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Executive Vice President  
General Counsel and Secretary

May 15, 2014

**By Electronic Mail**

Kevin M. O'Neill  
Deputy Secretary  
U.S. Securities and Exchange Commission  
100 F. Street, N.E.  
Washington, DC 20549  
[rule-comments@sec.gov](mailto:rule-comments@sec.gov)

Re: *Proposed Rule Change by The Options Clearing Corporation to Reflect the Elimination of a Discount to the Clearing Fee Schedule; Release No. 34-71769; File No. SR-OCC-2014-05*

Dear Mr. O'Neill:

The Options Clearing Corporation ("OCC"),<sup>1</sup> is submitting this letter in further response to comments of market participants on OCC's recent rule filing to eliminate an existing clearing fee discount (the "Proposal").<sup>2</sup> The Proposal, which was filed with the Securities and Exchange Commission (the "Commission" or "SEC") for immediate effectiveness under Section 19(b)(3)(A) of the Securities Exchange Act, as amended ("Exchange Act"), would reinstate OCC's permanent clearing fee schedule for securities options and securities futures (the "Permanent Fee Schedule"). The Permanent Fee Schedule became effective May 1, 2007.<sup>3</sup> Subsequently, OCC has provided discounts to the Permanent Fee Schedule (the "Discounted Fee Schedule").<sup>4</sup> Elimination of the Discounted Fee Schedule is necessary and appropriate at this time to meet increased operating expenses and satisfy both existing requirements and pending

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<sup>1</sup> OCC is a registered clearing agency with the SEC and a registered derivatives clearing organization ("DCO") with the Commodity Futures Trading Commission ("CFTC"). The Financial Stability Oversight Council ("FSOC") has designated OCC as a systemically important financial market utility ("SIFMU").

<sup>2</sup> Exchange Act Release No. 71769 (March 21, 2014), 79 FR 17214 (March 27, 2014) (SR-OCC-2014-05).

<sup>3</sup> Exchange Act Release No. 55709 (May 4, 2007), 72 FR 26669 (May 10, 2007) (SR-OCC-2007-05).

<sup>4</sup> *Id.*; see also Exchange Act Release Nos. 56386 (September 11, 2007), 72 FR 53273 (September 18, 2007) (SR-OCC-2007-09); 57192 (January 24, 2008), 73 FR 5618 (January 30, 2008) (SR-OCC-2007-17).

regulatory changes that would require OCC to hold liquid net assets funded by equity sufficient to cover a minimum of six months' projected operating expenses, as discussed further below.<sup>5</sup>

## **I. COMMENTS ON THE PROPOSAL**

To date, the SEC has received four comments on the Proposal.<sup>6</sup> On April 17, 2014, OCC submitted a letter in response to the Kramer I Letter, which at the time was the only comment appearing in the SEC's public comment file.<sup>7</sup> Subsequently, the SIFMA Letter, STA Letter and Kramer II Letter were also submitted and published in the SEC's public file. OCC appreciates the opportunity to respond to these additional comments.

## **II. RESPONSES TO COMMENTS**

### **A. OCC's Increased Costs of Operation**

The SIFMA Letter, STA Letter and Kramer II Letter each asked OCC to provide more detail regarding its increased costs of operation.<sup>8</sup> In the Proposal, and in greater detail in the OCC Letter, we identified several factors responsible for a significant increase in OCC's ongoing costs of operation: engagement of outside professionals to address various regulatory issues arising under the Dodd-Frank Act, including OCC's designation as SIFMU; costs related to assessing and achieving compliance with international standards on which the SEC based its recently proposed Standards for Covered Clearing Agencies (the "CCA Release");<sup>9</sup> and rising

