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 will also be available for inspection and copying at the principal office of the Chicago Stock Exchange. All submissions should refer to File No. SR-CHX-95-2 and should be submitted by February 15, 1995.

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

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95–1784 Filed 1–24–95; 8:45 am] BILLING CODE 8010–01–M

[Release No. 34–35235; File No. SR–NASD– 94–78]

Self-Regulatory Organizations; Notice of Filing of a Proposed Rule Change by the National Association of Securities Dealers, Inc., Relating to Exercise Cut-Off Procedures for Expiring Equity Options Contracts

January 18, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on December 23, 1994, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the NASD. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The NASD proposes to amend Section 63 of the NASD's Uniform Practice Code ("Practice Code") relating to the exercise of expiring standardized equity options contracts. The text of the proposed rule change is available at the Office of the Secretary, NASD, and at the Commission.

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 IV 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 the Statutory Basis for, the Proposed Rule Change

Currently, with regard to expiring standardized equity options, Section 63 of the Practice Code provides that NASD members and their customers are required to indicate their exercise decisions to clearing members no later than 5:30 p.m., E.S.T., on the business day immediately prior to the expiration date of the options ("Exercise Cut-Off Time").¹ this is the latest time by which an exercise instruction² may be: (1) Prepared by a clearing member for positions in its proprietary trading account; (2) accepted by a clearing member from a non-clearing member; or (3) accepted by a member from any customer.3

The only exemptions to the Exercise Cut-Off Times contained in Section 63 of the Practice Code are: (1) To remedy mistakes or errors made in good faith; (2) to take appropriate action as the result of a failure to reconcile an unmatched option transaction; (3) where exceptional circumstances relating to a customer's or member's

² For customers, an exercise instruction is a notice delivered to a member to exercise an option. for a clearing member of The Options Clearing Corporation ("OCC") or a market maker or floor broker on a national options exchange, an exercise instruction is a notice to OCC to exercise an option that would not be automatically exercised pursuant to OCC's exercise-by-exception procedure ("OCC Rule 805"), or not to exercise an option that would otherwise be automatically exercised pursuant to OCC Rule 805. See infra note 6. The OCC has separate rules regarding cut-off time by which exercise notices must be delivered to OCC by OCC clearing members. The proposed rule change does not in any way affect OCC rules.

³ In most cases, exercise instructions are electronically transmitted to OCC clearing members through the Clearing Management and Control System ("C/MACS").

ability to communicate exercise instructions to a member (or a member's ability to receive such exercise instructions) prior to the Exercise Cut-Off Time warrant such action; and (4) with respect to options contracts in an account maintained for another member in which only positions of customers of such other member are carried. Members are required to prepare a memorandum of every exercise instruction received from a customer stating the time when such instruction was received. In addition, in the event a member receives and acts on an exercise instruction pursuant to one of the exceptions noted above, the member must prepare a memorandum setting forth the circumstances giving rise to the exception. If the member is relying on either the first or the third exception described above, the member must promptly file a copy of the memorandum with the NASD.

Thus, it is presently a violation of Section 63 of the Practice Code for clearing members to accept exercise instructions after the Exercise Cut-Off Time, except in reliance on one of the exceptions noted above. Because exercise instructions are submitted to the clearing members, without having the audit trail pass directly through the NASD or the particular options exchange(s) trading the expiring option, it is difficult for the NASD to surveil for violations of Section 63. In fact, there have been some situations where members have either delayed making exercise decisions until after the Exercise Cut-Off Time in anticipation of the release of significant news concerning a particular underlying company or, havig made exercise decisions prior to the Exercise Cut-Off Time, changed these decisions based upon such news. In one notable situation, the NASD notes that certain firms that anticipated the release of material news regarding a particular company allegedly delayed making their exercise decisions until after the Exercise Cut-Off Time, causing firms who claimed to have been disadvantaged by such conduct to commence a series of highly publicized arbitration proceedings and lawsuits.⁴

Accordingly, in order to enable the options exchanges and the NASD to determine whether options holders have made their final exercise decisions no later than the prescribed Exercise Cut-Off Time and not on the basis of market developments occurring after the Exercise Cut-Off Time, the NASD proposes to amend Section 63 of the

¹ Generally, the rules of the options exchanges provide that equity options may be traded up until the close of business on the last business day before expiration, which is generally the third Friday of the expiration month ("Expiration Friday"), See, e.g., CBOE Rule 11.1 and Phlx Rule 1042.

⁴See, e.g., *In re Farmers Group Stock Options Litigation*, Master File No. 88–4994 (E.D.Pa).