

or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act. For the reasons stated above, the Fund believes that the requested relief satisfies this standard.

### Applicant's Condition

The Fund agrees that the order granting the requested relief will terminate upon the effective date of a registration statement under the Securities Act of 1933 for any future public offering by the Fund of its common shares other than: (i) A non-transferable rights offering to shareholders of the Fund, provided that such offering does not include solicitation by brokers or the payment of any commissions or underwriting fee; and (ii) an offering in connection with a merger, consolidation, acquisition or reorganization; unless the Fund has received from the staff of the SEC written assurance that the order will remain in effect.

For the Commission, by the Division of Investment Management, under delegated authority.

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-41503; File No. SR-Amex-99-10]

### Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change and Amendment No. 1 Thereto by the American Stock Exchange LLC Relating to the Listing and Trading of Options on the Credit Suisse First Boston Technology Index

June 9, 1999.

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 March 10, 1999, the American Stock Exchange LLC ("Exchange" or "Amex") 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 by the Exchange. The Exchange filed with the Commission Amendment No. 1 to the proposal on April 15, 1999.<sup>3</sup> 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 proposed rule change, as amended.

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

The Exchange proposes to list for trading options on the Credit Suisse First Boston Technology Index ("Index"), a new index developed by Credit Suisse First Boston Corporation ("CSFB")<sup>4</sup> that measures the stock performance of companies primarily engaged in the computer and communications technology industry. In addition, the Exchange seeks to make two conforming changes to its rules. First, the Exchange proposes to amend Commentary .01 of Exchange Rule 901C, "Designation of Stock Index Options," to indicate that 90% of the Index's numerical value will be accounted for by stocks that meet the current criteria and guidelines set forth in Exchange Rule 915.<sup>5</sup> Second, the Exchange proposes to amend Exchange Rule 902C, "Rights and Obligations of Holders and Writers of Stock Index Option Contracts," to include CSFB in the disclaimer provisions of that rule.

### 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 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 III below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

First Boston Technology Index ("Index") and provided revised market and trading data for all component securities. In addition, the Exchange clarified the formula used to calculate the value of the Index and identified the sub-sectors that comprise the technology sector. The Exchange also described in greater detail the annual rebalancing process. See Letter from Scott G. Van Hatten, Legal Counsel, Derivative Securities, Exchange, to Richard Strasser, Assistant Director, Division of Market Regulation ("Division"), Commission, dated April 12, 1999 ("Amendment No. 1").

<sup>4</sup>In its filing, the Exchange characterized CSFB as a "leading global investment banking firm that provides comprehensive financial advisory, capital raising, sales and trading, and financial products for users and suppliers of capital around the world."

<sup>5</sup>Exchange Rule 915, "Criteria for Underlying Securities," contains the criteria that securities underlying options contracts must satisfy. See *infra* note 9 for a description of those criteria.

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

#### I. Purpose

The Exchange proposes to list for trading options on the Index. The Index is designed to reflect and measure the performance of companies engaged in the computer and communications technology industry. Each of the companies included in the Index derives more than 50% of its revenues from the computer and communications technology industry.<sup>6</sup> The Exchange believes that options on the Index will provide investors with an investment vehicle to participate in the appreciation of the component securities, and a means to reduce the risk involved in selecting individual securities in the Index.

The Exchange has represented that except for the Index's calculation methodology, which is modified equal-dollar weighted, the proposal meets all the criteria set forth in Commentary .02 of Exchange Rule 901C and the Commission's order approving that rule<sup>7</sup> (collectively, the "generic listing criteria").

