

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

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*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-43912; File No. SR-Phlx-00-91]

### Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change by the Philadelphia Stock Exchange, Inc., Relating to Index Fund Shares

January 31, 2001.

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 December 4, 2000, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and III below, which Items have been prepared by the Phlx. On January 23, 2001, the Phlx filed an amendment to the proposed rule change.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule changes from interested persons and to approve the proposal on an accelerated basis.

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

The Phlx proposes to adopt listing standards and trading rules for Index Fund Shares, including generic listing standards, which would permit the Phlx to trade a series of Index Fund Shares pursuant to Rule 19b-4(e) under the Act. The text of the proposed rule change is available at the Phlx or 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 Phlx 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 III below. The Phlx 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 Statutory Basis for, the Proposed Rule Change

###### I. Purpose

a. *Listing Requirements for Index Fund Shares.* The Phlx proposes to adopt new listing and delisting requirements to accommodate the trading of Index Fund Shares, securities issued by an open-end management investment company ("Fund") that seek to provide investment results that correspond generally to the price and yield performance of a specified underlying index ("Index Fund Shares"). The listing standards will permit the Exchange to trade Index Fund Shares either by listing or pursuant to unlisted trading privileges ("UTP").

Index Fund Shares will be issued by an entity registered with the Commission as an open-end management investment company, and which may be organized as a series fund providing for the creation of separate series of securities, each with a portfolio consisting of some or all of the component securities of a specified securities index. Issuances of Index Fund Shares by a Fund will be made only in minimum size aggregations or multiples thereof ("Creation Units"). The size of the applicable Creation Unit size aggregation will be set forth in the Fund's prospectus, and will vary from one series of Index Fund Shares to another, but generally will be of substantial size (e.g., value in excess of \$450,000 per Creation Unit). It is expected that a Fund will issue and sell Index Fund Shares through a principal underwriter on a continuous basis at the net asset value per share next determined after an order to purchase Index Fund Shares in Creation Unit size aggregations is received in proper form. Index Fund Shares will be traded on the Exchange like other equity securities, and Phlx equity trading rules will apply to the trading of Index Fund Shares.

The Phlx expects that Creation Unit size aggregations of Index Fund Shares generally will be issued in exchange for the "in kind" deposit of a specified portfolio of securities, together with a cash payment representing, in part, the amount of dividends accrued up to the time of issuance. The Phlx anticipates that such deposits will be made primarily by institutional investors, arbitragers, and the Phlx specialist. Redemption of Index Fund Shares generally will be made "in kind," with a portfolio of securities and or cash exchanged for Index Fund Shares that have been tendered for redemption. Issuances or redemptions also could occur for cash under specified circumstances (e.g., if it is not possible to effect delivery of securities underlying the specific series in a particular foreign country) and at other times in the discretion of the Fund.

The Phlx expects that a Fund will make available on a daily basis a list of the names and the required number of shares of each of the securities to be deposited in connection with the issuance of Index Fund Shares of a particular series in Creation Unit size aggregations, as well as information relating to the required cash payment representing, in part, the amount of accrued dividends.

A Fund may make periodic distributions of dividends from net investment income, including net foreign currency gains, if any, in an amount approximately equal to accumulated dividends on securities held by the Fund during the applicable period, net of expenses and liabilities for such period. A Fund may also distribute its capital gains, if any. The Exchange notes that the trading prices of Index Fund Shares may differ in varying degrees from their daily NAV and can be affected by market forces such as supply and demand, economic conditions and other factors.<sup>4</sup>

Index Fund Shares will be registered in book entry form through The Depository Trust Company ("DTC"), which means no stock certificates will be issued. Trading in Index Fund Shares on the Exchange may be effected until either 4:00 p.m. or 4:15 p.m. each business day.

