office of NSCC. All submissions should refer to File No. SR–NSCC–95–07 and should be submitted by August 15, 1995.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.[7]

Margaret H. McFarland,

Deputy Secretary.

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[Release No. 34–35982; File No. SR–OCC–95–03]

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving a Proposed Rule Change Relating to OCC's Exercise-by-Exception Procedures Applicable to Expiring Index Options

July 18, 1995.

On February 16, 1995, The Options Clearing Corporation (''OCC'') filed with the Securities and Exchange Commission (''Commission'') a proposed rule change (File No. SR–OCC–95–03) 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 April 11, 1995.[2] No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description of the Proposal

The purpose of the proposed rule change is to modify the exercise threshold for expiring index option contracts, including American,[3] European,[4] and Capped [5] Quarterly Index Expiration option contracts, carried in a clearing member's customer account in connection with OCC's exercise-by-exception (''ex-by-ex'') processing procedures. The ex-by-ex exercise threshold used for flexibility structured index options is not effected by the rule change.

Ex-by-ex processing presumes that clearing members desire to exercise all options that are in-the-money by a specified threshold immediately prior to expiration. Accordingly, all options subject to ex-by-ex processing are identified as being in-the-money, at-the-money, or out-of-the-money in a report provided to each clearing member through OCC's Clearing/Management and Control System (''C/MACS'') [6] or by hard copy on each expiration date. After receipt and review of its report, each clearing member resubmits its report to OCC reflecting that the clearing member is instructing OCC to exercise all options that are in-the-money by the certain threshold amount. However, the clearing member can issue contrary instructions (''Contrary Exercise Advice'') to OCC by notating on the report additional contracts it desires to exercise and contracts that are in the money by the threshold amount that it does not want exercised.

OCC's Rules currently specify two ex-by-ex processing thresholds for index options.[7] The first threshold applies to index options carried in clearing members' customers' accounts, and the second threshold applies to index options carried in all other clearing members' accounts.[8] The current aggregate price threshold for customer positions is $25.00 per index option contract, and the aggregate price threshold for all other positions is $1.00 per index option contract. OCC's rule change reduces the aggregate price threshold for customer positions to $1.00 per index option contract. Now, any index option contract position, whether carried in clearing members' customers' accounts or in any of their other accounts, in-the-money by that amount or more, will be exercised immediately prior to expiration unless the clearing member submits a timely, contrary instruction to OCC. The proposed change to the threshold for ex-by-ex processing of certain index options carried in customers' accounts will not affect clearing members' obligations to their customers or correspondent brokers, which are determined by contract and by generally applicable principles of law.

II. Discussion

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.[9] As discussed below, the Commission believes that OCC's proposed rule change is consistent with this obligation because it should facilitate the prompt and accurate clearance and settlement of index options transactions by providing promptness and precision in the exercise of certain in-the-money index options.

The rule change should assure that certain customer-held index option contracts that are in-the-money by $1 or more will not go unexercised unless the clearing member provides contrary exercise advice. By lowering the ex-by-ex threshold for index option contracts carried in customer accounts from $25 to $1, OCC has reduced the burden placed on clearing members to provide exercise advice on index options in-the-money by $1 or more that are due to expire. Reducing the ex-by-ex processing threshold to $1 per index option contract will mean that clearing members will have to manually identify for exercise only those customer-held index option contracts that are in-the-money by less than $1.00 per contract; therefore, the cost associated with manually exercising customer-held index option contracts should be reduced. The proposal also should reduce the risk that a clearing member will fail to exercise a customer-held index option because under the new lower threshold only those options that are in-the-money by less than $1.00 will not be exercised.[10]

Originally, the $25 threshold was established because of the anticipation of transaction costs related to the exercise and settlement of index option contracts. Because index options are cash settled and the exercise fees for such options either do not exist, are waived, or are not expected to exceed the exercise proceeds, OCC believes that a lower ex-by-ex threshold can be applied and that its clearing members will not charge a fee for the cash settlement of an index option where a customer will be left with a loss.

III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements Section 17A(b)(3)(F) of the Act and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR–OCC–95–03) be, and hereby is, approved.

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[7] 17 CFR 200.30-3(a)(12) (1994).

[1] 15 U.S.C. 78s(b)(1) (1988).

[2] Securities Exchange Act Release No. 35566 (April 5, 1995), 60 FR 18435.

[3] OCC defines the term ''American'' option to mean an option contract that may be exercised at any time from its commencement time until its expiration.

[4] OCC defines the term ''European'' option to mean an option contract that may be exercised only on its expiration date.

[5] OCC defines the term ''Capped'' option to mean an option contract in a series which has a cap price at which all options in such series will be automatically exercised and which otherwise may only be exercised on its expiration date.

[6] C/MACS is an on-line, menu-driven system that allows OCC member firms to access or input trade information directly from or to OCC's clearing systems.

[7] Different ex-by-ex thresholds are applied to equity options.

[8] OCC Rule 1804(a) and (b).

[9] 15 U.S.C. 78q–1(b)(3)(F) (1988).

[10] As discussed earlier, clearing members can issue Contrary Exercise Advice instructions to exempt specified customer-held index option contracts from ex-by-ex processing.