SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-78834; File No. SR-OCC-2016-802)

September 14, 2016

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Advance Notice Concerning The Options Clearing Corporation's Escrow Deposit Program

Pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, entitled the Payment, Clearing, and Settlement Supervision Act of 2010[1] ("Payment, Clearing and Settlement Supervision Act") and Rule 19b-4(n)(1)(i) under the Securities Exchange Act of 1934,[2] notice is hereby given that on August 15, 2016, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the advance notice as described in Items I, II and III below, which Items have been primarily prepared by OCC. The Commission is publishing this notice to solicit comments on the advance notice from interested persons.

I. Clearing Agency's Statement of the Terms of Substance of the Advance Notice

This advance notice is filed by OCC in connection with changes that would improve the resiliency of OCC's escrow deposit program. Such changes are designed to: (1) increase OCC's visibility into and control over collateral deposits made under the escrow deposit program; (2) strengthen clearing member's rights to collateral in the escrow deposit program in the event of a customer default to the clearing member; (3) provide more specificity concerning the manner in which OCC or clearing members would take possession of collateral in OCC's escrow deposit program; and (4) improve the readability of the rules governing OCC's escrow deposit program by consolidating all such rules into a single location in OCC's Rulebook.

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1 12 U.S.C. 5465(e)(1).

2 17 CFR 240.19b-4(n)(1)(i).

II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Advance Notice

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the advance notice and discussed any comments it received on the advance notice. 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) and (B) below, of the most significant aspects of these statements.

(A) Clearing Agency's Statement on Comments on the Advance Notice Received from Members, Participants or Others

Communications with Custodian Banks

In light of the substantial changes proposed to the escrow deposit program, OCC has sought to keep custodian banks informed regarding the proposed changes. These communications began in January and February 2012, when OCC notified each custodian bank of the proposal to restructure the escrow deposit program. As part of this notification, OCC informed each custodian bank of (1) OCC's intention to require that security pledges be made through the Depository Trust Company ("DTC"), (2) the percentage of cash used in the escrow deposit program and (3) the potential elimination of cash deposits.[3]

[3] While it was ultimately determined in April 2014 that cash collateral would remain in the escrow deposit program, prior discussions with participating escrow banks reflected the evolution of OCC's decision on this point. For example, the PowerPoint presentation given to banks during June – August 2012 indicated that cash collateral would not be permitted in the escrow deposit program, while the PowerPoint presentation given during April – May 2013, as well as the draft rules distributed to participating escrow banks for comment in July – August 2013, indicated that it *would* be included. A number of current participants in the escrow deposit program use cash, some to a substantial degree, and OCC determined that the use of cash collateral should remain an essential aspect of the escrow deposit program.

In June through August 2012, OCC provided a PowerPoint presentation to each custodian bank summarizing proposed changes to the escrow deposit program. This presentation included an explanation of the reasons for the proposed changes, including the desire to enhance and strengthen the escrow deposit program and increase collateral transparency. The presentation also included a discussion of changes to the validation and valuation of collateral, and the calculation of contract quantities based on the collateral that has been pledged.

In April and May 2013, OCC provided each custodian bank with an operational overview of the restructured escrow deposit program in the form of a PowerPoint presentation. This presentation covered: eligible option types, types of eligible supporting collateral, required collateral value calculations for option contact coverage, valuation of supporting collateral, asset management locations/processing of supporting collateral, and validation and valuation of supporting collateral and calculation of option contract coverage.

In July and August 2013, OCC distributed a draft Participating Escrow Bank Agreement (as described below) and the related proposed OCC Rules to custodian banks along with a request for feedback. Following the receipt of questions and comments, OCC distributed "FAQ" responses to custodian banks.