*Criteria for Initial and Continued Listing.* The Phlx believes that the listing criteria proposed in its new rule are generally consistent with the listing standards for Index Fund Shares currently used by the American Stock

<sup>12</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>3</sup> See Letter from Carla Behnfeldt, Director, New Product Development Group, Phlx, to Nancy Sanow, Esq., Assistant Director, Division of Market Regulation ("Division"), Commission, dated January 22, 2001 ("Amendment No. 1"). Amendment No. 1 adds language to the rule text and the purpose section of the filing that clarifies Phlx's prospectus delivery requirements under the Securities Act of 1933. In addition, Amendment No. 1 adds representations by the Exchange in the purpose section of the filing regarding factors affecting (1) the trading prices of Index Fund Shares, (2) the minimum number of creation units, and (3) minimum trading variations.

<sup>4</sup> See Amendment No. 1, *supra* note 3.

Exchange ("Amex"),<sup>5</sup> and are similar to the recently approved listing standards for Trust Shares.<sup>6</sup>

**Initial Listing.** If Index Fund Shares are to be listed on the Exchange, the Phlx will establish a minimum number of Index Fund Shares that must be outstanding at commencement of trading, and such minimum number will be included in any required submission under Rule 19b-4. The Exchange anticipates that a minimum of two creation units in any series of Index Fund Shares will be required to be outstanding before trading can begin.<sup>7</sup>

**Continued Listing.** In connection with continued listing, the Phlx will consider the suspension of trading in, or removal from listing of, an Index upon which a series of Index Fund Shares is based when any of the following circumstances arise: (1) There are fewer than 50 beneficial holders of the series of Index Fund Shares for 30 or more consecutive trading days; (2) the value of the index or portfolio of securities on which the series of Index Fund Shares is based is no longer calculated or available; or (3) such other event shall occur or condition exists which, in the opinion of the Phlx, makes further dealings on the Exchange inadvisable. The Phlx will not, however, be required to suspend or delist from trading, based on the above factors, any Index Fund Shares for a period of one year after the initial listing of such Index Fund Shares for trading on the Exchange. The Phlx will require that Index Fund Shares be removed from listing upon termination of the Fund that issued such shares.

**b. Exchange Rules Applicable to the Trading of Index Fund Shares.** Index Fund Shares are considered "securities" under the rules of the Phlx and are subject to all applicable trading rules, including the provisions of Phlx Rule 2001A, ITS "Trade-Throughs" and "Locked Markets," which prohibit Exchange members from initiating trade-throughs for Intermarket Trading System securities, as well as rules governing priority, parity and precedence of orders, market volatility-related trading halt provisions and

responsibilities of the assigned specialist firm.<sup>8</sup> Similarly, the Phlx's equity margin rules will apply. The Phlx will maintain written surveillance procedures to surveil trading in Index Fund Shares.

**c. Standards to Permit Trading, Either by Listing or Pursuant to UTP, of Index Fund Shares Pursuant to Rule 19b-4(e) under the Act.** The Phlx proposes to adopt generic listing and delisting standards to permit the Exchange to approve for trading, pursuant to Rule 19b-4(e) under the Act,<sup>9</sup> a series of Index Fund Shares. Rule 19b-4(e) permits self-regulatory organizations ("SROs") to list and trade new derivative products that comply with existing SRO trading rules, procedures, surveillance programs and listing standards, without submitting a proposed rule change under Section 19(b) of the Act.<sup>10</sup> Accordingly, the Phlx proposes a series of Index Fund Shares for listing or trading, either by listing or pursuant to UTP, pursuant to Rule 19b-4(e) under the following criteria:

Upon the initial listing of a series of Index Fund Shares, component stocks that in the aggregate account for at least 90% of the weight of the underlying index or portfolio must have a minimum market value of at least \$75 million. In addition, the component stocks representing at least 90% of the weight of the index or portfolio must have a minimum monthly trading volume during each of the last six months of at least 250,000 shares.

The most heavily weighted component stocks in an underlying index or portfolio cannot exceed 25% of the weight of the index or portfolio, and the five most heavily weighted component stocks cannot together exceed 65% of the weight of the index or portfolio. The underlying index or portfolio must include a minimum of 13 stocks.<sup>11</sup> All securities in an underlying

index or portfolio must be listed on a national securities exchange or The Nasdaq Stock Market (including the Nasdaq SmallCap Market). Any series of Index Fund Shares must meet these eligibility criteria as of the data of the initial deposit of securities and cash into the trust or fund.