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<sup>5</sup> Subsequent to the Proposal, OCC submitted a proposed rule change with the SEC (SR-OCC-2014-11) that is designed to clarify that the special, reduced clearing fee rate charged for "Market Maker/Specialist Scratch Trades" also applies to "Linkage Fees." OCC implemented the linkage fee in 2012 to provide the same discount from the general pricing structure for certain "routing broker scratch trades" that applies to market maker/specialist scratch trades because both types of transactions exist to facilitate fair and orderly markets. Clarification was necessary to correct an inadvertent omission of the words "and Linkage Fees" in the line item that addresses Market Maker/Specialist Scratch trades in the Proposal's fee schedule. Going forward, both Market Maker/Specialist Scratch fees and Linkage fees will be discounted at the same rate, but the charge for both will be two cents per side rather than one cent per side.

<sup>6</sup> Letters from Howard L. Kramer, Partner, Willkie Farr & Gallagher LLP (March 26, 2014) ("Kramer I Letter") and (April 24, 2014) ("Kramer II Letter") (collectively, the "Kramer Letters"); letter from Ellen Greene, Vice President of Financial Services Operations, Securities Industry and Financial Markets Association (April 17, 2014) ("SIFMA Letter"); and letter from John Daley, Chairman, and James Toes, President & CEO, Security Traders Association (April 17, 2014) ("STA Letter").

<sup>7</sup> Letter from James E. Brown, General Counsel, The Options Clearing Corporation (April 17, 2014) ("OCC Letter").

<sup>8</sup> SIFMA Letter at 2; STA Letter at 2; Kramer II Letter at 5.

<sup>9</sup> Exchange Act Release No. 71699 (March 12, 2014), 79 FR 16866 (March 26, 2014).

costs, including employee costs, as OCC enhances its resources to demonstrate its compliance with the new standards and to respond to increased requests from regulators. Moreover, OCC is already subject to a CFTC regulatory obligation to have sufficient financial resources to cover operating costs for at least one year (calculated on a rolling basis and comprised of cash and/or highly liquid securities equal to at least six months' operating costs)<sup>10</sup> and the SEC has proposed a requirement to obligate OCC to hold liquid net assets funded by equity in a minimum amount equal to six months' current operating expenses.<sup>11</sup>

OCC's need to come into compliance with proposed SEC Rule 17Ad-22(e)(15) in particular represents a significant part of OCC's need for additional revenues. The rule would require OCC to cover potential general business losses so that it could continue operating if such losses were to materialize by requiring OCC to hold liquid net assets funded by equity equal to the greater of (i) six months operating expenses or (ii) an amount determined by OCC's Board to be necessary to recover or wind down OCC's critical operations and services necessitated by credit losses, liquidity shortfalls, losses from general business risk or any other losses. A substantial portion of OCC's net income has been refunded each year to market participants, including a \$47 million refund for 2013 that will be paid out by September of this year. As a result of the liability booked to reflect the pending refund, OCC's net working capital is approximately \$25 million, or the equivalent of approximately one and a half months' of operating expenses. OCC agrees that a SIFMU like OCC, that holds nearly \$100 billion in customer margin and guarantees settlement obligations to market participants, should maintain equity capital in line with the new SEC requirements,<sup>12</sup> resulting in the need to increase its equity capital in the near term.

Commenters request additional detail to justify the amount of capital needed by OCC, but the Commission itself, in Table 2 within the CCA Release, has already published information responsive to these requests.<sup>13</sup> Table 2 is part of the economic analysis prepared by the SEC regarding proposed Rule 17Ad-22(e)(15). In relevant part, and based on financial data from OCC's Annual Reports from 2008 to 2012, the table provides an estimated upper bound of \$68 million and a lower bound of \$63 million in additional equity that OCC likely needs to raise to comply with the rule. The SEC explains that it provided the upper and lower bounds using different assumptions of how much of OCC's cash and cash equivalents is first funded by liabilities versus being funded pro-rata by equity and liabilities.<sup>14</sup> OCC's own computations are consistent with the SEC estimates and, based on the proportion of cash and cash equivalents on

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<sup>10</sup> 17 C.F.R. 39.11(a)(2), (e)(2).

