

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62879; File No. SR-OCC-2010-15)

September 9, 2010

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Interpret By-Laws as to Dividend Adjustments

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ notice is hereby given that on August 31, 2010, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I and II below, which items have been prepared primarily by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested parties.

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

The purpose of the proposed rule change is to amend Interpretation and Policy .01 under Article VI, Section 11A of OCC’s By-Laws to allow the Securities Committee under certain conditions to cease adjusting for recurring cash dividends previously deemed to be non-ordinary dividends.

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

¹ 15 U.S.C. 78s(b)(1).

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.²

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

The principal purpose of this rule change is to amend Interpretation and Policy .01 under Article VI, Section 11A of OCC's By-Laws. Under that Interpretation, cash dividends or distributions of an issuer which are deemed by the Securities Committee³ to be non-ordinary will usually result in an adjustment to the terms of listed stock options.⁴

OCC is proposing to amend Interpretation .01 to allow the Securities Committee under certain conditions to cease adjusting for recurring cash dividends previously deemed to be non-ordinary dividends. Interpretation .01 under Section 3 of Article XII of OCC's By-Laws, which provides that non-ordinary (as determined by OCC) cash dividends or distributions of an issuer will usually occasion an adjustment to the terms of listed stock futures, would similarly be amended. The discussion below addresses the proposed amendments to Interpretation .01 of Section 11A of Article VI, but the purpose

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

³ The Securities Committee is comprised of one designated representative of each participant exchange and the Chairman of OCC or his designee. The OCC representative is not a voting member of the Committee except in cases of tie votes. Article VI, Section 11(c) of OCC's By-Laws.

⁴ Generally speaking, a cash dividend or distribution would be deemed to be "ordinary" if it is declared pursuant to a policy or practice of paying such dividends on a quarterly or other regular basis. Dividends paid outside such practice would be considered "non-ordinary". Non-ordinary cash dividends usually would trigger an adjustment to options contracts subject to the minimum size requirement. Article VI, Section 11A, Interpretation and Policy .01 of OCC's By-Laws. See Securities Exchange Act Release No. 55258 (February 8, 2007).

behind those changes is equally applicable to the changes proposed to Interpretation .01 of Section 3 of Article XII.⁵

The amendment was prompted by a series of cash dividends declared by Diamond Offshore Corporation (“DO”). DO characterized these dividends as “special” and differentiated them from the company’s “regular” cash dividends. These “special” and “regular” DO dividends have customarily gone “ex-distribution” on the same date. Initially, the Securities Committee deemed these “special” dividends to be non-ordinary under Interpretation .01 and appropriately adjusted listed options in response.⁶ Since Interpretation .01 was revised effective February 1, 2009, DO options have been adjusted for five successive quarterly “special” dividends. Notwithstanding that these dividends were characterized by DO as “special” dividends and clearly differentiated from the company’s “regular” dividends, OCC and the options exchanges have received strong feedback from investors that such dividends have been declared so consistently and thereby have achieved such predictability that they should no longer be considered “non-ordinary” for adjustment purposes. Furthermore, the options exchanges and many OCC clearing member firms believe that the proliferation of option strikes caused by successive quarterly adjustments will have an adverse affect on liquidity and occasion other adverse operational effects.⁷ The Securities Committee also solicited the opinion of

⁵ Stock futures likewise are adjusted in response to non-ordinary cash dividends or distributions. See Article XII, Section 3, Interpretation and Policy .01, of OCC’s By-Laws. See Securities Exchange Act Release No. 46595 (October 3, 2002).

⁶ In like manner, options on Oil Service HLDRS Trust (OIH) which contain DO as a component security and make pro-rata distributions in response to DO dividends, were also adjusted.

⁷ The standard method of adjustment is to reduce strike prices by the amount of the dividend. Options with “standard” strike prices are then reintroduced by the

participant members of the OCC Clearing Member Roundtable regarding this issue.⁸ The Roundtable strongly supported authorizing the Securities Committee to cease adjusting for “special” cash dividends whose consistency and predictability of payment have been demonstrated.