During September 2013, OCC provided a walkthrough of the functions of its ENCORE[4] system applicable to the enhanced escrow deposit program for custodian banks in order to provide an orientation of such functionality. In connection with the restructured escrow deposit program, clearing members will continue to use ENCORE to view member specific deposits, and custodian banks will use ENCORE to view third-party specific deposits and make escrow

[4] ENCORE is OCC's real-time clearing and settlement system that allows clearing members to, among other things, post and view margin collateral as well as deposits in lieu of margin.

deposits consisting of cash. Moreover, OCC sent requests to custodian banks for validation of the DTC pledgor accounts to be used for the restructured escrow deposit program. In October 2013, OCC distributed escrow deposit program eligible securities file details to custodian banks.

In February and March 2014, OCC arranged a series of calls with custodian banks to solicit feedback on a term sheet detailing cash account structures. Following the receipt of questions and comments, OCC distributed "FAQ" responses to custodian banks.

Comments Received from Custodian Banks

As described above, OCC discussed the proposed changes to its escrow deposit program with custodian banks several times since 2012. While these discussions were generally informational in nature, custodian banks provided OCC with comments and questions in two instances: the July/August 2013 discussions and the February/March 2014 discussion. The primary focus of the comments in both sets of discussions was the manner in which custodian banks would be required to hold cash under the new escrow rules: in an omnibus structure or in a tri-party structure. The omnibus structure would provide OCC with an account in OCC's name and thereby perfect OCC's right under the Uniform Commercial Code ("UCC") to take possession of cash escrow deposits in the event of a clearing member default. This would also eliminate the need for a separate tri-party agreement. However, the omnibus structure was less desirable to custodian banks since all of a custodian bank's OCC escrow deposit program clients' assets would be comingled in a single account. From an operational perspective, a single omnibus account at a custodian bank is easier for OCC to manage since OCC would only need to have "view access" into one account at a custodian bank. On the other hand, custodian banks expressed privacy concerns with respect to several clients having view access into a single account. Eventually, OCC decided to use a tri-party account structure for cash escrow deposits,

with certain controls to alleviate the concerns on both sides. Specifically, custodian banks agreed to facilitate the execution of a form tri-party agreement with each of its clients that participates in OCC's escrow deposit program, which perfects OCC's security interest in cash escrow deposits. Additionally, custodian banks agreed to establish an escrow specific cash account for each client so that OCC does not need to differentiate a client's OCC escrow cash from the client's non-escrow cash. OCC believes that the proposed structure for cash accounts strikes the appropriate balance between OCC's desire for legal certainty as to its right to take possession of cash escrow deposits in the event of a clearing member default, and the operational desire to only have view access to a client's OCC escrow deposit program cash account balance at a custodian bank.

Additional comments OCC received from the July/August 2013 discussions with custodian banks centered on administrative items such as the escrow deposit program documentation structure and the manner in which custodian banks would post escrow deposits in OCC's clearing system, ENCORE. As discussed below, OCC moved the substantial majority of its Amended and Restated On-Line Escrow Deposit Agreement into proposed Rule 610C in order to have the majority of escrow rules in one place. Custodian banks did not express any concerns regarding the operational steps necessary to post an escrow deposit in ENCORE once OCC provided custodian banks with a "walkthrough" of the operational process.

(B) Advance Notice Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Description of Change

The purpose of this proposed change is to improve the resiliency of OCC's escrow deposit program. The changes would: (1) increase OCC's visibility into and control over collateral deposits made under the escrow deposit program; (2) provide more specificity

concerning the manner in which OCC would take possession of collateral in OCC's escrow deposit program in the event of a clearing member or custodian bank default; (3) clarify clearing members' rights to collateral in the escrow deposit program in the event of a customer default to the clearing member; and (4) improve the readability of the rules governing OCC's escrow deposit program by consolidating all such rules into a single location in OCC's Rulebook. Upon implementation of the proposed change, all securities collateral in OCC's escrow deposit program would be held at DTC, and custodian banks would only be allowed to hold cash collateral.

