

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-88030; File No. SR-OCC-2020-001)

January 24, 2020

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change to Modify the Fees for Exercise Notices Submitted after the Deadlines and to Change the Deadline for Submitting a Late Exercise Notice on Non-Expiration Dates

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act” or “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on January 14, 2020, the Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

This proposed rule change by OCC would amend Rules 801 and 805 to modify the fees for exercise notices submitted after the deadlines and to amend Rule 801 to change the deadline for submitting a late exercise notice on non-expiration dates. The proposed changes to OCC’s Rules are included in Exhibit 5 of the filing. Material proposed to be added to OCC’s Rules as currently in effect is marked by underlining and material proposed to be deleted is marked with strikethrough text. All terms with initial

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

capitalization that are not otherwise defined herein have the same meaning as set forth in the By-Laws and Rules.³

II. Clearing Agency'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) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(1) Purpose

The purpose of this rule filing is to: (1) amend Rule 801 for exercises on non-expiration dates and Rule 805 for exercises on expiration dates to modify the fee applied to exercise notices that are submitted to OCC after the start of critical processing ("late exercise notices"), and (2) amend Rule 801 to change the deadline by which late exercise notices are to be submitted to OCC for exercises on non-expiration dates from 6:30a.m. CT (7:30a.m. ET) to 6:00a.m. CT (7:00a.m. ET).

Background

Rule 801 addresses the exercise of options other than at expiration. Subject to certain conditions, Rule 801(d) grants the Chief Executive Officer, Chief Operating Officer, or any delegate of such officer the discretion to permit a Clearing Member to file

³ OCC's By-Laws and Rules can be found on OCC's public website: <http://optionsclearing.com/about/publications/bylaws.jsp>.

an exercise notice after the prescribed deadline solely for the purpose of correcting a bona fide error on the part of the Clearing Member or a customer.⁴ However, the requesting Clearing Member must pay OCC a \$75,000 fee per line item for a late exercise notice.⁵ Similarly, Rule 805, which addresses exercises on expiration, imposes a \$75,000 fee per line item on a Clearing Member that submits an exercise notice after the prescribed deadline.⁶

Rule 801(d) further provides that the deadline for submitting late exercise notices for exercises other than at expiration is 6:30 a.m. CT, and that OCC will notify Clearing Members with short positions that they have been assigned a late exercise notice by 8:00 a.m. CT.⁷

Discussion

In 2008, OCC raised the late exercise fee from \$20,000 to \$75,000 per line item in Rules 801 and 805 in response to the increased amount of late exercise notices it had

⁴ The current deadline for submitting exercise notices other than at expiration is 6:00 p.m. CT.

⁵ A line item is an exercise instruction which includes the account, series, and quantity to be exercised.

⁶ The current deadline for submitting exercise notices at expiration is 8:00 p.m. CT on monthly standard Friday expirations, 7:00 p.m. CT on weekly Friday expirations, and 6:30 p.m. CT on Monday and Wednesday expirations. Any exercise notice submitted after these expiration deadlines until the “expiration time” of the option, which is currently 10:59 P.M. CT as set forth in Article 1, Section 1(E)(23) of the By-Laws, would be treated as a late exercise notice. Rule 805(d)(2) also provides for the ability to submit a notice to not exercise an in-the-money option (i.e., a contrary exercise). OCC does not allow for the submission of contrary exercise notices after these expiration deadlines.

⁷ As discussed below, OCC is proposing to change the deadline for submitting late exercises under Rule 801(d). OCC is not, however, proposing to make any changes to the deadline for submitting late exercises under Rule 805 (i.e., the expiration time for an option).

received in the prior two years.⁸ As noted in connection with that change, the late exercise fee is intended as an incentive for OCC Clearing Members to be especially diligent in processing exercise notices and to improve back office procedures, while at the same time while preserving their ability to correct bona fide operational errors. OCC believes that the increase achieved its intended purpose at the time of improving Clearing Members' processing proficiency and significantly reduced the amount of late exercise notices.