#### a. Eligibility Criteria for Index Components

CSFB has established objective criteria to select companies for the Index. Specifically, companies eligible for inclusion in the Index will: (1) Derive more than 50% of their revenues from the computer and communications technology industry; (2) have a minimum market capitalization greater than \$500 million; and (3) have a

<sup>6</sup>Exhibit 3B to the Exchange's proposed rule change identifies the 75 companies making up the Index. The component companies are: ADA Telecommunications, Advanced Micro Devices, Altera, Amazon.com, Amdocs, America Online, Analog Devices, Apple Computer, Applied Materials, At Home, BMC Software, Broadcom, Cadence Design, Cisco Systems, Citrix Systems, 3Com, Compaq Computer, Computer Associates, Computer Sciences, Compuware, Dell Computer, Earthlink Network, eBay, Electronic Arts, Electronic Data Systems, EMC, E\*TRADE Group, First Data, Gartner Group, Gateway 2000, General Instrument, Hewlett-Packard, i2 Technologies, IBM, Ingram Micro, Inktomi, Intel, Intuit, KLA-Tencor, Lexmark International Group, Linear Technology, Lucent Technologies, Maxim Integrated Products, Microchip Technology, Micron Technology, Microsoft, Motorola, Network Associates, Newbridge Networks, Nokia, Northern Telecom, Novell, Oracle, Parametric Technology, PeopleSoft, QUALCOMM, Rambus, Sammina, SAP, Sapient, Seagate Technology, Siebel Systems, Solectron, STMicroelectronics, Storage Technology, Sun Microsystems, Tellabs, Teradyne, Texas Instruments, Uniphase, Unisys, Veritas Software, Vitesse Semiconductor, Xilinx, and Yahoo.

<sup>7</sup>See Securities Exchange Act Release No. 34157 (June 3, 1994), 59 FR 30062 (June 10, 1994).

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

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

<sup>3</sup>In Amendment No. 1, the Exchange updated the list of component securities for the Credit Suisse

minimum trading volume of 1,000,000 shares per month for the preceding three months. Of these candidate components, the 50 largest eligible companies measured by average market capitalization (determined using the number of shares outstanding on the last day of each December, and the average price per share for the month of December) are automatically included in the Index. The remaining 25 Index components are selected by CSFB from the universe of eligible stocks to ensure that the Index provides appropriate representation of the sub-sectors comprising the computer and communications technology sector.<sup>8</sup>

If addition to the selection criteria established by CSFB, the Exchange represents that the Index component securities will substantially comply with the generic listing standards found in Commentary .02 of Exchange Rule 901C. Specifically: (1) Each Index component security will have a minimum market capitalization of at least \$75 million and a trading volume in each of the last six months of not less than 1,000,000 shares; (2) at least 90% of the Index's numerical index value and at least 80% of the total number of component securities will meet the current criteria for standardized options trading set forth in Exchange Rule 915;<sup>9</sup> (3) each Index component security will be listed for primary market trading on the Exchange, the New York Stock Exchange, or through the facilities of the Nasdaq Stock Market and will be a reported security; and (4) no component security will represent more than 25% of the weight of the Index, and the five highest weighted component securities in the Index will not in the aggregate account for more than 50% of the weight of the Index.<sup>10</sup>

<sup>8</sup> CSFB has categorized the computer and communications technology sector into the following sub-sectors: computer software, semiconductor, telecommunications equipment, electronic production equipment, electronic data processing peripherals, diversified electronic products, recreational products, electronic components, investment banking, electronic data processing, catalogue, electronic components, and electronic distribution industries.

<sup>9</sup> The Exchange's options listing standards, which are uniform among the options exchanges, provide that a security underlying an option must, among other things, meet the following requirements: (1) the public float must be at least 7,000,000 shares; (2) there must be a minimum of 2,000 securityholders; (3) trading volume in the U.S. must have been at least 2.4 million shares over the preceding twelve months; (4) the market price per share must have been at least \$7.50 for a majority of the business days during the preceding three calendar months; and (5) the issuer must be in compliance with any applicable requirements of the Act. See Exchange Rule 915, "Criteria for Underlying Securities," Commentary .01.

<sup>10</sup> In its filing, the Exchange mistakenly stated that the five highest weighted component securities

#### b. Index Calculation

The Exchange will calculate the Index using a modified equal-dollar weighting methodology, which is designed to ensure that no single component or group of components dominates the Index. At the time of the initial balancing and each subsequent rebalancing, each of the 25 largest component securities (measured by unadjusted market capitalization) will be assigned a weighting of approximately 2.4% of the Index's total weight. Thus, in the aggregate, the 25 largest component securities will account for 60% of the Index's total weight. Each of the remaining 50 Index component securities will be assigned a weighting of approximately 0.8% of the Index's total weight, resulting in an aggregate weighting of 40% of the Index's total weight.

