ⁴ in order to allow premiums and exercise prices of such options to be denominated in foreign currencies rather than in United States dollars.⁵ Accordingly, OCC is amending its By-Laws and Rules in order to clear and settle these options which OCC calls Flexibly Structured Index Options Denominated in a Foreign Currency ("FX Index Options").

To accommodate the clearance and settlement of FX Index Options, Article XXIII is being added to the Article of OCC By-Laws. Because FX Index Options are a type of index option, the OCC By-Laws governing index options, Article XVII, is being incorporated into new Article XXIII and is being made applicable to FX Index Options. In addition, because FX Index Options will settle in a foreign currency, certain of the OCC By-Laws governing Cross-Rate Foreign Currency Options in Article XX also are being incorporated into new Article XXIII where appropriate. For example, those By-Laws governing extraordinary events, adjustments, and the payment of premiums are being incorporated into the new article.

A Chapter XXIV is being added to the OCC Rules to accommodate FX Index Options. FX Index Options will be exercised pursuant to the rules governing existing index options. Accordingly, the rules governing exercise, assignment, allocation, and the exercise settlement date from Chapter XVIII, which pertains to index options, is being incorporated into new Chapter XXIV. In addition, the settlement procedure for FX Index Options will be the same as the procedure for existing index options. Exercised FX Index Options will be settled through the payment of an exercise settlement amount, which is the difference between the aggregate exercise price and the aggregate current index value. Accordingly, the rules governing exercise settlement and the exercise settlement date from Chapter XVIII are being incorporated into new Chapter XXIV. Because FX Index Options will settle in a foreign currency, certain settlement obligations of a party to an FX Index Option contract will be similar to the settlement obligations of a party to a cross-rate foreign currency option contract. Therefore, certain rules

governing settlement obligations from Chapter XXI, which pertains to crossrate foreign currency options, are being incorporated into new Chapter XXIV. Specifically, these include the obligation to set up bank accounts and the consequence of failing to pay a foreign currency. Finally, FX Index Options will be margined like cross-rate foreign currency options in that the margin requirement will be calculated in the applicable trading currency and then converted to United States dollars. Consequently, the language of Rule 2111 governing margin requirements for cross-rate foreign currency options is being incorporated into new Chapter XXIV

Two additional changes to the OCC By-Laws and an additional change to OCC's Rules also are being made. Specifically, the term "FX index option clearing member" is being added to the definition of "clearing member" in Article I, Section 1 of the By-Laws. In addition, the reference to the term "FLEX" in the definition of clearing member is being changed to "flexibly structured option" in order to make that term more generic. Finally, OCC Rule 401 is being amended to require that the currency in which the option is denominated, the expiration date of the option contract as opposed to the expiration month, and the cap price, if any, be included in the Report of Matched Trades.

II. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder and particularly with the requirements of Section 17A(b)(3)(F). 6 Section 17A(b)(3)(F) requires that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions, and to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which it is responsible. The Commission believes that OCC's proposed rule change meets these requirements by establishing a framework in which existing OCC systems, rules, and procedures are extended to the processing of the FX Index Options. OCC should be able to implement the clearance and settlement of the FX Index Options without much difficulty because FX Index Options are similar to regular index options and cross-rate foreign currency options currently cleared by OCC. The Commission believes that the use of

¹ 15 U.S.C. 78s(b)(1) (1988).

² Securities Exchange Act Release No. 34837 (October 13, 1994), 59 FR 52852.

³ Securities Exchange Act Release No. 31912 (February 23, 1993), 58 FR 11879 [File No. SR–OCC–92–33] (order approving proposed rule change relating to flexibly structured index options).

⁴Securities Exchange Act Release No. 34203 (June 13, 1994), 59 FR 31658 [File No. SR–CBOE–

^{93–33] (}order approving a proposed rule change relating to FLEX options designated in foreign currencies)

⁵ Premium and exercise prices for these non-United States dollars flexibly structured index options may be denominated in any of the foreign currencies currently underlying foreign currency options. Those currencies include: (1) Australian dollars, (2) British pounds, (3) Canadian dollars, (4) European Economic Community currency units, (5) French francs, (6) German Deutsche marks, (7) Japanese yen, and (8) Swiss francs.

^{6 15} U.S.C. 78q-1(b)(3)(F) (1988).