

Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder² to grant authority to NASD staff to adjust the fidelity bond required of a member in certain circumstances. By letter dated May 27, 1998, the Association filed Amendment 1 to the proposed rule change.³ The proposed rule change and Amendment 1 were published for comment in the **Federal Register** on June 10, 1998.⁴ No comments were received. This order approves the proposal.

II. Description of the Proposal

Rule 3020 of the Conduct Rules of the NASD specifies that members are required to maintain fidelity bonds to insure against certain losses and the potential effect of such losses on firm capital. The rule applies to all members with employees who are required to join the Securities Investor Protection Corporation and who are not covered by the fidelity bond requirements of a national securities exchange. The amount of coverage a member is required to maintain is linked to the member's net capital requirements under Rule 15c3-1 under the Act.⁵ Under paragraph (c) of Rule 3020, each member must annually review the adequacy of its fidelity bond coverage and maintain coverage that is adequate to cover its highest net capital requirement during the preceding 12 months. For example, even if a full-service member divests its clearing business, so that it no longer holds customer funds or securities, it would still be required to maintain bond coverage that is based on the higher net capital requirement that applied during the preceding year.

The proposed rule change would amend Rule 3020 to permit staff of NASD Regulation, Inc., ("NASD Regulation") to adjust the fidelity bond requirements to reflect changes in a member's business. Requests for exemption would be considered under recently adopted Procedures for Exemption in the 9600 Series of Rules in the Code of Procedure. Under the procedures, NASD Regulation staff issues written determinations that are subject to review by the National Adjudicatory Council.

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of Section 15A(b)(6) of the Act,⁶ which provides, among other things, that the rules of a national securities association be designed to protect investors and the public interest.⁷ The Commission believes that the proposed rule change will allow members to be relieved from maintaining unnecessarily high fidelity bond coverage without compromising investor protection.

The rule change applies a "good cause" standard that will require a member to demonstrate that a modification from the bonding requirement is justified by the level of loss exposure that may be expected from the member. The premiums are changed from time to time to reflect changes in loss experience and to ensure that sufficient funds are available to pay any losses reported to the insurer. NASD Regulation represents that it will apply this authority only where it is clear that an exemption will not have any unintended impact on the insurance pool, and the modified coverage will adequately protect the member against potential losses. In addition, the proposed rule change will permit NASD Regulation staff to include conditions in an exemption to ensure that any subsequent increase in capital requirements is accompanied by a corresponding increase in coverage.

IV. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,⁸ that the proposed rule change (SR-NASD-98-33) is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁹

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40205; File No. SR-OCC-97-12]

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving a Proposed Rule Change Regarding Initial and Minimum Net Capital Requirements for Futures Commission Merchants

July 15, 1998.

On July 15, 1997, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change (File No. SR-OCC-97-12) 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 February 19, 1998.² No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description

The proposed rule change amends OCC's initial and ongoing minimum net capital requirements and early warning notice provisions to establish additional requirements for clearing members that are also registered futures commission merchants ("FCMs"). Currently, OCC's rules require its members to satisfy initial and ongoing minimum net capital requirements of \$1,000,000 and \$750,000, respectively.³ Under the proposed rule change, the initial and ongoing minimum net capital of OCC members that are also FCMs must exceed the greater of the following standards: OCC's current initial and ongoing minimum net capital requirements or that required by the clearing organization of the FCM member's designated self-regulatory organization ("DSRO").⁴

The proposed rule change also modifies OCC's early warning notice provisions to require OCC members that are also FCMs to notify OCC if that member's net capital falls below OCC's requirements or if its net capital falls below the minimum net capital required by the clearing organization of the FCM member's DSRO.

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 39648 (February 11, 1998), 63 FR 8509.

³ OCC Rules 301 and 302.

⁴ Robert C. Rubenstein from OCC in a letter dated September 3, 1997, to the Commission stated that according to OCC, the terms clearing organization and SRO shall have the meanings ascribed to them in the General Regulation of the Commodity Exchange Act, 17 CFR 1.3(d) and 17 CFR.1.3(ff) (1) and (2).

¹ 15 U.S.C. 78s(b)(1) (1994).

² 17 CFR 240.19b-4 (1997).

³ Amendment 1 revised the last sentence of proposed new paragraph (c)(4) of Rule 3020. See Letter from Elliott R. Curzon, Assistant Chief Counsel, NASD Regulation, to Lisa Henderson, Attorney, SEC, dated May 27, 1998.