<sup>11</sup> CCA Release at 16906 (discussing the proposal of Rule 17Ad-22(e)(15)).

<sup>12</sup> See remarks by Craig Donohue, Executive Chairman, OCC, Options Industry Council ("OIC") conference, Heightened Expectations for Systemically Important Clearing Houses: How OCC is Meeting the Challenge (May 1, 2014), [http://www.theocc.com/about/press/releases/2014/05\\_01.jsp](http://www.theocc.com/about/press/releases/2014/05_01.jsp)

<sup>13</sup> CCA Release at 16963.

<sup>14</sup> *Id.*

OCC's balance sheet funded by liabilities and equity,<sup>15</sup> we believe the upper bound of \$68 million is the more accurate estimate.

As noted above, increased capital requirements are not the only factor driving OCC's need for additional revenue. With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") and similar initiatives around the globe, regulation of central counterparties like OCC has been transformed. The net result is that regulatory standards for clearinghouses are becoming similar to those in place for complex, systemically important banking institutions. This has fundamentally altered the environment in which OCC operates and has increased OCC's need for additional resources, in particular in control functions such as compliance, enterprise risk management and internal audit, as well as areas such as risk management and model validation. For example, OCC's 2013 workforce planning initiative resulted in a decision to add 51 new employees in 2014, 36 of which will be working on tasks associated with the increased regulatory expectations, including compliance and other control functions. As a result, OCC projects an increase in total employee costs for 2014 of approximately 20% over the cost for 2013. In addition, the initiative identified the need to add 46 consultants in 2014 to work on these matters as well, resulting in a projected increase for professional consulting fees for 2014 of approximately 35% over 2013. Overall, OCC projects an increase in total operating expenses for 2014 of more than 15% over 2013.<sup>16</sup>

While OCC seeks to be appropriately transparent with respect to the basic elements of its operating costs, we believe that the Proposal does not require, and that it would be inappropriate for the SEC to conduct, a line item review of OCC's operating budget. Additional detailed information about OCC's budget is simply not germane to the issue immediately at hand. OCC's budgets are established using a thorough and lengthy process subject to detailed review by OCC's Board. OCC's Board is dominated by representatives of clearing members and public directors who have strong incentives to keep costs as low as possible, and OCC believes that it has an excellent record in doing so over its entire history. Particularly since OCC and the SEC have already reached the same conclusion as to the amount of additional capital required for OCC to satisfy proposed Rule 17Ad-22(e)(15), we believe that it would serve no purpose to suspend effectiveness of the Proposal to debate whether OCC's projected operating costs are appropriate. This matter is properly left to OCC's SEC-approved governance structure, over which there is no shortage of regulatory oversight.

#### B. OCC's Inability to Forecast Reinstatement of Discounts

Commenters suggest that reinstatement of the Permanent Fee Schedule represents a cost increase that is potentially perpetual, and they express concern that there is a "lack of a defined

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<sup>15</sup> OCC, *2013 Annual Report*, 19 (2013) (the Statements of Financial Condition provides data as of December 31, 2013 and 2012 that is illustrative of the relationship between OCC's assets, liabilities and shareholders' equity).

<sup>16</sup> *See supra* note 12.

exit strategy from the fee schedule once OCC raises the required level of capital and surplus.”<sup>17</sup> We understand these concerns in sum to be a request for OCC to clarify the projected timeframe and criteria concerning when fees will again be discounted and the amount of any discount. As noted in the Proposal and OCC Letter, we expect OCC’s capital needs to affect 2014 but do not presently expect them to materially carry over to 2015 or subsequent years. Of course, OCC’s fee schedule must at all times cover OCC’s projected operating expenses, its reasonable reserves and the additional surplus deemed advisable by the Board, as provided in Article IX, Section 9, as described more fully below.

