

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-55565; File No. SR-OCC-2007-04)

April 2, 2007

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Relating to Portfolio Margining of Customer Securities

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), notice is hereby given that on March 2, 2007, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change described in Items I, II, and III below, which items have been prepared primarily by OCC. The Commission is publishing this notice and order to solicit comments 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 proposed rule change amends OCC's Rule 611, Segregation of Long Option Positions, to allow a clearing member to instruct OCC to unsegregate a long options position that is carried in a customer's portfolio margining account.

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 these statements.

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

In a rule filing submitted in 2003 and subsequently approved by the Commission,¹ OCC created a "customers' lien account" in which clearing members are permitted to carry positions and collateral that are carried for customers at the firm level in portfolio margining accounts. In a regular customers account at OCC, all long positions must be "segregated" (i.e., held free of OCC's lien and therefore given no value in determining margin requirements) except when a long position is part of a customer spread. This practice was adopted to comply with Commission Rule 15c3-3, which requires that customers' "fully paid" and "excess margin" securities be held free of lien. Because it is anticipated that brokers will ordinarily be extending credit in portfolio margin accounts, the Commission approved OCC's rule filing effectively providing that longs in such accounts need never be treated as fully paid or excess margin securities. The Division of Market Regulation also issued a "no action" letter to the effect that no enforcement action would be taken against broker-dealers under Rule 15c3-3 for failing to segregate customer longs carried in portfolio margin accounts.²

OCC has been informed by several clearing members that a customers' lien account is not practical for them because their customer trades are routed to them from many sources and having more than one customers' account could result in a large number of clearing errors.³ OCC is therefore proposing an alternative procedure ("Proposed Procedure") for clearing members that are unable or that elect not to use a customers' lien account. Under the Proposed Procedure, a clearing member would be

¹ Securities Exchange Act Release No. 50509 (October 8, 2004), 69 FR 61289 (October 15, 2004) (OCC-2003-04).

² Letter to William H. Navin, Executive Vice President, General Counsel and Secretary, OCC (July 14, 2005).

³ Information from Jean Cawley, Deputy General Counsel (March 26, 2007).

permitted to carry portfolio margin positions in its regular securities customers' account at OCC. When the clearing member submits instructions to unsegregate customer longs that are part of a spread position, it will also submit instructions to unsegregate all longs that are carried at the firm level in customers' portfolio margin accounts. The result of the Proposed Procedure will be that long options required to be segregated in the customers' account will continue to be segregated and longs that would be unsegregated in a customers' lien account will be unsegregated in the regular customers' account.

The lien language in both the regular customers' account and in the customers' lien account provides in effect that to the extent that OCC has a lien on property in the account, the lien secures only other assets in that particular account. This limitation not only ensures that customer longs are not pledged to secure proprietary obligations of the firm in violation of the hypothecation rules, but it is conservative in that it does not allow the longs to secure positions in other customer accounts. Thus, to the extent that regular clearing member customers have unsegregated longs in the account, those positions would be subject to a lien securing the obligations of such clearing member with respect to its portfolio-margining customers whose short positions may be included in the account as well. Conversely, the longs belonging to portfolio-margining customers would collateralize the shorts of regular customers.

OCC believes that the proposed procedure is appropriate under Rule 15c3-3 and the hypothecation rules (Rules 8c-1 and 15c-2) and is appropriate as a matter of policy and fairness. There is no requirement to separate positions of portfolio margining customers from positions of other customers and the separate customers' lien account was intended merely as a convenience to avoid the need for daily submission of

instructions to unsegregate long positions in portfolio margining accounts. Clearing members that are willing to accept that burden in order to carry the positions in a regular customers' account should be permitted to do so. OCC has requested supplemental no-action relief from the Commission staff in order to confirm the applicability of the previous no-action relief to long positions in customer's portfolio margining accounts that are carried on an unsegregated basis in the regular customers' account at OCC rather than in a customers' lien account.

In SR-OCC-2003-04, Rule 611 was amended to provide that "all positions in cleared securities that are carried in a customers' lien account shall be deemed to be unsegregated for purposes of this Rule 611." Although OCC's rules do not specifically require that positions in a portfolio margin account at the firm level be carried in a customers' lien account at OCC, the rule filing indicated that they would be. In approving SR-OCC-2003-04 creating the customers' lien account and amending Rule 611, the Commission stated:

Under the portfolio margining methodology program, all long positions in the customers' lien account will be available as an offset to all short positions, regardless of the identity of the customer. This should provide for a greater diversification benefit to OCC's clearing members in the calculation of their margin. However, because all positions in the customers' lien account will be unsegregated and will be therefore subject to OCC's lien, the long positions in the account will be available to OCC in the event a clearing member fails to settle its obligations relating to a short position. Accordingly, because the proposed rule change is designed to ensure that transactions in securities which are eligible for the new portfolio margining approved by the Commission will be cleared and settled by OCC in a manner that will not reduce the adequacy of collateral available to OCC, the proposed rule change should not adversely affect OCC's ability to assure the safeguarding of securities and funds which are in OCC's custody or control or for which OCC is responsible.

The Commission's rationale for approving SR-OCC-2003-04 should apply to the Proposed Procedure as well. Rule 611 would simply be amended to provide an additional basis by which a clearing member may give instructions to release long options from segregation-- namely when they are carried for a customer in a portfolio margin account.

The proposed rule change is consistent with the purpose and requirements of Section 17A of the Act because it fosters cooperation and competition with persons engaged in the clearance and settlement of securities transactions, removes impediments to and perfects the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and in general protects investors and the public interest by facilitating the implementation of portfolio margining programs previously approved by the Commission. The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended.

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

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

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

Written comments were not and are not intended to be solicited with respect to the proposed rule change, and none have been received.

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

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder and particularly with the

requirements of Section 17A(b)(3)(F)⁴ of the Act, which requires that the rules of a clearing agency be designed to provide for the safeguarding of securities and funds which are in its possession or control or for which it is responsible. The proposed rule change will allow OCC's clearing members and their customers to benefit from the portfolio margining program, which includes having greater liquidity and more efficient use of collateral, in a manner that is consistent with OCC's overall risk management process.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing because such approval will allow OCC's members to immediately participate in the expanded portfolio margining pilot scheduled to be implemented on April 2, 2007.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-OCC-2007-04 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

⁴ 15 U.S.C. 78 q-1(b)(3)(F).

All submissions should refer to File Number SR-OCC-2007-04. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of OCC and on OCC's Web site at www.optionsclearing.com. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-OCC-2007-04 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-OCC-2007-04) be and hereby is approved on an accelerated basis.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁵

Florence E. Harmon
Deputy Secretary

⁵ 17 CFR 200.30-3(a)(12).