The narrative below is comprised of four sections. The first section provides a background of OCC's current escrow deposit program as well as an overview of the proposed changes to the rules and agreements that govern the escrow deposit program. The second section discusses the changes associated with: 1) increasing OCC's visibility into and control over collateral deposits made under the escrow deposit program; 2) providing more specificity concerning the manner in which OCC would take possession of collateral in OCC's escrow deposit program in the event of a clearing member or custodian bank default; and, 3) clarifying clearing member's rights to collateral in the escrow deposit program in the event of a customer default to the clearing member as well as providing additional detail concerning the manner in which clearing members may take possession of such collateral. The third section discusses proposed technical and conforming changes to the rules and agreements governing the current escrow deposit program that would allow OCC to consolidate all such terms into a single location in OCC's Rulebook. The second and third sections also discuss changes that improve the readability of the rules governing OCC's escrow deposit program, which is primarily achieved by consolidating all such rules into a single location in OCC's Rulebook. The fourth

section discusses the manner in which OCC proposes to transition from the current escrow deposit program to the new escrow deposit program, including the removal of certain rules and contractual provisions that would no longer be applicable to the new escrow deposit program.

SECTION 1: BACKGROUND AND OVERVIEW OF PROPOSED CHANGES

Background/Current Escrow Deposit Program

Each day OCC collects collateral from its clearing members in order to protect OCC and the markets it serves from potential losses stemming from a clearing member default. Approximately half of the collateral deposited by clearing members at OCC is deposited through OCC's escrow deposit program. Users of OCC's escrow deposit program are customers of clearing members who, through the escrow deposit program, are permitted to collateralize eligible positions directly with OCC (instead of with the relevant clearing member who would, in turn, deposit margin at OCC). Currently, collateral deposits made through OCC's escrow deposit program are characterized as either "specific deposits" or "escrow deposits." Specific deposits are deposits of the security underlying a given options positions and are made through the DTC by a clearing member on behalf of its customer (at the direction of the customer).[5] Escrow deposits are deposits of cash or securities made by a custodian bank on behalf of a customer of an OCC clearing member in support of an eligible options position. OCC's Rules currently contemplate two forms of escrow deposits: "third-party escrow deposits" and "escrow program deposits." Third-party escrow deposits are substantially similar to specific deposits except for the fact that third-party escrow deposits are made by a custodian bank, and not a clearing member. Third-party escrow deposits consist entirely of securities and, like specific

[5] For example, if customer XYZ holds a short position of options on AAPL, customer XYZ could, through its clearing member's DTC account, pledge shares of AAPL to OCC in order to collateralize such options position and not be charged margin by OCC.

deposits, are made through DTC. In order to effect third-party specific deposits, custodian banks must be DTC members. Escrow program deposits are bank deposits of eligible securities or cash, which are held at the custodian bank (versus third-party escrow deposits and specific deposits, which are held at DTC).

When a customer of a clearing member makes a deposit in lieu of margin through OCC's escrow deposit program, the relevant positions are excluded from the clearing member's margin requirement at OCC. The escrow deposit program therefore provides users of OCC's services with a means to more efficiently use cash or securities they may have available.

Overview of Rule Changes (including terminology changes) and New Agreements

Rule Consolidation and Terminology Changes

Currently, the rules concerning OCC's escrow deposit program are located in OCC Rules 503, 610, 613 and 1801. Additionally, OCC and custodian banks participating in OCC's escrow deposit program enter into an Escrow Deposit Agreement ("EDA"), which also contains substantive provisions governing the program. OCC is proposing to consolidate all of the rules concerning the escrow deposit program, including the provisions of the EDA relevant to the revised escrow deposit program, into proposed Rules 610, 610A, 610B and 610C.[6] OCC believes that consolidating the many rules governing the escrow deposit program into a single location would significantly enhance the understandability and transparency of the rules concerning the escrow deposit program for current users of the program as well as any persons that may be interested in using the program in the future.