As explained in the OCC Letter, OCC operates as a market utility and essentially on an at-cost basis. Consistent with this model, the method for determining the level of OCC’s clearing fees is set forth in Article IX, Section 9 of OCC’s By-Laws, which provides that clearing fees are to be set at a level sufficient to cover operating expenses, maintain reserves reasonably necessary to the conduct of OCC’s business and accumulate such additional surplus as the Board deems advisable for OCC to meet its obligations to clearing members and the general public. OCC is required under Section 19(g)(1) of the Exchange Act to comply with its By-Laws and therefore also with this “at-cost” framework in its fee structure.<sup>18</sup> OCC’s annual financial statements are available on its website, so that its total operating expenses figure (\$165.4 million in 2013) and its total shareholders’ equity figure (\$25.4 million as of December 31, 2013) are available to the public. From that information, one can readily determine whether OCC’s fees continue to be set at a level specified in Article IX, Section 9.

The at-cost fee structure in Article IX, Section 9 coupled with the rule filing process for self-regulatory organizations (“SROs”) under the Exchange Act creates a well-defined “exit strategy” from the Permanent Fee Schedule because it causes OCC to operate essentially as an at-cost market utility, the structure is binding on OCC, it is publicly available as part of the By-Laws on OCC’s website and any subsequent fee schedule changes by OCC to comply with its requirements must be conducted in the public domain as part of the SRO rule filing process. This structure represents a built-in limitation on the amount of capital OCC is permitted to raise through the collection of clearing fees and provides clear opportunities for public comment on changes to the fee structure. Accordingly, commenters can take comfort that OCC cannot continue the Permanent Fee Schedule without direct regard for its expenses and capital needs. Failure to do so would violate OCC’s By-Laws and therefore the Exchange Act.

While the “exit strategy” is dictated by the existing governance structure, it is impossible for OCC to predict with accuracy the exact level of fees that will be required on an on going basis once the minimum additional capital goal of \$68 million has been accumulated, or exactly when that will be. OCC’s on going fee schedule and refund policies will also need to be informed by the status and content of the longer-term capital plan OCC is developing to model

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<sup>17</sup> SIFMA Letter at 2; *see also* Kramer II Letter at 3; STA Letter at 2 (the STA Letter provided a closely related comment advocating for a policy and procedure for any reconciliation performed should the increased schedule of fees result in an over-collection).

<sup>18</sup> 15 U.S.C. 78s(g)(1).

expenses, capital requirements, fees and refunds so that OCC's fee structure is more predictable to its users. As noted above, there will be opportunities for all interested constituencies to express their views in that process.

### C. Alternative Funding Solutions Considered

Commenters requested additional information on the basis for OCC's decision to reinstate its Permanent Fee Schedule rather than raise capital to meet operating costs using other methods.<sup>19</sup> As explained in the OCC Letter, OCC studied and carefully developed several alternative methods which were all presented to the Performance Committee of the Board.<sup>20</sup> These alternatives were: (i) issuing capital stock to clearing members; (ii) securing capital contributions from existing stockholder exchanges; (iii) issuing perpetual preferred shares to outside institutional investors; (iv) undertaking a complete recapitalization of OCC based upon a strategic realignment of OCC's governance structure and its market utility business model; and (v) accumulating retained earnings by removing the Discounted Fee Schedule. In advance of developing and considering these alternatives, OCC also considered issuing subordinated debt.

In addition to considering the steps needed to carry out each of these approaches, OCC and its Board were mindful of the likely compliance deadline for meeting increased liquid net asset requirements based on projected operating expenses.<sup>21</sup> Moreover, we note that proposed SEC Rule 17Ad-22(e)(15) requires that the liquid net assets held by OCC must be "funded by equity."

We are providing immediately below executive summaries of the approaches to raising capital that were developed and considered.