The proposed amended Interpretation .01 enumerates factors that the Securities Committee may take into account in determining whether a dividend is “ordinary.” Importantly, it allows the Securities Committee to reclassify as “ordinary” dividends previously deemed “non-ordinary.” The conditions under which this may occur are as follows: (1) the issuer discloses that it intends to pay such dividends or distributions on a quarterly or other regular basis, (2) the issuer has paid such dividends or distributions for four or more consecutive months or quarters or two or more years after the initial payment, whether or not the amounts paid were the same from period to period, or (3) the Securities Committee determines for other reasons that the issuer has a policy or practice of paying such dividends or distributions on a quarterly or other regular basis.⁹

It is the intent of the Securities Committee that any such recharacterization of a dividend as “ordinary” would be announced in advance to investors. For example, after

listing option exchange(s). With each successive adjustment, this process is repeated, proliferating strike prices. Liquidity naturally gravitates to the options with standard strike prices at the expense of liquidity for options with non-standard strikes.

⁸ The OCC Roundtable is an OCC sponsored advisory group comprised of representatives from OCC’s participant exchanges, OCC, a cross-section of OCC clearing members, and industry service bureaus. The Roundtable considers operational improvements that may be made to increase efficiencies and lower costs in the options industry.

⁹ These same factors would be used by OCC to reclassify a recurrent non-ordinary dividend as “ordinary” with respect to its determination to adjust stock futures.

adjusting for a given dividend, OCC would announce that subsequent dividends of the same nature would no longer occasion adjustment.¹⁰ A discussion of the new adjustment approach also will be included in published interpretative guidance.¹¹ Clean and marked copies of the interpretative guidance are attached as Exhibit 5 to the OCC filing of the proposed rule change. The marked copy shows changes from the current language.

In fairness to existing holders of open interest (especially DO and OIH) who may have assumed option positions with the belief that OCC would continue to adjust for recurring “special” dividends, OCC has determined that the portion of Interpretation .01, which allows recharacterization of dividends as ordinary will be effective only for dividends and distributions announced after February 1, 2012. This date is chosen because it occurs after the latest expiration of all existing open interest in DO and OIH options (inclusive of LEAPS options). All existing open interest and any positions created with new expiration dates occurring before February 1, 2012, will thus be “grandfathered” under the current adjustment approach for these dividends.¹²

OCC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act¹³ and the rules and regulations thereunder applicable to OCC

¹⁰ OCC will follow a similar practice with respect to stock futures.

¹¹ Securities Exchange Act Release Nos. 58059 (June 30, 2008) and 59442 (February 24, 2009). Consistent with past practice, the interpretative guidance will be available on OCC’s public website but not incorporated into OCC’s By-Laws and Rules. Other technical or clarifying changes have also been made to update the guidance. For example, the use of the term “special dividend” has been removed in favor of the term “non-ordinary.”

¹² For consistency, the changes to the Interpretation relating to stock futures also will not be effective until February 1, 2012.

¹³ 15 U.S.C. 78q-1.

because it provides for the prompt and accurate clearance and settlement of securities transactions, ensures the protection of investors and reduces unnecessary costs and burdens on them and persons facilitating transactions on their behalf. It does so by responding to strong investor feedback regarding the need to cease treating certain cash dividends or distributions as “non-ordinary” for adjustment purposes based on the consistent declaration of such dividends, by publishing information regarding those factors which would lead OCC to make such a determination, and by reducing the likelihood of series proliferation in the case of options contracts. 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 have any impact on or impose any burden on competition.

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

No written comments relating to the proposed rule change have been solicited or received. OCC will notify the Commission of any written comments received by OCC.

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

The foregoing rule change has become effective upon filing pursuant to Section 19(b)(3)(A)(i) of the Act¹⁴ and Rule 19b-4(f)(1)¹⁵ thereunder because the proposed rule

¹⁴ 15 U.S.C. 78s(b)(3)(A)(i).

¹⁵ 17 CFR 240.19b-4(f)(1).

constitutes an interpretation with respect to the meaning, administration, or enforcement of an existing rule. At any time within sixty days of the filing of such rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

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-2010-15 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-OCC-2010-15. 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 website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule changes 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, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filings also will be available for inspection and copying at the principal office of OCC and on OCC's website at <http://www.theocc.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-2010-15 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.¹⁶

Elizabeth M. Murphy
Secretary

¹⁶ 17 CFR 200.30-3(a)(12).