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[6] As described herein, OCC is proposing to eliminate the EDA based on such consolidation. When appropriate, and as described in more detail below, conforming changes were made to certain Rules as a result of OCC proposing to require that all non-cash deposits in the escrow deposit program be made through DTC (and not held at custodian banks).

In connection with the above described rule consolidation, OCC is also proposing to rename the types of escrow deposits available within the escrow deposit program, as well as rename the term "approved depository" to "approved custodian." Specific deposits would now be called "member specific deposits," which are equity securities deposited by clearing members at DTC at the direction of their customers; third-party escrow deposits would now be called "third-party specific deposits," which are equity securities deposited by custodian banks at DTC at the direction of their customers; and, escrow program deposits would now be called, "escrow deposits," which are either cash deposits held at a custodian bank for the benefit of OCC, or Government securities deposited at DTC by custodian banks at the direction of their customers. The term "approved depository" would also be changed to "approved custodian" to eliminate any potential confusion with the term "Depository," which is defined in the Rules, to mean DTC.

New Rule Organization

With respect to the rules governing the escrow deposit program, proposed Rule 610 would set forth general terms and conditions common to all types of deposits permitted under the escrow deposit program. Specifically, proposed Rule 610: (1) sets forth the different types of eligible positions for which a deposit in lieu of margin may be used, (2) sets forth operational aspects of the escrow deposit program such as the days and the times during which a deposit in lieu of margin may be made and where the different types of deposits in lieu of margin must be maintained (either DTC or a custodian bank), (3) provides the conditions under which OCC may take possession of a deposit in lieu of margin (from DTC or a custodian bank), and (4) describes OCC's security interest in deposits in lieu of margin.[7] Proposed Rule 610 is supplemented by:

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[7] OCC would continue to maintain a perfected security interest in deposits in the escrow deposit program under the proposed Rules notwithstanding changes to the location of the rules that perfect such security interest. OCC's security interest in securities deposits in

(1) proposed Rule 610A for member specific deposits, (2) proposed Rule 610B for third-party specific deposits, and (3) proposed Rule 610C for escrow deposits. Proposed Rules 610A, 610B and 610C provide further guidance and specificity on the topics initially addressed in proposed Rule 610 (and delineated above) as they relate to member specific deposits, third-party specific deposits and escrow deposits, respectively.

The new rule structure differs from the existing rule structure in that existing Rules 503, 610, 613 and 1801 discuss topics concerning deposits in lieu of margin (such as withdrawal, roll-over[8] and release) in general terms and without regard to the type of deposit in lieu of margin. The existing rule structure also does not provide operational details of the escrow deposit program. The new rule structure discusses each aspect of OCC's escrow deposit program by type of deposit in lieu of margin (member specific deposits, third-party specific deposit or escrow deposits) as well as provides operational details concerning the program. OCC believes that the more detailed presentation of the new rules concerning the escrow deposit program enhances the understandability of the program to all users, and potential users, of the program because all such persons will be able to better understand how topics apply by type of deposit in lieu of margin and with regard to the operational differences between each type of deposit in lieu of margin.

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the escrow deposit program, which are held at DTC, is perfected by operation of DTC's rules. OCC's security interest in cash deposits in the escrow deposit program is perfected under proposed Rules 610C(i), 610C(j) and 610C(k), which replace Sections 3.3, 3.4, 4.3, 4.4, 5.3, 5.4 and 21 of the EDA. Proposed Rule 610(g) also concerns OCC's security interest in deposits in escrow deposit program.

[8] A "roll-over" occurs when a customer chooses to maintain an existing escrow deposit after the options supported by the escrow deposit expires, or are closed-out, and the customer re-allocates the escrow deposit to a new options position.