#### Private Placement of Unsecured Notes

Before it became clear that the SEC intended to propose the standards in the CCA Release for adoption, thereby requiring OCC to maintain liquid net assets "funded by equity" to meet future operating expenses, OCC had intended to enhance its liquid resources through the issuance of unsecured senior notes. This approach was abandoned when it became apparent that it would not satisfy the anticipated regulatory requirements of Proposed Rule 17Ad-22(e)(15), which OCC believes are reasonably likely to become effective by year end.

#### Issuance of Capital Stock to Clearing Members

OCC considered issuance of capital stock to clearing members to obtain an infusion of additional capital. Potential variations in the particular type of capital stock to be issued were

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<sup>19</sup> SIFMA Letter at 2; Kramer II Letter at 2.

<sup>20</sup> OCC Letter at 6.

<sup>21</sup> For example, we noted in footnote 8 of the Proposal that OCC reasonably anticipates that the requirements of proposed SEC Rule will need to be met by the end of 2014.

also considered. This approach would have required significant changes to OCC's organizational documents and capital and governance structures to support a capital stock issuance that consequently would have required approvals by each of OCC's stockholder exchanges and the Board. OCC also took into consideration OCC's likely inability to receive tax deductions for dividends paid as well as the risk that future clearing fee refunds to clearing members that are stockholders might be treated as dividends taxable as such to clearing members. These considerations caused issuance of capital stock to clearing members to be an unattractive alternative, at least in the near term, and in any event could not be relied upon to produce the required funds within the applicable time frame.

#### Additional Capital Contribution by Stockholder Exchanges

OCC considered the possibility of obtaining additional capital contributions from OCC's stockholder exchanges. As stated in the OCC Letter, OCC's not-for-profit model pursuant to Article IX, Section 9, which delivers OCC's low-cost clearing solution to options market participants, also prevents OCC from paying dividends to OCC's stockholder exchanges. Because stockholder exchanges receive no investment return from OCC's activities, they have no incentive to make additional capital contributions, and OCC has no power to compel them to do so. Changing OCC's longstanding utility model in order to provide investment incentives would require very significant changes to OCC's organizational documents, capital structure and governance structure. These changes are not feasible in the short term, and it is not at all clear that they would result in lower clearing fees.

#### Issuance of Perpetual Preferred Shares to Institutional Investors

Another method that was considered was issuance of a class of perpetual preferred stock that would grant OCC a redemption right after a number of years. Like the alternative described above regarding issuance of capital stock to clearing members, this alternative would require approvals from each of OCC's stockholder exchanges and by the Board. Issuing stock to outside investors would also introduce a need to carefully consider what voting rights and liquidation rights would be needed to make the stock attractive to potential outside investors while at the same time balancing the implications of those rights on OCC's governance structure. While OCC is continuing to seriously evaluate this alternative, it is not a viable short term solution because of, among other things, continuing uncertainty as to whether capital sourced from an issuance of preferred stock would meet the "funded by equity" requirement.

#### Comprehensive Recapitalization with Rebalancing of Common Equity Ownership

Finally, a comprehensive recapitalization was considered that would entail rebalancing of common equity ownership among OCC clearing members and potentially among outside investors. Of all of the alternatives considered, this option would likely require the most significant changes to OCC's organizational documents. Such changes would require consent of all stockholder exchanges, the affirmative vote of two-thirds of OCC's Board and regulatory approvals for changes to the rules of OCC.

## Elimination of the Discounted Fee Schedule

The By-Laws require OCC's fee structure to be designed "to cover the operating expenses of [OCC] . . ." and "maintain such reserves as are deemed reasonably necessary by the Board of Directors" to conduct certain development and planning activities in connection with OCC's services and "accumulate such additional surplus [above \$1 million and amounts received from sales of stock to exchanges] as the Board of Directors may deem advisable to permit the Corporation to meet its obligations to clearing members and the general public."<sup>22</sup> Because the number of stockholder exchanges is now effectively capped at the current five,<sup>23</sup> and for the reasons discussed above, OCC cannot expect to receive additional capital from sales of stock to its stockholder exchanges. The fee structure that has been in place since the founding of OCC clearly contemplates that necessary additions to capital will come from retained earnings and *requires* that fees be set at an amount sufficient to provide it. While OCC is not prohibited from accessing other sources of capital, OCC's Board for the reasons described above has concluded that there are no alternative sources of funding that can be relied upon to provide sufficient net liquid assets "funded by equity" to comply with new capital requirements in the timeframe in which they are expected to become effective.