The Exchange believes that the modified equal-dollar weighting methodology allows the Index to more accurately reflect the investment performance of computer and communication technology-based securities. The Exchange further believes that although the weighting methodology provides for a higher weighting for the 25 largest capitalized components, the uniformly low percentage level of weighting for each security keeps those components from dominating the Index.

As of the close of trading on December 31, 1998, a portfolio of Index component stocks was established representing an investment of \$2.4 million in each of the 25 highest weighted securities in the Index and \$800,000 in each of the remaining 50 securities (rounded to the nearest whole share). The value of the Index equals the current market value (based on the U.S. primary market prices) of the sum of the assigned number of shares of each of the securities in the Index portfolio divided by the Index divisor. The Index divisor was initially determined to yield a benchmark value of 200.00 at the close of trading on December 31, 1998.

#### c. Maintenance of the Index

The Exchange will maintain the Index consistent with its original purpose to include companies that derive more than 50% of their revenue from the computer and communications technology industry. Further, the Exchange will maintain the Index in

the Index would not in the aggregate account for more than 60% of the weight of the Index. The Exchange has confirmed that the correct figure is 50%. Telephone conversation between Scott G. Van Hatten, Legal Counsel, Derivative Securities, Exchange, and Michael Loftus, Attorney, Division, Commission (May 27, 1999).

accordance with Exchange Rule 901C, Commentary .02 so that: (1) The Index is comprised of not less than 50 component securities and not more than 100 component securities (*i.e.*, the total number of Index component securities will not increase or decrease by more than one-third from the number of component securities in the Index at the time of its initial listing); (2) component securities constituting the top 90% of the Index, by weight, will each have a minimum market capitalization of \$75 million, and the component securities constituting the bottom 10% of the Index, by weight, will each have a minimum market capitalization of \$50 million; (3) 90% of the Index's numerical index value and at least 80% of the total number of components will meet the listing criteria for standardized options that appear in Exchange Rule 915;<sup>11</sup> (4) foreign country securities, or American Depositary Receipts ("ADRs") thereon, that are not subject to comprehensive surveillance agreements will not in the aggregate represent more than 20% of the weight of the Index; (5) all component securities will be listed on the Exchange, the NYSE, or Nasdaq (as National Market securities); (6) no component security will represent more than 25% of the weight of the Index, and the five highest weighted components will not in the aggregate account for more than 50% of the weight of the Index; and (7) the trading volume for each component security shall be at least 500,000 shares for each of the last six months or, for each of the lowest weighted components that in the aggregate account for no more than 10% of the weight of the Index, the monthly trading volume may be at least 400,000 shares for each of the last months.

The Exchange shall not open for trading any additional option series should the Index fail to satisfy any of the maintenance criteria set forth above unless such failure is determined by the Exchange not to be significant and the Commission concurs with that determination, or unless the continued listing of the index option has been approved by the Commission pursuant to Section 19(b)(2) of the Act.<sup>12</sup>

#### d. Rebalancing

The Exchange and CSFB will review the Index components at the end of each calendar year to ensure that the components continue to meet eligibility requirements and that the Index is representative of the computer and

<sup>11</sup> As part of its rule filing, the Exchange proposes to include this requirement in Commentary .01 of Exchange Rule 901C.

<sup>12</sup> 15 U.S.C. 78s(b)(2).

communications technology industry. Following the close of trading on the second Friday of January of each calendar year, the component shares included in the Index portfolio will be rebalanced by adjusting the number of whole shares for each component such that each component security again approximately represents its assigned weighting in the Index: either 2.4% or 0.8% of the Index's total weight.