⁴ Securities Exchange Act Release No. 40065 (June 3, 1998), 63 FR 31819.

⁵ 17 CFR 240.15c-1 (1997).

⁶ 15 U.S.C. 78f(b)(6).

⁷ In approving this rule, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁸ 15 U.S.C. 78s(b)(2).

⁹ 17 CFR 200.30-3(a)(12).

II Discussion

Section 17A(b)(3)(F) of the Act⁵ requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible. The Commission believes that the proposed rule change is consistent with OCC's obligations under the Act because the proposed rule change increases the effectiveness of OCC's financial surveillance of its clearing members in situations where the clearing member's net capital falls below that level required by its futures clearing organization.

Many of OCC's clearing members are also registered as FCMs under the Commodity Exchange Act and as such are subject to the financial reporting requirements and the early warning notice requirements of the Commodity Futures Trading Commission and of commodity DSROs. Because of differences in the initial and ongoing minimum net capital requirements used by the commodity regulatory organizations and those used by the securities regulatory organizations, a clearing member could fail to meet the net capital requirements of its DSRO and still satisfy the net capital requirements established by OCC. Consequently, a situation could occur where an FCM clearing member is required to give early warning notice to its commodity regulatory authority but nothing currently would require the clearing member to give notice to OCC. As a result, OCC could continue to clear trades without notice for a clearing member that may or may not be able to satisfy its financial obligations.

Therefore, requiring a clearing member to satisfy the higher applicable net capital standard and to provide OCC with early warning notices when it fails to meet the net capital requirements set by its DSRO or by OCC should assist OCC in assessing the ongoing creditworthiness of its clearing members and also should help OCC to safeguard securities and funds in OCC's custody or control.

III Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A 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-97-12) be and hereby is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.⁶

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-40209; File No. SR-OCC-97-13]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Relating to Adjustments to Exercise Prices

July 15, 1998.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on September 22, 1997, the Options Clearing Corporation ("CCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change (File No. SR-OCC-97-13) as described in Items I and II below, which items have been prepared primarily by OCC. The Commission is publishing this notice and order to solicit comments on the proposed rule change from interested persons and to grant accelerated approval of the proposal.

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

The purpose of the proposed rule change is to amend OCC's by-laws regarding the adjustment of exercise prices. Specifically, adjustment of exercise prices will be rounded to the next nearest trading increment as specified by the primary market for the underlying security.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, OCC 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. OCC has prepared summaries, set forth in sections A, B,

and C below, of the most significant aspects of such statements.²

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

Under the proposed rule change, OCC will amend Article VI, Section 11(i) of its by-laws to provide for the rounding of adjustments of exercise prices to the nearest "trading increment" for the underlying security, as fixed by the primary market for the security.³ Currently, OCC rounds adjustments to exercise prices to the nearest eighth of a dollar. The securities industry has moved from quoting prices in eighths of a dollar ("eighths") to sixteenths of a dollar ("sixteenths") and is moving towards quoting prices in decimals. Therefore, OCC believes that the adjustment provisions of its by-laws require amendment. Amending its by-laws to provide for rounding to the nearest trading increment will accommodate the interim change to pricing in sixteenths and any final change to decimal pricing.

The proposed rule change also will add a new interpretation .09 to Article VI, Section 11 expressly authorizing OCC's securities committee to adjust exercise prices of outstanding options to a new trading increment (e.g., decimals) to correspond to a change in the trading increment in the underlying security in its primary market. The rule change will not mandate such adjustments, but it will give clear authority to the committee to adjust exercise prices if the committee deems such action to be appropriate in light of the factors cited in Article VI, Section 11(b) of OCC's by-laws.

Currently, exercise prices of newly introduced options series are expressed in half dollar increments. However, there generally will be options series outstanding with exercise prices expressed in eighths or sixteenths as a result of previous adjustments. Eighths cannot be converted to fewer than three decimal places and sixteenths cannot be converted to fewer than four without rounding. As a result, the rule change will provide for rounding adjusted exercise prices to the nearest unit of the applicable trading increment or, where an exercise price is equidistant between two units, to the next lowest unit. Rounding would result in a small gain (\$0.25 per contract in the case of

² The Commission has modified the text of the summaries prepared by OCC.

³ The complete text of the amendments was submitted with OCC's rule filing and is available for inspection and copying at the Commission's Public Reference Room and through OCC.

⁵ 15 U.S.C. 78q-1(b)(3)(F).

⁶ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).