Elimination of the Discounted Fee Schedule does not require changes to OCC's organizational documents or require that OCC devote resources to developing and implementing such changes. There is no doubt that retained earnings meet the "funded by equity" standard. In determining the amount of increased revenue needed from clearing fees to meet operating costs, OCC also took into account that such revenues are taxable income to OCC and deductible as business expenses to clearing members (and market-makers, to the extent they are passed through). Section 19(b)(3)(A) of the Exchange Act permits a proposed rule change to become effective immediately if it is designated by the SRO as "establishing or changing a due, fee or other charge on any person, whether or not the person is a member of the self-regulatory organization," thus assuring that an SRO can respond quickly to its funding needs by adjusting its fee schedule.<sup>24</sup>

It is consistent with OCC's industry utility model to raise the needed liquid net assets through clearing fees because it places the funding obligation for operating expenses on users who benefit most from OCC's clearance and settlement services.

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<sup>22</sup> OCC Article IX, Section 9.

<sup>23</sup> Exchange Act Release No. 46469 (September 6, 2002); 67 FR 58093 (September 13, 2002) (SR-OCC-2002-02) (SEC order approving OCC's proposed rule change relating to providing clearing services to options exchanges that are not stockholders).

<sup>24</sup> The words "on any person, whether or not the person is a member of the self-regulatory organization" were added by Section 916 of the Dodd-Frank Wall Street Reform and Consumer Protection Act and make clear that the potential pass through of fees to customers of a clearing member is not a reason to set aside the immediate effectiveness of the filing. *See* Pub. L. No. 111-203, 124 Stat. 1835 (2010) (amending the Exchange Act at 15 U.S.C. 78s(b)(3)(A)).

#### D. Communications Regarding the Proposal

In their letters, some commenters expressed concern over the timing and amount of notice concerning the Proposal.<sup>25</sup> OCC has satisfied all applicable notice requirements under the Exchange Act, and these comments do not form any legal basis for suspending the effectiveness of the Proposal. OCC had to balance notice considerations against the ultimate need to act quickly enough to assure it will remain in compliance with its regulatory requirements. The CCA Release and Rule 17Ad-22(e)(15) were proposed by the SEC on March 12, 2014 and are not yet final. However, OCC has limited ability to predict the precise effective date. In response to that uncertainty, OCC has calculated that by reverting to the Permanent Fee Schedule as of April 1, 2014 it has reasonable assurance of meeting the increased capital requirements before year end, which is considered to be the earliest likely effective date. To have delayed implementation pending more extensive discussions would have led OCC to need higher fees to raise the same amount of capital over a shorter period, jeopardized OCC's ability to comply with the SEC's new regulation and been of questionable value given the absence of practical alternatives under the circumstances.

OCC is committed on an ongoing basis to meeting its obligations to participants and the public under the Exchange Act to help them understand the risks and costs of OCC's services.<sup>26</sup> It was in that interest that OCC met with clearing members likely to be most affected by the Proposal and also published to all clearing members two Information Memos in advance of filing the Proposal to notify them of the likely effect on refunds, including an explanation that the effect on refunds is not expected to extend beyond 2014 based on current projections. These efforts were meaningful attempts to provide notice of the Proposal, and we note further that many of SIFMA's members and two of the market makers identified in the Kramer Letters are in fact OCC clearing members that received these notifications and therefore had notice and an opportunity to discuss the filing with OCC in advance of its submission. At a recent industry conference of the OIC, our Executive Chairman reaffirmed OCC's commitment to communication with options market participants,<sup>27</sup> and going forward, we emphasize that OCC invites direct feedback from clearing members in response to Information Memo releases and encourages commenters generally to participate in and express their views through OCC sponsored forums, such as OIC roundtables. Meanwhile, however, OCC has taken the only action available to it to assure its important obligation to remain in regulatory compliance.

