

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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**Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Incorporated, Relating to Warrants on the Japanese Export Stock Index**

August 21, 1995.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 7, 1995, the Chicago Board Options Exchange, Incorporated ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 Exchange proposes to list and trade warrants on the Japanese Export Stock Index ("Japan Export Index" or "Index"). The text of the proposed rule change is available at the Office of the Secretary, the Exchange, 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 Exchange included statements concerning the purpose of and basis for the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Section (A), (B), and (C) below, of the most significant aspects of such statements.

**(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

The Exchange represents that it is permitted to list and trade index warrants under CBOE Rule 31.5(E). The Exchange is now proposing to list and trade index warrants based upon the Japan Export Index. The Exchange further represents that the listing and trading of Index warrants will comply in all respects with CBOE Rule 31.5(E), as discussed below.

**Index Design**

The Japan Export Index is an "equal dollar weighted" broad-based index comprised of the stocks of 40 of the largest Japanese export companies, as measured by total yen-denominated export revenue, listed on the Tokyo Stock Exchange ("TSE").<sup>3</sup> At the outset each of the component securities comprising the Index will be equally represented. Thus, on the day warrants on the Index are priced for sale to the investing public, each component security will represent 2.5% of the original Index value.

The Japan Export Index stocks are drawn from a broad base of industries and are representative of the industrial composition of the broader Japanese equity market. Business sector representation in the Index as of June 30, 1995, was as follows: (1) Autos and auto parts (25%) (10 Issues); (2) Electric Machinery—diversified (22.5%) (9 issues); (3) Consumer Electronics (20%) (8 issues); (4) Iron and Steel (7.50%) (3 issues); (5) Precision instruments (7.5%) (3 issues); (6) Shipbuilding (5%) (2 issues); (7) Chemicals (5%) (2 issues); (8) Machinery (2.5%) (1 issue); (9) Computers and semiconductors (2.5%) (1 issue); and (10) Services (2.5%) (1 issue).

As of June 30, 1995, the CBOE represents that the 40 stocks contained in the Index range in market capitalization from \$1.59 billion to \$74.76 billion. The median capitalization of the component securities in the Index was \$7.6 billion.

<sup>3</sup>The components of the Index are as follows: Aiwa; Bridgestone Corp.; Canon; Casio Computer; Citizen Watch; Fuji Heavy Inds.; Fuji Photo Film; Hitachi; Honda Motor; Isuzu Motor; Kawasaki Heavy Ind.; Kawasaki Steel; Komatsu Ltd.; Konica Corp.; Kyocera Corp.; Kyushu Matsushita; Matsushita Eltr.; Matsushita Elect I; Mazda Motor; Mitsubishi Heavy; Mitsubishi Motors; NEC; Nikon Corp.; Nintendo; Nippon Steel; Nissan Motor; OKI Electric Ind.; Pioneer Eltr.; Ricoh Co. Ltd.; Sanyo Electric; Sega Enterprises; Sharp Corp.; Sony; Sumitomo Mtl. Ind.; Suzuki Motor; TDK Corporation; Toshiba; Toyota Motor; Victor Co. of Japan; and Yamaha Motor.

Total market capitalization for the Index was approximately \$451 billion.<sup>4</sup>

**Calculation**

The Index will be calculated by determining a multiplier such that each security will represent an equal percentage (2.5%) of the Index on the date the warrants are priced for initial sale to the public. The Index value for any day will equal the sum of the products of the most recently available market prices and the applicable multipliers for the component securities. The Index value will be set equal to 100 on the date the warrants are priced for initial offering to the public. In the event that a security does not trade on a given day, the previous day's last sale price is used for purposes of calculating the Index. In the event that a given security has not traded for more than one day, then the last sale price on the last day on which the security was traded will be used.

**Maintenance**

The Index will be calculated by the Exchange based on closing prices on the TSE each day and will be disseminated before the opening of trading via Options Price Reporting Authority. The Index will be rebalanced on the last trading day of the year such that the components again represent an equal percentage (2.5%) of the Index. The components of the Index will remain unchanged unless it becomes necessary to remove a component security due to a merger, takeover, or some other event where the issuer of the component security is not the surviving entity. If a component security is removed, another security will be added to preserve the character of the Index. To ensure continuity in the Index's value, the index divisor will be adjusted to reflect, among other things, certain rights issuances, stock splits, rebalancing, and component security changes.