The index underlying a series of Index Fund Shares will be calculated based on either the market capitalization, modified market capitalization, price, equal-dollar or modified equal-dollar weighting methodology. In addition, if the index is maintained by a broker-dealer, the broker-dealer shall erect a "fire wall" around the personnel who have access to information concerning changes and adjustments to the index and the index shall be calculated by a third party who is not a broker-dealer.

The current index value will be disseminated every 15 second over the Consolidated Tape Association's Network B. The Reporting Authority will disseminate for each series of Index Fund Shares an estimate, updated every 15 seconds, of the value of a share of each series. This may be based, for example, upon current information regarding the required deposit of securities plus any cash amount to permit creation of new shares of the series or upon the index value.

A minimum of 100,000 shares of a series of Index Fund Shares is required to be outstanding at commencement of trading. Trading will occur between 9:30 a.m. and either 4 p.m. or 4:15 p.m. for each series of Index Fund Shares, as specified by the Exchange. The minimum variation may vary among different series of Index Fund Shares, but will be set at 1/16, 1/32 or 1/64 of \$1.00 (as established by the Exchange for Index Fund Shares trading in fractions) and \$.01 (for Index Fund Shares trading in decimals).<sup>12</sup> The Exchange will utilize existing surveillance procedures for Index Fund Shares that it trades pursuant to Rule 19b-4(e).<sup>13</sup> The provisions of Phlx's proposed Rule 803(1) will apply to all series of Index Fund Shares.

**d. Notice to Members.** Prior to the commencement of trading in Index Fund Shares, the Phlx will issue a circular to members highlighting the characteristics of purchases in Index Fund Shares. The circular will discuss the special characteristics and risks of trading this type of security. Specifically, the circular, among other

securities account for less than 5% of such fund's total assets.

<sup>12</sup> See Amendment No. 1, *supra* note 3.

<sup>13</sup> *Id.*

<sup>5</sup> The Amex's listing criteria were approved by the Commission on March 8, 1996. See Securities Exchange Act Release No. 36947 (March 8, 1996), 61 FR 10606 (March 14, 1996). Pursuant to Rule 12f-5 under the Act, to trade a particular class or type of security pursuant to UTP, the Exchange must have rules providing for transactions in such class or type of security. The Amex has enacted listing standards for Index Fund Shares, and the Phlx's proposed rule change is designed to create similar standards for Index Fund Shares listed and/or trading on the Phlx.

<sup>6</sup> See Securities Exchange Act Release No. 43717 (December 13, 2000), 65 FR 80976 (December 22, 2000).

<sup>7</sup> See Amendment No. 1, *supra* note 3.

<sup>8</sup> Phlx Rule 746 will also apply to the trading of Index Fund Shares. That rule provides that every member is required either personally or through a general partner or an officer who is a holder of voting stock in his organization to use due diligence to learn the essential facts relative to every customer and to every order or account accepted by his organization.

<sup>9</sup> 17 CFR 240.19b-4(e).

<sup>10</sup> See Securities Exchange Act Release No. 40761 (December 8, 1998), 63 FR 70952 (December 22, 1998).

<sup>11</sup> Thirteen stocks is the minimum number to permit qualification as a regulated investment company under Subchapter M of the Internal Revenue Code. Under Subchapter M of the Internal Revenue Code, for a fund to qualify as a regulated investment company, the securities of a single issuer can account for no more than 25% of a fund's total assets, and at least 50% of a fund's total assets must be comprised of cash (including government securities) and securities of single issuers whose

issues, will discuss what Index Fund Shares are, how they are created and redeemed, the requirement that members and member firms deliver a prospectus to investors purchasing Index Fund Shares prior to or concurrently with the confirmation of a transaction, applicable Phlx rules, dissemination information, trading information, and the applicability of suitability rules.

