

comprising the collar in excess of the applicable basic position limit (*i.e.*, 4,500) must be hedged on a one-for-one basis with 450,000 shares. The total number of allowable option contracts on the same side of the market in this example would be 13,500.

B. An investor is short 1,000 calls. The investor may establish an OTC collar consisting of 6,250 short calls and 6,250 long puts. Pursuant to proposed Section 33(b)(3)(A)(6)(b)(6), the options comprising the collar in excess of the applicable basic position limit (*i.e.*, 4,500) must be hedged on a one-for-one basis with 450,000 shares. The total number of allowable option contracts on the same side of the market in this example would be 13,500.

C. An investor is short 6,500 calls (4,500 pursuant to the position limit and 2,000 pursuant to the hedge exemption) and long 200,000 shares of stock. An OTC collar consisting of 2,500 short calls and 2,500 long puts may be established. Pursuant to proposed Section 33(b)(3)(A)(6)(b)(6), the options comprising the collar in excess of the applicable basic position limit (*i.e.*, 4,500) must be hedged on a one-for-one basis with an additional stock position of 250,000 shares. The total number of allowable option contracts on the same side of the market in this example would be 11,500.

D. An investor is short 9,000 calls (4,500 pursuant to the position limit and 4,500 pursuant to the hedge exemption) and long 450,000 shares of stock. An OTC collar may not be established since the investor has already reached the maximum allowable position limit.

III. Commission Findings and Conclusions

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange, and, in particular, the requirements of Section 6(b)(5) of the Act. Specifically, the Commission believes the conditions and limitations contained in the proposal strike a reasonable balance between the need to facilitate legitimate hedging needs of market participants and the need to have rules in place that do not compromise the regulatory purposes served by the equity option position limit rules. In particular, because the conditions and limitations for the OTC Collar Aggregation Exemption effectively provide that neither leg of the OTC collar can be in-the-money at the time the collar is established and that no more than one leg of the collar can ever be exercised throughout the term of the collar, the Commission does not believe that the larger options position resulting from the proposed non-aggregation of short (long) calls and long (short) puts for the hedge exemption portion of the position limit pursuant to the OTC Collar Aggregation

Exemption will increase the potential for market manipulation or disruption.¹¹

In addition, even though the conventional options positions involved in a particular OTC collar transaction do not have to be aggregated (if the collar meets the standards for the aggregation exemption), the collar position must be aggregated with all other standardized and conventional options on the same side of the market overlying the same security. In this respect, the Commission notes that while the NASD's proposal does not change the recognized position limit levels (*i.e.*, 4,500, 7,500, 10,500), it does alter the manner in which contracts are aggregated for position limits purposes, with the net result being an increase in certain situations in the number of contracts an investor may hold on the same side of the market from 9,000 to 13,500 (assuming a position limit of 4,500). While the maximum number of contracts an investor may hold is effectively increased, the proposal's requirements ensure that the amount of stock that may be controlled by an investor's option position is not increased. Instead, the proposal merely facilitates the use of an OTC collar by not aggregating the positions for determining the number of contracts pursuant to the hedge exemption. To the extent that investors have greater latitude to use a collar for hedging purposes, the proposal will enhance investors' risk management of stock positions.¹²

The Commission also believes that the larger options positions available by virtue of the proposal will not result in disruptions to the underlying stock market due to the conditions and limitations that must be met to be eligible for the aggregation exemption, and the NASD's surveillance program. In this connection, the Commission notes the NASD will monitor the use of the OTC Collar Aggregation Exemption to ensure that NASD members are complying with the requirements of the exemption.

The Commission finds good cause for approving Amendment No. 2 to the proposed rule change prior to the thirtieth day after the date of publication of notice of filing thereof in

¹¹ Furthermore, in order to ensure that the positions covered by this proposal are maintained in a collar transaction, the proposal requires that all of the conventional options comprising the OTC collar must be European-style and expire on the same date.

¹² As noted above, the non-aggregation of collar positions only applies to positions established pursuant to the existing hedge exemption. See *supra* note 10.

the **Federal Register**. Amendment No. 2 has the effect of limiting and clarifying the maximum number of contracts that may comprise a particular OTC collar established pursuant to the OTC Collar Aggregation Exemption, and as a result, should further reduce any speculative or manipulative impact caused by the net increase in the number of options held by an investor. Therefore, the Commission believes there is good cause to approve Amendment No. 2 to the proposal on an accelerated basis.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 2. 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 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 NASD. All submissions should refer to the file number in the caption above and should be submitted by July 19, 1995.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,¹³ that the proposed rule change (SR-NASD-94-60) is approved, as amended.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁴

Margaret H. McFarland,
Deputy Secretary.

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Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to the Adjustment of Open Orders

June 21, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934

¹³ 15 USC 78s(b)(2) (1988).

¹⁴ 17 CFR 200.30-3(a)(12) (1994).