Agreements Concerning the Escrow Deposit Program

In addition to the above-described Rule changes, many provisions of the EDA would be moved in to the Rules. Accordingly, OCC is proposing to eliminate the EDA and replace it with a simplified agreement entitled the "Participating Escrow Bank Agreement."[9] The Participating Escrow Bank Agreement would provide that custodian banks are subject to all terms of the Rules governing the revised escrow deposit program,[10] as they may be amended from time to time.[11] The Participating Escrow Bank Agreement would contain eligibility requirements for custodian banks, including representations regarding the custodian bank's Tier 1 Capital,[12] and provide OCC with express representations concerning the bank's authority to enter into the Participating

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9 The Participating Escrow Bank Agreement is attached to this filing as Exhibit 5A, with changes from the EDA marked. Custodian banks participating in the revised escrow deposit program are defined as "Participating Escrow Banks" in the Participating Escrow Bank Agreement, and such banks must also be an Approved Custodian pursuant to proposed Section 1.A(13) of OCC's By-Laws. In addition, and as described above, certain provisions of the EDA are proposed to be incorporated into OCC's Rules; however, no rights or obligations of either OCC or a custodian bank would change solely as a result of such an incorporation.

10 The Rules governing the revised escrow deposit program are proposed Rules 610, 610A, 610B and 610C.

11 Under the Participating Escrow Bank Agreement, however, OCC will agree to provide custodian banks with advance notice of material amendments to the Rules relating to deposits in lieu of margin and custodian banks will have the opportunity to withdraw from the escrow deposit program if they object to the amendments. As a general matter, the Participating Escrow Bank Agreement will not be negotiable, although OCC may determine to vary certain non-material terms in limited circumstances.

12 OCC recently enhanced the measurement it uses—Tier 1 Capital instead of shareholders' equity—to establish minimum capital requirements for banks approved to issue letters of credit that may be deposited by clearing members as a form of margin asset. *See* Securities Exchange Act Release No. 74894 (May 7, 2015), 80 FR 27431 (May 13, 2015) (SR-OCC-2015-007). For the reasons set forth in SR-OCC-2015-007, OCC is proposing to adopt the same standard with respect to custodian bank escrow deposits.

Escrow Bank Agreement.[13] Moreover, standard contractual provisions concerning topics such as assignment, governing law and limitation of liability have been enhanced in the Participating Escrow Bank Agreement when compared to the EDA.[14] OCC is also proposing to move notification requirements into proposed Rule 610C(l), which is an enhancement of Section 7 of the EDA that requires custodian banks to provide notice to OCC only when there are changes to the "authorized persons" and changes to the address of the bank. Proposed Rule 610C(l) would require escrow banks to provide OCC with notices of material changes to the bank (in additional to items such as changes of authorized persons and the address of bank, as currently required under Section 7 of the EDA).

OCC, under Proposed Rule 610C(b), would also require customers wishing to deposit cash collateral and custodian banks holding escrow deposits comprised of cash to enter into a tri-party agreement involving OCC, the customer and the applicable custodian bank ("Tri-Party Agreement," attached hereto as Exhibit 5B). The Tri-Party Agreement governs the customer's use of cash in the program, confirms the grant of a security interest in the customer's account to OCC and the relevant clearing member, as set forth in proposed Rule 610C(f), and causes customers of clearing members to be subject to all terms of the Rules governing the revised

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13 These provisions include, but are not limited to, Sections 1.1 and 1.2 of the EDA.

14 Sections 2.1, 2.2, 3.5, 3.6, 3.8, 4.7, and 5.6, 6 and 7 of the EDA would be removed entirely since they are no longer needed under OCC's revised escrow deposit program. These provisions concern a custodian bank's movement of securities escrow collateral; such collateral would be deposited at DTC under the revised escrow deposit program (as described below). Section 2.3 of the EDA would also be removed in its entirety because escrow deposits would not be permitted for equity calls in the revised escrow deposit program. Additionally, the concept of cash settlements concerning escrow deposits would not be included in the revised escrow deposit program and, as a result, Sections 15, 16, 17 and 18(b) to 18(d) would be removed in their entirety.

escrow deposit program.[15] Each custodian bank entering into the Tri-Party Agreement ("Tri-Party Custodian Bank"), would agree to follow the directions of OCC with respect to cash escrow deposits without further consent by the customer.[16] As discussed in greater detail below, use of the Tri-Party Agreement significantly enhances OCC's rights concerning cash escrow deposits, and provides OCC with greater certainty regarding its rights to cash escrow deposits in the event of a customer or clearing member default.