In 2017, OCC received four late exercise notices.⁹ This amount was significantly more than the four late exercise notices OCC had received in the seven years preceding 2017, and it prompted OCC to review the late exercise fee again. OCC discussed the issue on November 9, 2017 with the OCC Roundtable, which is an OCC-sponsored advisory group comprised of representatives from OCC's participant exchanges, a cross-section of OCC clearing members, and OCC staff. These discussions noted the dollar amount at issue in connection with each of the four late exercises in 2017, which reflected the amount of dividends received by the person submitting the late exercise as a result of receiving the underlying shares. These dividend amounts ranged from \$188,000 to \$375,810.¹⁰ As a result of these discussions, OCC's Roundtable agreed that it was appropriate to increase the late exercise fee to \$250,000 per line item for late exercise

⁸ See Exchange Act Release No. 59046 (December 3, 2008), 73 FR 75486 (December 11, 2008) (SR-OCC-2007-16).

⁹ Until recently, OCC had not received a late exercise notice from a Clearing Member since these ones in 2017. On December 14, 2019, OCC received three late exercise notices from a Clearing Member.

¹⁰ The dividend amounts for the recent December 14, 2019 late exercise notices ranged from \$93,600 to \$436,800.

notices submitted under Rules 801 and 805. Consistent with the purposes of the late exercise fee noted above, the Roundtable believed this amount would be in a range to incent OCC Clearing Members to be especially diligent in processing exercise notices while at the same time still allowing firms to correct bona fide errors.

In connection with the four late exercise notices received in 2017, OCC also reviewed its procedures for processing a late exercise. OCC Rule 801(d) provides that the current deadline for a Clearing Member to formally request a late exercise for an exercise on a non-expiration date is 6:30 a.m. CT and that OCC must notify the assigned Clearing Members by 8:00 a.m. CT of the late exercise. Given the compressed timeframe in which to process a late exercise (i.e., 6:30 a.m. CT to 8:00 a.m. CT) and that they are an exception to the normal processing routine, OCC's procedures for processing a late exercise involve significant resources. They include a review of the positions of the Clearing Member, escalation of the request to senior management, random assignment of the exercise to Clearing Members holding the short position, and a detailed communication to those assigned Clearing Members. The late exercises in 2017 have shown the 6:30 to 8:00 AM CT window is a narrow window for OCC staff to properly process the exercise and assignments without delays, and OCC therefore believes it needs another 30 minutes to process the late exercises. Accordingly, OCC is proposing to change the deadline for the submission of late exercises to 6:00 a.m. CT from the current 6:30 a.m. CT deadline. OCC also discussed this proposal with the OCC Roundtable in connection with discussions noted above and they agreed with it.

(2) Statutory Basis

Section 17A(b)(3)(F) of the Act¹¹ requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities and derivatives transactions. OCC believes that the proposed rule change is consistent with this provision because it would promote the prompt and accurate clearance and settlement of securities transactions by providing an incentive for Clearing Members to improve back office processing with respect to identifying and handling positions for which an exercise notice is to be submitted, while preserving their ability to correct bona fide operational errors. Similarly, providing OCC an additional 30 minutes in which to process a late exercise notice is consistent with this provision because it is designed to help OCC process such notices without delays. As noted, OCC discussed both of these changes with the OCC Roundtable and they agreed with them. The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended.

(B) Clearing Agency's Statement on Burden on Competition

Section 17A(b)(3)(I) of the Act¹² requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the Act. OCC does not believe that the proposed rule change would impact or impose any burden on competition.¹³ The proposed rule change would not affect the competitive dynamics between Clearing Members in that it would apply to all Clearing Members equally. The

¹¹ 15 U.S.C. 78q-1(b)(3)(F).

¹² 15 U.S.C. 78q-1(b)(3)(I).

¹³ 15 U.S.C. 78q-1(b)(3)(I).

proposed rule change also would not inhibit access to OCC's services or disadvantage or favor any particular user in relationship to another. In this regard, as described above, the proposed rule change is designed to further facilitate the prompt and accurate clearance and settlement of securities transactions. It is designed to incent Clearing Members to be especially diligent in processing exercise notices and to improve back office procedures, while at the same time preserving their ability to correct bona fide operational errors

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments on the proposed rule change 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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove the proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

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-2020-001 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2020-001. 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 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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of OCC.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information

from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-OCC-2020-001 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.¹⁴

J. Matthew DeLesDernier
Assistant Secretary

¹⁴ 17 CFR 200.30-3(a)(12).