At the time of the annual rebalancing, the Index components that continue to satisfy the Exchange's and CSFB's eligibility requirements are ranked in descending order by average market capitalization (determined using the shares outstanding on the last day in December and the average share price for the month of December). The 50 largest Index components that continue to meet all eligibility requirements automatically remain in the Index. The remaining Index components securities are evaluated, and removed if necessary, to ensure that the Index continues to accurately represent the sub-sectors of the technology industry and to allow for the addition of new companies that are participating in emerging areas of technology. The Exchange will add new companies to the Index by selecting replacements from a list of replacement candidates prepared semi-annually by CSFB.<sup>13</sup>

As part of the rebalancing, each of the 25 largest component securities (measured by average market capitalization) is assigned a weight of approximately 2.4% of the Index's total weight. The remaining 50 Index components, are assigned a weight of 0.8% of the Index's total weight.

After the fifth trading day of each January, CSFB will make available to the Exchange a list of all components to be included in the Index for the coming year, as well as their respective weightings—either 2.4% or 0.8%. This list will be based on average component trading data for the preceding month of December. Following the close of trading on the second Friday in January, the next Index portfolio will be created by determining the number of whole shares for each component security so that each component represents its assigned weighting in the Index. After the composition of the Index has been determined, and prior to the third Friday in January, information concerning the selected components of the Index and their weightings will be announced by the Exchange. On the first trading day following the January

expiration, all option contracts on the Index will trade based upon the newly rebalanced Index. An adjustment to the Index divisor will be made to ensure the continuity of the Index's value.

The number of shares for each component stock included in the Index portfolio will remain fixed between annual rebalancings except in the event of certain types of corporate actions such as: the payment of a dividend other than an ordinary cash dividend, stock distribution, stock split, reverse stock split, rights offering, distribution, reorganization, recapitalization, or similar event with respect to the component securities. In the case of a merger or the consolidation of an issuer of a component security, if the security remains in the Index, the number of shares for that component security included in the portfolio may be adjusted to the nearest whole share to maintain the component's relative weight in the Index at the level immediately prior to the corporate action.<sup>14</sup>

#### e. Component Replacements

The Exchange shall remove and replace an Index component security if: (1) The security no longer trades due to a merger, takeover, or similar extraordinary corporate event; (2) the security fails to satisfy the maintenance and eligibility criteria; or (3) the underlying company no longer represents the computer and communications technology industry.<sup>15</sup> At the time of the annual review in January and after the fifth day of trading in July, CSFB will provide the Exchange with a list of approximately 30 eligible securities from which the Exchange will select replacements. The securities in the replacement list will be selected and ranked by CSFB based on a number of criteria, including conformity with the eligibility standards for Index components. To facilitate the selection of a replacement, the list will be categorized according to the sub-sectors represented in the Index. The Exchange will publicly disseminate the list of replacement securities upon receipt.

The Exchange will select replacement securities from the list based upon market capitalization, liquidity, and

sector category. Although CSFB will prepare the list of replacement securities, the Exchange will determine which replacement security will be added to the Index. The Exchange will ensure that replacement securities meet all eligibility criteria at the time they are included in the Index.

If a component security is added or replaced, the Exchange shall: (1) calculate the average dollar value of the remaining Index components that were not among the 25 largest stocks assigned a weighting of 2.4% at the time of the most recent annual rebalancing; and (2) invest that amount in the new component security, to the nearest whole share. In all cases the divisor will be adjusted, if necessary, to ensure continuity in the Index value.

All replacements of component securities and the handling of non-routine corporate actions (e.g., merger or acquisition) will be announced at least ten business days in advance of such effective change, whenever possible. The Exchange will make this information available to the public through dissemination of an information circular.

#### f. Dissemination of Index

The Exchange will disseminate the value of the Index in a manner similar to the dissemination of values for other stock indexes that underlie Exchange-traded options. Specifically, during standard trading hours, the Exchange will continuously calculate the value of the Index and disseminate such value every 15 seconds over the Consolidated Tape Association's Network B.

#### g. Capacity

The Exchange has represented that it has the necessary systems capacity to provide for the trading of options on the Index. Furthermore, the Exchange has confirmed with the Options Price Reporting Authority ("OPRA") that OPRA has sufficient capacity to provide for the Exchange's listing and trading of options on the Index.<sup>16</sup>

#### h. Expiration and Settlement

Options on the Index will be European style options<sup>17</sup> that will be cash settled. Standard option trading hours (9:30 A.M. to 4:02 P.M. Eastern Time) will apply to options on the Index. The Index option will expire on

<sup>14</sup> In the case of routine corporate events such as stock splits, the Exchange will adjust the Index divisor without consulting CSFB. However, adjustments to the Index divisor following extraordinary corporate events such as a merger or bankruptcy will be made by the Exchange only after consulting with CSFB.