**Index Warrant Trading**

The proposed warrants will be direct obligations of their issuer subject to cash-settlement in U.S. dollars, and either exercisable throughout their life (i.e., American-style) or exercisable only immediately prior to their expiration date (i.e., European-style). Upon exercise, the holder of a warrant structured as a "put" would receive payment in U.S. dollars to the extent that the index value has declined below a pre-stated cash settlement value. Conversely, upon exercise, the holder of a warrant structured as a "call" would

<sup>4</sup>Based on the exchange rate of 85 yen/US\$ 1 prevailing on June 30, 1995.

<sup>16</sup> 17 CFR 200.30-3(a)(12) (1994).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

receive payment in U.S. dollars to the extent that the index value has increased above the pre-stated cash settlement value. Warrants that are "out-of-the-money" at the time of expiration will expire worthless.

#### *Warrant Listing Standards and Customer Safeguards*

The Exchange has established listing standards for index warrants which are contained in CBOE Rule 31.5E.<sup>5</sup> The Exchange also has established certain sales practice rules for the trading of index warrants which are contained in Chapter IX of the Exchange's Rules. The Exchange represents that the listing and trading of index warrants on the Japan Export Index will be subject to these guidelines and rules.

The Exchange has submitted to the Commission a proposed rule change to amend its listing criteria for stock index warrants.<sup>6</sup> The Exchange represents that the Generic Warrant Listing Standards will be applicable to the listing and trading of currency and index warrants generally, including Japan Export Index warrants. If the listing of Japan Export Index warrants is approved prior to Commission approval of the Generic Warrant Listing Standards, the CBOE represents that it will require that (1) these warrants be sold only to accounts approved for the trading of standardized options<sup>7</sup> and (2) index options margin will be applied.<sup>8</sup> Finally, prior to the commencement of trading, the Exchange will distribute a circular to its membership calling attention to certain compliance responsibilities when handling transactions in the Japan Export Index warrants.<sup>9</sup>

<sup>5</sup> Currently, Rule 31.5E provides that: (1) Issues of warrants must substantially exceed the Exchange's criteria for the listing of equity issues under CBOE Rule 31.5A and have assets in excess of \$100 million; (2) particular warrant issues must have at least (i) one million warrants outstanding, (ii) a principal amount/aggregate market value of \$4 million, and (iii) 400 public holders; and (3) warrant issues must have a term of one to five years from the date of issuance.

<sup>6</sup> These proposed standards will govern all aspects of the listing and trading of index warrants, including, position and exercise limits, reportable positions, automatic exercise, settlement, margin, and notification of early exercise. See Securities Exchange Act Release No. 35178 (December 29, 1994), 60 FR 2409 (January 9, 1995) (notice of File No. SR-CBOE-94-34) ("Generic Warrant Listing Standards").

<sup>7</sup> See CBOE Rule 9.7.

<sup>8</sup> Telephone conversation between Eileen Smith, Director, Product Development, Research Department, CBOE, and John Ayanian, Attorney, Office of Market Supervision ("OMS"), Division of Market Regulation ("Market Regulation"), Commission, on August 17, 1995.

<sup>9</sup> *Id.*

#### *Surveillance*

The Exchange expects to apply its existing index warrant surveillance procedures to Japan Export Index warrants. The Exchange has a market surveillance agreement with the Tokyo Stock Exchange ("TSE") which was obtained in connection with CBOE trading of options of the Nikkei 300 Index ("Nikkei 300"). Approximately 73% of the stocks in the Index are also components of the Nikkei 300 Index. The Exchange notes that the TSE is under the regulatory oversight of the Ministry of Finance ("MOF") and believes that the ongoing oversight of all securities trading activity on the TSE by the MOF will help to ensure that trading of the component securities included in the Japan Export Index will be appropriately monitored. Finally, the Exchange is aware of a Memorandum of Understanding ("MOU") between the Commission and the MOF that provides a framework for mutual assistance in investigatory and regulatory matters.

The Exchange believes that the proposed rule change is consistent with Section 6 of the Act, in general, and furthers the objectives of Section 6(b)(5) of the Act, in particular, in that it is designed to facilitate transactions in securities and to remove impediments to and perfect the mechanism of a free and open market and facilitate transactions in securities because the Index warrants will provide investors a means by which to hedge existing investments in the Japanese equity market.

#### *(B) Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition.

#### *(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others*

No written comments were solicited or received with respect to the proposed rule change.

#### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing. 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 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 CBOE. All submissions should refer to SR-CBOE-95-41 and should be submitted by September 18, 1995.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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#### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Extending the Pilot Program for Equity and Index Option Specialist Enhanced Parity Split Participations**

August 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 August 3, 1995, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared

<sup>10</sup> 17 CFR 200.30-3(a)(12).