#### E. Liquid Net Assets Are Not a "Rainy Day Account" for Stockholders

It was asserted by one commenter that the heightened financial resources OCC needs to meet its operating expenses, including its obligations under proposed SEC Rule 17Ad-22(e)(15), do not reflect operating expenses but instead represent a "rainy day account" that "will be an

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<sup>25</sup> SIFMA Letter at 2; Kramer II Letter at 3.

<sup>26</sup> 17 C.F.R. 240.17Ad-22(d)(9).

<sup>27</sup> *See supra* note 12.

OCC asset of sole benefit to the OCC stockholders” and that “[t]o require others to provide those funds would be inappropriate. . .”<sup>28</sup> These assertions are not accurate. The increased revenues from the elimination of the Discounted Fee Schedule would not fund an all-purpose reserve benefitting stockholders but rather would be specifically earmarked for ongoing and future operating costs.

OCC’s stockholder exchanges receive no economic benefit from OCC’s retention of liquid net assets to meet potential business losses as required by proposed Rule 17Ad-22(e)(15). The liquid net assets are not available for use by the stockholder exchanges or for distribution to them. Instead, the purpose of the liquid net assets is to permit OCC to continue to meet its regulatory responsibilities to clearing members, their customers and the public even if it were to suffer substantial general business losses. For the reasons discussed above, the stockholder exchanges are not in a position to be able to realize any financial benefit from this additional capital cushion other than the enhanced assurance of continued clearing services to support their markets.

When the FSOC designated OCC as a SIFMU, it found that “a failure or disruption to OCC could increase the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability of the financial system of the United States.”<sup>29</sup> Therefore, given OCC’s systemic importance to the U.S. financial system, requiring the maintenance of liquid net assets to cover its potential business losses and, if necessary, safely wind down OCC’s business operations is far from solely beneficial to OCC’s stockholders. OCC’s continued stability is in the interest of the financial system of the United States, including but not limited to options market makers who directly rely on the continuous presence of safe and reliable facilities for clearance and settlement to allow them to effectively conduct their business and serve customers. It is not unreasonable, and certainly not inconsistent with the Exchange Act, for market participants that enjoy the benefit of the safety and resilience OCC provides to the options markets to pay for and maintain safeguards and protections required by law.

To the extent commenters object to the increased capital requirement imposed by the SEC in proposed Rule 17Ad-22(e)(15), it would be more appropriate to direct those objections to the SEC by submitting comments on the CCA Release.<sup>30</sup>

#### F. OCC Must Ensure Equitable Allocation of Fees Among Clearing Members

One commenter objected to OCC’s statement that reinstatement of the Permanent Fee Schedule applies uniformly because, according to that commenter, clearing members typically

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<sup>28</sup> Kramer II Letter at 2.

<sup>29</sup> 2012 Annual Report of the FSOC, Appendix A at 187, <http://www.treasury.gov/initiatives/fsoc/Documents/2012%20Appendix%20A%20Designation%20of%20Systemically%20Important%20Market%20Utilities.pdf>.