<sup>15</sup> The Exchange and CSFB may consult from time to time to evaluate Index component securities and determine whether they continue to represent the computer and communications technology industry in the manner intended.

<sup>16</sup> See Letter from Joseph P. Corrigan, Executive Director, OPRA, to Richard Strasser, Assistant Director, Division, Commission, dated March 2, 1999.

<sup>17</sup> Exchange Rule 900C(b)(20) defines a European style option as "an option contract that can be exercised only at its expiration pursuant to the rules of The Options Clearing Corporation."

<sup>13</sup> See *infra* Section II(A)(1)(e), "Components Replacements" for further information regarding the replacement list.

the Saturday following the third Friday of the expiration month ("Expiration Friday"). The last trading day in expiring option series will normally be the second to last business day preceding the Saturday that follows an Expiration Friday (normally a Thursday). Trading in expiring options will cease at the close of trading on the last trading day.

The Exchange plans to list options series with expirations in the three near-term calendar months and in two additional calendar months in the January cycle. The Exchange may list and trade flexible Exchange options ("FLEX Options") as well as longer term option series that have up to thirty-six months to expiration. In lieu of long-term options on the full value of the Index, the Exchange may instead list long-term, reduced value options based on one-tenth ( $\frac{1}{10}$ th) the full value of the Index. In no case will the interval between expiration months for a full value or reduced value long-term option contract be less than six months.

The trading of options on the Index, including any long-term options, will be subject to the same rules that govern the trading of all the Exchange's index options, including sales practice rules, margin requirements, and floor trading procedures. Position limits on reduced value long-term Index options will be equivalent to the position limits for regular (full value) Index options and will be aggregated with such options. For example, if the position limit for the full value Index options is 15,000 contracts on the same side of the market, then the position limit for the reduced value Index options will be 150,000 contracts on the same side of the market.

The exercise settlement value for all of the Index's expiring options will be calculated based upon the primary exchanges' regular way opening sale prices for the component securities. In the case of Nasdaq-listed securities, the first reported regular way sale price will be used. If any component stock does not open for trading on its primary market on the last trading day before expiration, the previous trading day's last sale price will be used to calculate the settlement of the Index.

#### i. Exchange Rules Applicable to Stock Index Options

The Index is deemed to be a "stock index group" under Exchange Rule 901C(a), "Designation of Stock Index Options," and a "stock index industry group" under Exchange Rule 900C(b)(1), "Stock Index Options: Applicability and Definitions." Consequently, Exchange Rules 900C through 980C will apply to

the trading of Index option contracts. These rules cover issues such as surveillance, exercise prices, and position limits.

Surveillance procedures currently used to monitor trading in each of the Exchange's other index option contracts will also be used to monitor trading in options on the Index. With respect to Exchange Rule 903C(b), "Series of Stock Index Options," the Exchange proposes to list near-the-money (i.e., within ten points above or below the current Index value) option series on the Index at  $2\frac{1}{2}$  point strike (exercise) price intervals when the value of the Index is below 200 points. The Exchange believes that under Exchange Rule 904C(c), "Position Limits," it is appropriate for the Exchange to establish a position limit for options on the Index at a level no greater than 15,000 contracts.

#### j. Disclaimer Provisions of Rule 902C

The Exchange proposes to amend Exchange Rule 902C to include CSFB in the disclaimer provisions of that rule. Because CSFB will have no control over dissemination of the value of the Index, the Exchange believes that CSFB should be included in the disclaimer provisions of Exchange Rule 902C, similar to other such entities whose names are attached to indexes underlying options listed on the Exchange.

#### k. Regulatory Circular for Member Firms

Prior to the commencement of trading of options on the Index, the Exchange will issue a circular to members with relevant information concerning options on the Index. The circular also will remind Exchange members of their regulatory responsibilities; for example, members must comply with Exchange Rule 9.9, "Suitability of Recommendations."