In addition, the circular will inform members of the Exchange's policies about trading halts in such securities. First, the circular will advise that trading will be halted in the event the market volatility trading halt parameters set forth in Phlx Rule 133 have been reached. Second, the circular will advise that, in addition to other factors that may be relevant, the Phlx may consider factors such as the extent to which trading is not occurring in a deposited security(s) and whether other unusual conditions or circumstances detrimental to the maintenance of a fair and orderly market are present.

e. *Disclosure.* The Phlx will provide all purchasers of newly-issued Index Fund Shares with a Fund prospectus. Because the Units will be in continuous distribution, the prospectus delivery requirements of Section 5(b)(2) of the Securities Act of 1933 ("Securities Act")<sup>14</sup> will apply to all investors in Index Fund Shares, including secondary market purchases on the Phlx in Index Fund Shares.<sup>15</sup> With respect to series of Index Fund Shares that are the subject of an order by the SEC exempting such series from certain prospectus delivery requirements under Section 24(d) of the Investment Company Act of 1940 (the "1940 Act")<sup>16</sup> and that are not otherwise subject to prospectus delivery requirements under the Securities Act,<sup>17</sup> the Phlx will inform members and member organizations regarding disclosure obligations with respect to a particular series of Index Fund Shares by means of a circular prior to commencement of trading in such series. For these exempted series, the Phlx requires that members and member organizations provide to all purchasers of a series of Index Fund Shares a written description of the terms and characteristics of such securities, in a form prepared by the open-end management investment company issuing such securities, not later than the time a confirmation of the first transaction in such series is delivered to such purchaser. In addition, members

and member organizations shall include such a written description with any sales material relating to a series of Index Fund Shares that is provided to customers or the public. Any other written materials provided by a member or member organization to customers or the public making specific reference to a series of Index Fund Shares as an investment vehicle must include a statement in substantially the following form: "A circular describing the terms and characteristics of [the series of Index Fund Shares] has been prepared by the [open-end management investment company name] and is available from your broker or the Phlx. It is recommended that you obtain and review such circular before purchasing [the series of Index Fund Shares]. In addition, upon request you may obtain from your broker a prospectus for [the series of Index Fund Shares]."

A member or member organization carrying on omnibus account for a non-member broker-dealer is required to inform such non-member that execution of an order to purchase a series of Index Fund Shares for such omnibus account will be deemed to constitute agreement by the non-member to make such written description available to its customers on the same terms as are directly applicable to members and member organizations under this rule.

Upon request of a customer, a member or member organization shall also provide a prospectus for the particular series of Index Fund Shares.

f. *Minimum Variation.* Index Fund Shares will trade in the appropriate minimum variation, pursuant to Phlx Rule 125. For Index Fund Shares traded pursuant to UTP, the minimum variation for any series of Index Fund Shares will be the minimum variation established by the primary market for such series. The Phlx proposes that the minimum fractional change for Index Fund Shares on the Phlx will be  $\frac{1}{16}$ ,  $\frac{1}{32}$ , or  $\frac{1}{64}$  of \$1.00 depending on the series of Index Fund Shares. In addition, the Phlx is proposing to set its minimum variation at \$.01 for Index Fund Shares trading in decimals.

g. *Limitation of Exchange Liability.* The Phlx proposes a provision limiting potential liability of the Exchange, the Reporting Authority, and any agent of the Phlx in connection with Index Fund Shares.

## 2. Statutory Basis

The Phlx believes that the proposed rule change is consistent with section 6(b)(5) of the Act<sup>18</sup> in that it is designed to promote just and equitable principles

of trade, to foster cooperation and coordination with persons engaged in regulating securities transactions, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest.

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

The Phlx 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 Phlx has neither solicited nor received written comments on 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, NW, Washington, DC 20549-0609. 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. 5552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the Phlx. All submissions should refer to File No. SR-Phlx-00-91 and should be submitted by February 28, 2001.

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

The Commission finds that the proposed rule change, as amended, 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)(5).<sup>19</sup> Specifically, the Commission finds that the proposals to provide standards to permit listing and trading

<sup>14</sup> 15 U.S.C. 77e(5)(b)(2).

<sup>15</sup> See Amendment No. 1, *supra* note 3.

<sup>16</sup> 15 U.S.C. 80a-24(d).

<sup>17</sup> See *supra* note 3.

<sup>18</sup> 15 U.S.C. 78f(b)(5).