SECTION 2: TRANSPARENCY AND CONTROLS, TAKING POSSESSION OF COLLATERAL, AND CLEARING MEMBER RIGHTS TO COLLATERAL

Transparency and Control over Collateral Included in Escrow Deposits

Currently, securities deposits in the escrow deposit program are held at either DTC or a custodian bank, and cash deposits in the escrow deposit program are held at a custodian bank. In the case of either cash or securities held at a custodian bank, OCC relies on the custodian bank to verify the value and control of collateral since OCC does not have any visibility into relevant accounts. OCC is proposing to require that all securities deposited within the escrow deposit program, regardless of the type of deposit, be held at DTC.[17] Additionally, OCC is proposing to

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15 The Rules governing the revised escrow deposit program are proposed Rules 610, 610A, 610B and 610C.

16 OCC has determined to use this cash account structure as a result of a series of discussions with certain custodian banks involved in the cash portion of the escrow deposit program, as described in Item 5 above. The intended structure would permit a greater number of customers to participate in the escrow deposit program than, for example, a commingled "omnibus" account structure at each custodian bank, which would preclude the participation of customers subject to restrictions under the Investment Company Act of 1940 requiring segregation of a registered investment company's funds.

17 OCC has discussed the proposed changes to the escrow deposit program with DTC and, based on feedback from DTC, no concerns were communicated to OCC by DTC regarding the proposed changes. DTC has also indicated that the proposed changes to the escrow deposit program are consistent with DTC's operations.

require Tri-Party Custodian Bank to provide OCC with view access into the account in which the deposit is held.

Holding securities escrow deposit program collateral at DTC would provide OCC with increased visibility into the collateral within the escrow deposit program because OCC would be able to use its existing interfaces with DTC to view, validate and value collateral within the escrow deposit program in real time, allowing OCC to perform the controls for which it currently relies on the custodian banks. It would also provide OCC with the ability to obtain possession of deposited securities upon a clearing member default by issuing a demand of collateral instruction through DTC's systems, without the need for custodian bank involvement. Furthermore, a clearing member would have the ability to obtain possession of deposited securities upon a customer default in a similar manner by notifying OCC of such customer default and submitting a request for delivery of such deposited securities (OCC's and clearing members' ability to take possession of a deposit within the escrow deposit program is discussed in greater detail below). OCC does not believe that requiring use of DTC to deposit securities escrow collateral presents a material change for users of OCC's escrow deposit program because such users currently use DTC to effect certain types of deposits in lieu of margin under the current escrow deposit program.[18]

Cash collateral pledged to support an escrow deposit would continue to be facilitated through the existing program interfaces; however, for increased security, any pledges of cash would be required to be made in a customer's account at the Tri-Party Custodian Bank that is

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[18] Specifically, users of OCC's escrow deposit program would use DTC's Collateral Loan Services, which is described at: http://www.dtcc.com/products/training/helpfiles/settlement/settlement_help/help/collateral_loans.htm.

used solely for the purpose of making escrow deposits. As described above, under the proposed changes OCC would require Tri-Party Custodian Bank and customers to enter into a Tri-Party Agreement in order to provide legal certainty concerning this arrangement. Further, and as set forth in the Tri-Party Agreement, each Tri-Party Custodian Bank would agree to disburse funds from the pledged account only at OCC's direction. From an operational perspective, each Tri-Party Custodian Bank would provide OCC with online view access to each customer's cash account designated for the escrow deposit program, allowing visibility into transactional activity and account balances. OCC would not process a cash escrow deposit in its systems until it sees the appropriate amount of cash deposited in the designated bank account at the Tri-Party Custodian Bank. This process ensures that OCC does not rely on a third party to value, or warrant the existence of, collateral within the escrow deposit program. The Tri-Party Agreement, in connection with the new cash collateral structure, would provide OCC with additional transparency and control over cash collateral under the revised escrow deposit program.