#### 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,<sup>18</sup> in general, and furthers the objectives of Section 6(b)(5)<sup>19</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in facilitating transactions in securities, and remove impediments to and perfect the mechanism of a free and open market and a national market system.

<sup>18</sup> 15 U.S.C. 78f(b).

<sup>19</sup> 15 U.S.C. 78f(b)(5).

#### B. Self-Regulatory Organization's Statement on Burden on Competition

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

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

The Exchange did not solicit or receive written comments with respect to the proposed rule change.

#### III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549-0609. Copies of the submissions, 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 persons, 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 in 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 Exchange. All submissions should refer to File No. SR-Amex-99-10 and should be submitted by July 8, 1999.

#### IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

The Commission has carefully reviewed the Exchange's proposed rule change and finds, for the reasons set forth below, that the proposal is consistent with the requirements of Section 6 of the Act<sup>20</sup> and the rules and regulations thereunder applicable to a national securities exchange. Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in

<sup>20</sup> 15 U.S.C. 78f.

facilitating transactions in securities, and remove impediments to and perfect the mechanism of a free and open market and a national market system. The Commission believes that the trading of options on the Index will serve to promote the public interest and help to remove impediments to a free and open securities market by providing investors with a means of hedging exposure to market risks associated with the securities issued by companies in the computer and communications technology industry.

The Commission finds that the trading of options on the Index will permit investors to participate in the price movements of the 75 securities on which the Index is based. Further, trading of options on the Index will allow investors holding positions in some or all of the securities underlying the Index to hedge the risks associated with these securities. Accordingly, the Commission believes that options on the Index will provide investors with an additional trading and hedging mechanism.<sup>21</sup>

Nevertheless, the trading of options on the Index raises several issues related to design of the Index, customer protection, and surveillance. The Commission believes, however, for the reasons discussed below, that the Exchange adequately has addressed these issues.

#### A. Index Design and Structure

The Commission believes that it is appropriate for the Exchange to apply its rules governing options on stock index industry groups to the trading of options on the Index. The Commission notes that the Index contains 75 securities representing one industry group, and thus reflects a narrow segment of the U.S. equities market.

The Commission notes that the 75 securities comprising the Index are actively-traded. The average daily trading volume among the component securities, calculated over a six month period ending April 9, 1999, ranged from a high of 49.5 million shares per day (Dell Computer) to a low of 220,000 shares per day (Amdocs). In addition, the market capitalizations of the securities in the Index are large, ranging

from a high of \$475.7 billion (Microsoft) to a low of \$888.1 million (Ingram Micro) as of April 9, 1999. Finally, no one component security accounted for more than 3.99% of the Index's total weight, and the percentage weighting of the three largest issues in the Index accounted for 10.68% of the Index's total weight.<sup>22</sup>

With respect to the maintenance of the Index, the Commission believes that the Exchange has implemented several measures to ensure that the Index remains comprised of highly-capitalized, actively-traded securities, thereby ensuring that the Index will remain substantially the same over time. In this regard, the Exchange will maintain the Index so that: (1) the component securities comprising the top 90% of the Index, by weight, each will have market capitalizations of at least \$75 million, and the remaining 10% each will have market capitalizations of no less than \$50 million; (2) the component securities comprising the top 90% of the Index, by weight, each will have monthly trading volumes of at least 500,000 shares, and the remaining 10% each will have monthly trading volumes no less than 400,000 shares; (3) at least 90% of the components in the Index, by weight, and 80% of the number of components in the Index will be eligible for standardized options trading; (4) the component securities will have primary listings on the Exchange, NYSE, or Nasdaq and will be "reported" securities pursuant to Rule 11Aa3-1 of the Act,<sup>23</sup> and (5) absent approval from the Commission pursuant to Section 19(b)(2) of the Act, the Exchange will not increase the number of components to more than 100 or reduce the number of components to fewer than 50.