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

of Index Fund Shares will provide investors with a convenient and less expensive way of participating in the securities markets. The proposal should advance the public interest by providing investors with increased flexibility in satisfying their investment needs by allowing them to purchase and sell a single security replicating or to a large extent representing the performance of several portfolios of stocks at negotiated prices throughout the business day.

In addition, the proposal to provide generic standards to permit listing and trading of Index Fund Shares pursuant to Rule 19b-4(e) furthers the intent of that rule by facilitating commencement of trading in these securities without the need for notice and comment and Commission approval under section 19(b) of the Act. Thus, by establishing generic standards, the proposal should reduce the Exchange's regulatory burden, as well as benefit the public interest, by enabling the Exchange to bring qualifying products to the market more quickly. Accordingly, the Commission finds that the Exchange's proposal will promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, and, in general, protect investors and the public interest consistent with section 6(b)(5) of the Act.<sup>20</sup>

The Commission believes that the proposal to list and trade Index Fund Shares will provide investors with an alternative to trading a broad range of securities on an individual basis, and will give investors the ability to trade a product representing an interest in a portfolio of securities designed to reflect substantially the applicable underlying index. Index Fund Shares will allow investors to: (1) Respond quickly to market changes through intra-day trading opportunities (2) engage in hedging strategies similar to those used by institutional investors; and (3) reduce transactions costs for trading a portfolio of securities. Although Index Fund Shares are not leveraged instruments, and therefore do not possess any of the attributes of stock index options, their prices will be derived and based on the value of the securities and the cash held in the Fund. Accordingly, the level of risk involved in the purchase or sale of these Index Fund Shares is similar to the risk involved in the purchase or sale

of traditional common stock, with the exception that the pricing mechanism for these Index Fund Shares is based on a portfolio of securities.

The Commission finds that the Phlx's proposal contains adequate rules and procedures to govern the trading of Index Fund Shares. Under Phlx rules, Index Fund Shares are subject to the full panoply of rules governing the trading of equity securities on the Phlx, including, among others, rules and procedures governing the priority, parity and precedence of orders, responsibilities of all types of market-makers, trading halts, disclosures to members, margin requirements, and customer suitability requirements. Further, the Commission notes that the Phlx will use surveillance procedures that incorporate and rely upon existing Phlx surveillance procedures governing equities, and the Commission believes that these procedures are adequate under the Act. In addition, the rules we are approving today contain specific listing and delisting criteria for Index Fund Shares that will help to ensure that the markets for Index Fund Shares will be deep and liquid to allow for the maintenance of fair and orderly markets. The Commission believes that these criteria should serve to ensure that the underlying securities of an Index Fund Shares series are well capitalized and actively traded, and that new series of Index Fund Shares do not contain features that are likely to impact adversely the U.S. securities markets.

In addition, the Exchange has designated that a minimum of two creation units will be required to be outstanding at start-up of trading. The Commission believes this minimum number is sufficient to help to ensure that a minimum level of liquidity will exist at the start of trading. Furthermore, the Commission finds that registering the Index Fund Shares in book-entry form through DTC, managing the distribution of dividends from net investment income, if any, and distributing capital gains, if any, are characteristics of Index Fund Shares that are consistent with the Act and should allow for the maintenance of fair and orderly markets and perfect the mechanism of a free and open market pursuant to section 6(b)(5) of the Act.<sup>21</sup>

Furthermore, the Commission believes that the Exchange's proposal to trade Index Fund Shares in minimum fractional increments of 1/16, 1/32 or 1/64 of \$1.00 or .01 for Index Fund Shares

trading in decimals is consistent with the Act. The Commission believes that such trading should enhance market liquidity, and should promote more accurate pricing, tighter quotations, and reduced price fluctuations. The Commission also believes that such trading should allow customers to receive the best possible execution of their transactions in Index Fund Shares.

The Exchange represents that the Reporting Authority will disseminate for each Fund of Index Fund Shares an estimate, updated every 15 seconds, of the value of a share of each Fund. The Commission believes that the information the Exchange proposes to have disseminated will provide investors with timely and useful information concerning the value of each Fund.

