specifications for the XOC remain unchanged.

The proposed rule change appeared in the Federal Register on November 14, 1995.[4] No letters were received in response to the Commission's solicitation for comment on the proposed rule filing.[5] This order approves the Phlx's proposal.

II. Background and Description

The Phlx began trading the XOC in 1985.[6] The Index was created with a value of 150 on its base date of September 28, 1984, which rose to 548 in June 1994, and to 700 in June 1995. On September 14, 1995, the Index value was 868. Thus, the Index value has increased significantly, especially during the last year. Consequently, the premium for XOC options has also risen.

As a result, the Phlx proposes to conduct a ''two-for-one split'' of the Index, such that the value will be reduced by one-half. In order to account for the split, the number of outstanding XOC contracts will be doubled, such that for each XOC contract currently held, the holder will receive two contracts at the reduced value, with a strike price of one-half the original strike price. For instance, the holder of an XOC 800 call will receive two XOC 400 calls. In addition, the Phlx will double to the position and exercise limits applicable to the XOC, from 17,000 contracts to 34,000 contracts until the last expiration then trading, which is the June 1996 expiration.[7] According to the Phlx, this procedure is similar to that employed with equity options when the underlying security is subject to a two-for-one stock split, as well as that used for the recent split of the Phlx's Semiconductor Index.[8]

In conjunction with the split, the Exchange will list strike prices surrounding the new, lower Index value, pursuant to Phlx Rule 1101A. The Phlx will announce the effective date by way of an Exchange memorandum to its membership, which will also serve as notice of the strike price and position limit changes.[9]

According to the Phlx, the purpose of the proposal is to attract additional liquidity to the product in those series that public customers are most interested in trading. For example, according to the Phlx, a near-term, at-the-money call option series currently trades at approximately $1,200 per contract. After the Index split, the same option series (once adjusted), with all else remaining equal, could trade at approximately $600 per contract. Thus, while certain investors and traders may currently be impeded from trading at such levels, a reduced Index value should encourage additional investor interest.

The Phlx believes the XOC options provide an important opportunity for investors to hedge and speculate upon the market risk associated with the underlying over-the-counter stocks. By reducing the value of the Index such investors will be able to utilize this trading vehicle, while extending a smaller outlay of capital. According to the Phlx, this should attract additional investors, and, in turn, create a more active and liquid trading environment.

III. Summary of Comments

The Phlx received one comment letter opposing the proposed rule change from a financial planner at Smith Barney Shearson.[10] The issues raised therein and the Phlx's response thereto [11] are discussed below.

According to the commenter, one of the primary inducements to trading the Index is its volatility. If the Index is split in half, however, the commenter believes that investors will be unnecessarily forced to trade twice as many contracts in order to maintain their current degree of leverage. In response, the Phlx stated that a lower priced, less volatile Index will better serve the needs of investors as the Exchange will be able to more timely update quotes, particularly during periods of active market conditions.

The commenter also opposes the proposed rule change because he believes that splitting the Index will reduce its value to an inappropriately low level. In this regard, the commenter suggests alternative split levels (*e.g.*, a 4 for 3 split, or a 3 for 2 split) as a less problematic approach. In this manner, according to the commenter, the Index will retain a greater percentage of its current value. The Phlx responded that splitting the Index in a manner other than two-for-one would result in unnecessary calculations and adjustments to the divisor, position limits, and strike prices and would thereby create investor confusion and excessive system demands.

Finally, the commenter suggests that the Exchange postpone the splitting of the Index to provide investors with a reasonable amount of time to adjust their positions as a result of the proposed rule change. In this regard, the Commission notes that to avoid investor confusion the Phlx has stated that it intends to provide market participants with adequate notice of the change to the Index value.[12]

IV. Discussion

After careful consideration of the comment letter and the Phlx's response thereto, the Commission has decided to approve the proposed rule change. For the reasons discussed below, the Commmission 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, with the requirements of Section 6(b).[13] Specifically, the Commission believes that the proposal is consistent with the Section 6(b)(5) requirement to protect investors and the public interest and to remove impediments to a free and open securities market. By reducing the value of the Index, the Commission believes that a broader range of investors will be provided with a means of hedging their exposure to the market risk associated with the underlying over-the-counter stocks. Similarly, the Commission believes that reducing the value of the Index could help attract additional investors, thus creating a more active and liquid trading market.

The Commission also believes that the Phlx's position and exercise limits and strike price adjustments are appropriate and consistent with the Act. In this regard, the Commission notes that the position and exercise limits and strike price adjustments are identical to the

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[4] See Securities Exchange Act release No. 36460 (November 6, 1995), 60 FR 57256 (November 14, 1995).

[5] The Commission notes, however, that the Phlx forwarded to the Commission one comment letter it received prior to filing this rule proposal. This letter and the Phlx's response is discussed below. See *infra* note 10 and accompanying discussion.

[6] See Securities Exchange Act Release Nos. 21576 (January 18, 1985), 50 FR 3445 (January 24, 1985); and 22044 (May 17, 1985), 50 FR 21532 (May 24, 1985) (File No. SR–Phlx–84–28).

[7] Separately, the Exchange is proposing to increase the XOC position and exercise limits to 25,000 contracts. *See* SR–Phlx–95–38.

[8] See Securities Exchange Act Release No. 35999 (July 20, 1995), 60 FR 38387 (July 26, 1995) (File No. SR–Phlx–95–41).

[9] In this regard, the Commission notes that in a memorandum dated November 20, 1995, the Phlx provided notice to its members and member organizations of its intention to reduce the value of the XOC by one-half.

[10] See letter from Barry J. Weisberg, Vice President, Smith Barney Shearson, Inc., to Andy Kolinsky, Vice President, Phlx, dated August 1, 1995. The Commission notes that the commenter also raised other concerns regarding the trading of the XOC unrelated to the rule proposal which are not discussed herein.

[11] See letter from Gerald D. O'Connell, First Vice President, Market Regulation and Trading Operations, Phlx, to Barry J. Weisberg, Vice President, Smith Barney Shearson, Inc., dated November 20, 1995.

[12] See supra note 9.

[13] 15 U.S.C. 78f(b) (1988).