The Commission further believes that the maintenance standards governing the Index will help protect against material changes in the composition and design of the Index that might adversely affect the Exchange's obligations to protect investors and to maintain fair and orderly markets in options based on the Index. The Exchange is required to immediately notify the Commission staff if the Index fails at any time to satisfy one or more of the specified

maintenance criteria. Further, in such an event, the Exchange will not open for trading any additional series of options on the Index, unless the Exchange determines that such failure is insignificant and the Commission concurs in that determination, or unless the Commission approves the continued listing of options on the Index under Section 19(b)(2) of the Act.<sup>24</sup>

#### B. Customer Protection

The Commission believes that a regulatory system designed to protect public customers must be in place before the trading of sophisticated financial instruments, such as options based on the Index, can commence on a national securities exchange. The Commission notes that the trading of standardized exchange-listed options occurs in an environment that is designed to ensure that: (1) the special risks of options are disclosed to public customers; (2) only investors capable of evaluating and bearing the risks of options trading are engaged in such trading; and (3) special compliance procedures are applicable to options accounts. Accordingly, because the Index options will be subject to the same regulatory regime as the other standardized options currently traded on the Exchange, the Commission believes that adequate safeguards are in place to ensure the protection of investors in Index options.

#### C. Surveillance

In evaluating new derivative instruments, the Commission, consistent with the protection of investors, considers the degree to which the exchange sponsoring the derivative instrument has the ability to obtain information necessary to detect and deter market manipulation and other trading abuses. The Commission believes that a surveillance sharing agreement between an exchange proposing to list a security index derivative product and the primary exchange(s) trading the securities underlying the derivative product is an important measure for surveillance of the derivative and underlying securities markets. Such agreements facilitate and ensure the availability of information needed to fully investigate manipulation if it were to occur.<sup>25</sup> In this regard, the Commission notes that the Exchange and the primary markets for the stocks underlying the Index—the NYSE and the NASDR (the self-regulatory

<sup>21</sup> Pursuant to Section 6(b)(5) of the Act, the Commission must predicate approval of any new option proposal upon a finding that the introduction of such new derivative instrument is in the public interest. Such a finding would be difficult for a derivative instrument that served no hedging or other economic function, because any benefits that might be derived by market participants likely would be outweighed by the potential for manipulation, diminished public confidence in the integrity of the markets, and other valid regulatory concerns.

<sup>22</sup> At the most recent annual rebalancing (*i.e.*, January 1999), each of the 25 largest component securities was assigned a weighting of approximately 2.4% of the total Index weight. This weighting is not static, however, and varies in response to changes in the market price of each component security. Therefore, increases in the market prices of some component securities have caused their weightings to increase above the original 2.4% setting (*e.g.*, America Online had a weighting of 3.99% as of April 9, 1999).

<sup>23</sup> 17 CFR 240.11Aa3-1.

<sup>24</sup> 15 U.S.C. 78s(b)(2).

<sup>25</sup> See Securities Exchange Act Release No. 31243 (Sept. 28, 1992), 57 FR 45849 (Oct. 5, 1992), 57 FR 45849 (Oct. 5, 1992).

organization which oversees Nasdaq)—are members of the Intermarket Surveillance Group, which provides for the sharing of all necessary surveillance information among members. The Commission believes that this arrangement will ensure the availability of information necessary to detect potential manipulations and other trading abuses. In addition, the Exchange has represented that foreign country securities, or ADRs thereon, that are not subject to comprehensive surveillance agreements will not in the aggregate represent more than 20% of the weight of the Index.

The Commission notes that certain concerns are raised when a broker-dealer, such as CSFB, is involved in the development and maintenance of a stock index that underlies an exchange-traded derivative product. For several reasons, however, the Commission believes that the Exchange has adequately addressed this concern with respect to options on the Index.

First, the value of the Index, including the final settlement value, will be calculated and disseminated by the Exchange independently of CSFB. Accordingly, neither CSFB nor any of its affiliates or other persons will be in receipt of the values prior to their public dissemination. Second, CSFB has established informational barriers around the CSFB personnel who have access to information regarding changes and adjustments to the Index.<sup>26</sup> The Commission believes that these barriers will help prevent the improper use of material non-public information concerning the Index and strengthen the proposal by maintaining the integrity of changes made to the Index. In addition, CSFB currently has in place internal review procedures to monitor trading activity in Index component securities and securities included in the replacement list. Finally, the Exchange's existing surveillance procedures for stock index options will apply to the options on the Index and should provide the Exchange with adequate information to detect and deter trading abuses. In sum, the Commission believes that the procedures discussed above will help to ensure that CSFB does not unfairly use any information regarding the Index that it obtained through its role in developing and maintaining the Index.