In addition, the Commission believes that the Index Fund Shares proposal contains several provisions that will ensure that investors are adequately apprised of the terms, characteristics, and risks of trading Index Fund Shares. Index Fund Shares will be subject to a prospectus delivery requirement or, for series that have been granted relief from the prospectus delivery requirements of the 1940 Act<sup>22</sup> and are not otherwise subject to prospectus delivery requirements under the Securities Act, a product description delivery requirement. The requirement extends to a member or member organization carrying an omnibus account for a non-member broker-dealer, who must notify the non-member to make the product description available to its customers on the same terms as are directly applicable to members and member organizations. Finally, a member or member organization must deliver a prospectus to a customer upon request.

The Commission also notes that upon the initial listing of any Index Fund Shares under the generic standards, the Exchange will issue a circular to its members explaining the unique characteristics and risks of this particular type of security. The circular also will note the Exchange members' prospectus or product description delivery requirements, and inform members of their responsibilities under Phlx rules in connection with customer transactions in these securities.

Rule 19b-4(e) under the Act provides that the listing and trading of a new derivative securities product by an SRO shall not be deemed a proposed rule change, pursuant to paragraph (c)(1) of Rule 19b-4; if the Commission has approved, pursuant to Section 19(b) of the Act, the SRO's trading rules,

<sup>20</sup> 15 U.S.C. 78f(b)(5). 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).

<sup>21</sup> In approving this rule, the Commission notes that it has also considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>22</sup> 15 U.S.C. 80a-1, *et seq.*

procedures and listing standards for the product class that include the new derivative securities product and the SRO has a surveillance program for the product class.<sup>23</sup> The Commission believes that the Phlx's proposal to adopt generic listing standards for Index Fund Shares and applying Rule 19b-4(e) should fulfill the intended objective of that rule by allowing those series of Index Fund Shares that satisfy those standards to start trading, without the need for notice and comment and Commission approval. The Exchange's ability to rely on Rule 19b-4(e) for these products potentially reduces the time frame for bringing these securities to the market and thus enhances investors' opportunities. The Commission notes that while the proposal reduces the Exchange's and the Commission's regulatory burden, the Commission will maintain regulatory oversight over any products listed under the generic standards through regular inspection oversight.

The Commission previously concluded that Index Fund Shares it previously approved for listing under existing rules governing those securities would allow investors to: (1) Respond quickly to market changes through intraday trading opportunities; (2) engage in hedging strategies similar to those used by institutional investors; and (3) reduce transactions costs for trading a portfolio of securities. The Commission believes, for the reasons set forth below, that the product classes that satisfy the proposed generic standards for Index Fund Shares and, therefore, can be listed under Rule 19b-4(e) without prior Commission approval, should produce the same benefits to the Phlx and to investors.

The Commission finds that the Exchange's proposal contains adequate rules and procedures to govern the listing and trading of Index Fund Shares under Rule 19b-4(e). All series of Index Fund Shares listed under the generic standards will be subject to the full panoply of Phlx rules and procedures that now govern the trading of existing securities on the Phlx. Accordingly, any new series of Index Fund Shares listed and traded under Rule 19b-4(e) will be subject to Phlx rules governing the trading of equity securities, including, among others, rules and procedures governing trading halts, disclosures to members, responsibilities of the specialist, account opening and customer suitability requirements, and margin.

In addition, the Phlx has developed specific listing criteria for series of

Index Fund Shares qualifying for rule 19b-4(e) treatment that will help to ensure that a minimum level of liquidity will exist to allow for the maintenance of fair and orderly markets. Specifically, the Exchange has designated that a minimum of 100,000 shares of a series of Index Fund Shares will be required to be outstanding as of the start of trading. The Commission believes that this minimum number of securities is sufficient to establish a liquid Exchange market at the commencement of trading.