<sup>30</sup> The comment period for the CCA Release is scheduled to close on May 27, 2014.

pass clearing fees through to their customers.<sup>31</sup> The commenter's point appears to be that customers will bear a disproportionate share of the increased fees. Under Section 17A(b)(3)(E) of the Exchange Act, a registered clearing agency is expressly prohibited from maintaining rules that impose "any schedule of prices or fixing rates or other fees for services rendered by its participants."<sup>32</sup> Accordingly, OCC cannot dictate the proportion of the burden of increased fees that ultimately falls on customers and clearing members. Similarly, it has no ability to impose fees on participant exchanges. OCC's statutory obligation with respect to allocation of fees under Section 17A(b)(3)(D) of the Exchange Act is limited to "the equitable allocation of reasonable dues, fees, and other charges among its participants."<sup>33</sup> This standard is clearly met by the Proposal.

#### G. Immediate Effectiveness is Consistent with the Exchange Act

Commenters have stated that as a matter of policy that they would prefer for the Proposal to have been filed under alternative provisions of the SRO rule filing framework, but do not identify any legal basis to suggest that OCC was not entitled to file the Proposal for immediate effectiveness, as specifically permitted by the Exchange Act.<sup>34</sup> In the OCC Letter, we cited the operative provisions from Section 19(b)(3)(A)(ii) of the Exchange Act and SEC Rule 19b-4(f)(2) that plainly support the immediate effectiveness of the Proposal. These provisions are controlling. Other commenters have conceded this point but suggest that the SEC should nevertheless suspend effectiveness to allow further consideration.<sup>35</sup> Given that the immediate elimination of the Discounted Fee Schedule is essential to assure that OCC will be able to comply with the SEC's own proposed regulations, it would be highly inappropriate for the SEC to do so. As we have noted, the adoption of a longer term capital plan and consideration of alternative sources of funding is a project already underway, and there will be ample opportunity for all constituencies to be heard in that process. Meanwhile, it is both essential, and entirely consistent with the provisions of the Exchange Act and sound regulatory policy, for OCC to be permitted to use the only practical means available to comply with proposed regulatory requirements within the relevant time frame.

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<sup>31</sup> Kramer II Letter at 4.

<sup>32</sup> 15 U.S.C. 78q-1(b)(3)(E).

<sup>33</sup> Under Section 3(a)(24) of the Exchange Act, "[t]he term 'participant' when used in respect to a clearing agency means any person who uses a clearing agency to clear or settle securities transactions or to transfer, pledge, lend, or hypothecate securities. *Such term does not include a person whose only use of a clearing agency is (A) through another person who is a participant, or (B) as a pledgee of securities.*" [emphasis added].

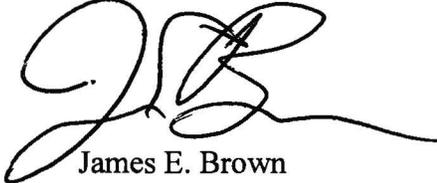
<sup>34</sup> Kramer II Letter at 5 (cross referencing policy statements in the Kramer I Letter at 3).

<sup>35</sup> STA Letter at 3.

### III. CONCLUSION

Throughout OCC's 40 year history, our clearing fees have remained the lowest in the industry, in most cases by a significant margin,<sup>36</sup> and we have refunded more than \$2 billion to clearing members, many of which primarily pass on those refunds to users of the markets OCC serves. OCC takes very seriously commenters' concerns regarding the impact of clearing fees on market participants. We believe in particular that quantifying OCC's increased operating costs in relationship to proposed Rule 17Ad-22(e)(15) should help commenters and the public better understand the capital targets that OCC must achieve to meet current and reasonably projected operating costs. Moreover, OCC will continue to monitor its expenses and the related fees it imposes with the goal of discharging its risk management obligations as a SIFMU while at the same time providing cost-effective clearing services and operating in compliance with OCC's market utility structure established in Article IX, Section 9 of its By-Laws. No basis exists under the Exchange Act on which to summarily temporarily suspend the Proposal. It is entirely consistent with the Exchange Act and the rules and regulations thereunder applicable to OCC as well as with the public interest and protection of investors. It should remain effective as filed.

Sincerely,



James E. Brown

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<sup>36</sup> See *supra* note 12.