The Commission also believes that it is appropriate for the Exchange to make

conforming changes to Exchange Rules 901C and 902C. The revisions are technical in nature and are designed to ensure that the Exchange's rules remain current. The Commission believes that it is important for the Exchange to update its rules to reflect newly listed derivative products. Pursuant to Section 19(b)(2) of the Act,<sup>27</sup> the Commission finds good cause for approving the proposal, including Amendment No. 1 thereto, prior to the thirtieth day after the date of publication of notice of the filing thereof in the **Federal Register**. The Commission notes that proposed rule changes regarding the listing and trading of options on industry group or narrow-based stock indexes may become effective immediately upon filing provided they satisfy certain generic listing standards.<sup>28</sup> The generic listing standards establish minimum guidelines concerning the design and operation of narrow-based indexes.

The Commission recognizes that the Index, as amended, satisfies all of the generic listing standards save two, the weighting methodology<sup>29</sup> and the frequency of rebalancing.<sup>30</sup> The Commission believes that because these deviations from the generic listing standards are not significant, they should not preclude the Exchange from receiving accelerated approval for its proposal.

Specifically, the modified equal-dollar weighted methodology will ensure that the weighting of the Index does not become concentrated in one or several component securities. Because the weightings assigned to the component securities are low (*i.e.*, 2.4% and 0.8%), it is unlikely that the weighting of a single component or group of component securities would increase to such a level that concentration issues would arise. Furthermore, the Exchange has represented that in no instance will a single component security represent more than 25% of the weight of the Index, nor will the five highest weighted

component securities in the aggregate account for more than 50% of the weight of the Index.

For similar reasons, the Commission believes that it is appropriate for the Exchange to rebalance the Index annually rather than quarterly. Quarterly rebalancings were designed as a prophylactic measure against concentration problems. The Commission believes, however, that the low weightings assigned to component securities of the Index at the annual rebalancings addresses the concentration concerns that underlie the need for more frequent rebalancings. Accordingly, because the Index substantially complies with the generic listing standards, and the investor protection concerns have been addressed, the Commission finds good cause exists for granting accelerated approval to the proposed rule change Amendment No. 1 thereto.

## V. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>31</sup> that the proposed rule change, SR-Amex-99-10, and Amendment No. 1 thereto, are hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>32</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 99-15349 Filed 6-16-99; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-41501; File No. SR-CBOE-99-17]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Chicago Board Options Exchange, Inc. Governing the Operation of the Retail Automatic Execution System

June 9, 1999

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 April 16, 1999, the Chicago Board Options Exchange, Inc. ("CBOE" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the CBOE. On

<sup>27</sup> 15 U.S.C. 78s(b)(2).

<sup>28</sup> See Securities Exchange Act Release No. 34157 (June 3, 1994), 59 FR 30062 (June 10, 1994) and Commentary .02 of Exchange Rule 901C. While a proposed rule change filed in accordance with the generic listing standards becomes effective immediately upon filing, trading in the approved options may not commence until 30 days from the date of filing.

<sup>29</sup> Although the generic listing standards contemplate the calculation of indexes using capitalization weighted, price weighted, or equal-dollar weighted methods, the standards do not specifically encompass the modified equal-dollar weighted methodology that the Exchange proposes to use for the Index.

<sup>30</sup> Under the generic listing standards, indexes based upon the equal-dollar weighting methodology must be rebalanced at least quarterly.

<sup>31</sup> 15 U.S.C. 78s(b)(2).

<sup>32</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>26</sup> Details of the CSFB informational barriers have been submitted to the Commission under separate cover. See Letter from Robert L. Mazzeo; Solomon, Zauderer, Ellenhorn, Frischer & Sharp; to Richard Strasser, Assistant Director, Division, Commission, dated June 9, 1999.