The Exchange has also established that upon initial listing, component stocks that in the aggregate account for at least 90% of the weight of the index or portfolio must have a minimum market value of at least \$75 million. Further, the component stocks in the index must have a minimum monthly trading volume during each of the last six months of at least 250,000 shares for stocks representing at least 90% of the weight of the index or portfolio. The most heavily weighted component stock cannot exceed 25% of the weight of the index or portfolio, and the five most heavily weighted component stocks cannot exceed 65% of the weight of the index or portfolio. The index or portfolio must include a minimum of 13 stocks, and all securities in an underlying index or portfolio must be listed on a national securities exchange or the Nasdaq Stock Market. Moreover, any series seeking to list under the generic standards must meet these eligibility criteria as of the date of the initial deposit of securities and cash into the trust or fund. The Commission believes that these criteria should serve to ensure that the underlying securities of these indexes and portfolios are well capitalized and actively traded, which will help to ensure that U.S. securities markets are not adversely affected by the listing and trading of new series of Index Fund Shares under Rule 19b-4(e). These listing criteria also will make certain that new series of Index Fund Shares do not contain features that are likely to impact adversely the U.S. securities markets. Accordingly, the Commission finds that these criteria are consistent with section 6(b)(5) of the Act, because they serve to prevent fraudulent or manipulative acts, promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

In addition, as previously noted, all series of Index Fund Shares listed under the generic standards will be subject to the existing continued listing criteria for these securities. This requirement

allows the Phlx to consider the suspension of trading and the delisting of a series if an event occurred that makes further dealings in such securities inadvisable. The Commission believes that this will give the Phlx flexibility to delist Index Fund Shares if circumstances warrant such action.

The Phlx will rely upon its existing surveillance procedures for supervision of trading in index Fund Shares. The Exchange also will file Form 19b-4(e) with the Commission within five business days of commencement of trading a series under the generic standards, and will comply with all Rule 19b-4(e) recordkeeping requirements. The Commission believes that these surveillance procedures are adequate to address concerns associated with listing and trading Index Fund Shares under the generic standards. Accordingly, the Commission believes that the rules governing the trading of such securities provide adequate safeguards to prevent manipulative acts and practices and to protect investors and the public interest, consistent with Section 6(b)(5) of the Act.<sup>24</sup>

The Commission also notes that certain concerns are raised when a broker-dealer is involved in both the development and maintenance of a stock index upon which a product such as Index Fund Shares is based. The proposal would require that in such circumstances, the broker-dealer must have procedures in place to prevent the misuse of material, non-public information regarding changes and adjustments to the index, and the index shall be calculated by a third party who is not a broker-dealer. The Commission believes that these requirements should help address concerns raised by a broker-dealer's involvement in the management of such an index.

The Commission finds good cause for approving the proposed rule change (SR-Phlx-00-91), as amended, prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. The Commission notes that the proposed rule change is based on Amex Rule 1000A *et seq.*, and is similar to Boston Stock Exchange rules relating to Index Fund Shares, which the Commission approved in the past.<sup>25</sup> The Commission also observes that the proposed rule change concerns issues that previously have been the subject of a full comment period pursuant to

<sup>24</sup> 15 U.S.C. 78f(b)(5).

<sup>25</sup> See Securities Exchange Act Release No. 36947 (March 8, 1996), 61 FR 10606 (March 14, 1996); Securities Exchange Act Release No. 42988 (June 28, 2000), 65 FR 42041 (July 7, 2000).

<sup>23</sup> See Securities Exchange Act Release No. 40761, 63 FR 70952 (December 22, 1998).

section 19(b) of the Act.<sup>26</sup> The Commission does not believe that the proposed rule change raises novel regulatory issues that were not addressed in the previous filings. Further, the changes in Amendment No. 1 clarify: (1) The trading prices of Index Fund Shares; (2) the minimum number of creation units; (3) the minimum trading variations; and (4) the prospectus delivery requirements. Accordingly, the Commission finds that there is good cause, consistent with section 6(b)(5) of the Act, to approve the amended proposal on an accelerated basis.

## V. Conclusion

*It is therefore ordered*, pursuant to section 19(b)(2) of the Act,<sup>27</sup> that the proposed rule change (SR-Phlx-00-91), as amended, is hereby approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>28</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SOCIAL SECURITY ADMINISTRATION

### Supplemental Security Income for the Aged, Blind and Disabled (SSI) Program Demonstration Project; Treatment of Cash Received and Conserved To Pay for Medical or Social Services

**AGENCY:** Social Security Administration (SSA).

**ACTION:** Notice.

**SUMMARY:** The Commissioner of Social Security is extending the application of an existing SSA demonstration project which tests how certain altered resources counting rules might apply in the SSI program. The SSI program is authorized by title XVI of the Social Security Act (the Act). The rules to be tested apply to the treatment of cash received and conserved to pay for medical or social services.

Cash received to pay for medical or social services is not counted as income to the beneficiary when received. Conserved cash received for medical or social services (which is not a reimbursement for these services already paid for by the beneficiary) is not counted as a resource for the calendar month after the month of

receipt, so long as it remains separately identifiable from other resources. Beginning with the second calendar month following the month of receipt, cash received for the payment of medical or social services becomes a countable resource used in the determination of SSI eligibility.

On November 2, 1998, the Commissioner of Social Security published a Notice in the **Federal Register** (63 FR 58802), which waives the rules for counting as resources conserved cash received for medical or social services for Cash and Counseling demonstration participants for five years. All participants in Arkansas, Florida and New Jersey who are members of a test group receive personal assistance services. Personal assistance services are help with the basic activities of daily living, including bathing, dressing, transferring, toileting, and eating, and/or instrumental activities of daily living such as housekeeping, meal preparation, shopping, laundry, money management and medication management. Consumers of personal assistance services who participate in the demonstration are empowered by purchasing the services they require (including medical and social services) to perform the activities of daily living. In order to accomplish the objective of the demonstration project, cash allowances and information services are provided directly to persons with disabilities to enable them to choose and purchase services from providers that they feel would best meet their needs. Participants are also free to engage a fiscal intermediary to assist with proper disbursement of these cash allowances.

This Notice extends the temporary resources counting rules for Cash and Counseling participants to participants in Oregon's similar Independent Choices demonstration project. All participants in the Independent Choices demonstration project are consumers of personal assistance services.

Medicaid is the predominant source of public financing for personal assistance services programs for the aged, blind and disabled. The Secretary of the Department of Health and Human Services (DHHS) will exercise her authority under section 1115 of the Act to waive certain Medicaid provisions to permit the State of Oregon to exercise its Independent Choices demonstration. Medicaid beneficiaries who participate in this demonstration will be given cash to purchase the services they need from traditional and nontraditional providers, as they deem appropriate. Assistance will be available to help these

beneficiaries effectively use funds allotted for personal assistance services.

Many of the Medicaid beneficiaries who will participate in the Independent Choices demonstration are SSI beneficiaries or belong to coverage groups using eligibility methodologies related to those of the SSI program under title XIX of the Act. Under the Cash and Counseling demonstration project, the Commissioner of Social Security is testing the appropriateness of current SSI rules which require counting cash received for the purchase of medical or social services as resources if retained for more than one month after the month of receipt. This extension of the waiver of these SSI resources counting rules will help SSA obtain a larger test group of beneficiaries making provider hiring and payment decisions without a fiscal intermediary. Oregon will encourage participants to make their own fiscal decisions about providers. SSA will use these additional data for the evaluation of its policies on excluding cash received to purchase medical or social services. This SSA test will also assist the Secretary of DHHS in testing the possibility of providing greater autonomy to the consumers of personal assistance services by empowering them to purchase the services they require (including medical and social services) to perform their activities of daily living. In order to do so, the Commissioner has exercised his authority under section 1110(b) of the Act and waived SSI resources counting of cash received and conserved for future purchases of medical and social services.

The extension of this waiver of SSI resources counting rules will apply to participants in Oregon's Independent Choices demonstration project for the duration of their participation. Cash provided to participants for purchase of medical or social services must be conserved in a form that is separately identifiable from other resources that may be countable or excludable under title XVI of the Act. The cash received for medical or social services and conserved towards payment for those services by SSI beneficiaries who participate in this demonstration will not be included in SSI countable resources only for so long as the individual continues to participate in the Independent Choices demonstration project.

Existing SSI resource-counting rules are suspended only where application of such rules would adversely affect participation by SSI beneficiaries in the Independent Choices demonstration project.

<sup>26</sup> 15 U.S.C. 78s(b).

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

<sup>28</sup> 17 CFR 200.30-3(a)(12).