In order to effect the foregoing, OCC is proposing to adopt proposed Rules 610A(a), 610B(a), 610C(b) and 610C(c). Proposed Rules 610A(a) and 610B(a), Effecting a Member Specific Deposit and Effecting a Third-Party Specific Deposit, respectively, require that member specific deposits and third-party specific deposits must be made through DTC, and are largely based upon existing Rule 610(e), which discusses effecting deposits in lieu or margin generally. Language has been added to each proposed rule to more accurately articulate that member specific deposits and third-party specific deposits must be made through DTC and the party that is required to effect each type of deposit (i.e., a clearing member or a third-party depository). In the case of member specific deposits and third-party specific deposits, which are already made

through DTC, OCC believes that proposed Rules 610A(a) and Rule 610B(a) are rules that clarify existing practices and provide additional operational detail to users of the escrow deposit program (i.e., member specific deposits and third-party specific deposits must be made through DTC's Electronic Data Processing ("EDP") Pledge System and clearing members are required to maintain records of such deposits). Proposed Rules 610C(b) and 610C(c), Manner of Holding and Method of Effecting Escrow Deposits, respectively, are largely based upon existing Rules 610(d), 610(g), 1801(d) and 1801(g), as well as Section 8 of the EDA with language added to more accurately articulate that securities escrow deposits must be made through DTC and cash must be deposited through a Tri-Party Custodian Bank, and provide operational detail concerning effecting escrow deposits. Moreover, OCC is proposing to adopt new Rule 610(e) in order to specify that all types of deposits in the escrow deposit program may be made only during the time specified by OCC. The purpose of specifying the time frames in which participants are allowed to effect deposits in the escrow deposit program is to facilitate OCC daily margin processing and ensure that all of the positions it guarantees are timely collateralized.[19]

In addition to the above, and with respect to escrow deposits only, OCC is proposing enhancements to its process of ensuring that customers meet initial and maintenance minimums.[20] Specifically, under the revised escrow deposit program, in the event a customer falls below the maintenance minimum, the custodian bank, pursuant to the Participating Escrow Bank Agreement, would be required to ensure that the customer deposits additional collateral or

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19 In the event a deposit in the escrow deposit program is not timely made, OCC would collect margin from the relevant clearing member.

20 Initial and maintenance minimums do not apply to member specific deposits and third-party specific deposits since the clearing member or custodian bank, as applicable, is pledging the security that is deliverable upon exercise of the germane options position.

escalate the matter to OCC. In addition to such notification requirement, OCC would also implement automated processes to ensure that escrow deposits meet required initial and maintenance minimums. In the event the matter is escalated to OCC or OCC's systems identify a shortfall, OCC would: (1) demand that the relevant clearing member post additional margin to cover the margin requirement on the applicable position, and (2) if the relevant clearing member fails to satisfy such a demand for additional margin, OCC would close-out the applicable position and demand the escrow deposit from DTC or the Tri-Party Custodian Bank, as applicable, under its existing authority pursuant to Rule 1106. This process is much more robust than the current process concerning maintenance minimums in that OCC currently relies entirely on custodian banks holding escrow deposits to ensure the customer deposits additional collateral, as necessary, to meet initial and maintenance minimums. OCC believes that the proposed new process is more streamlined and efficient because OCC would not have to rely entirely on a custodian bank to ensure customers comply with initial and maintenance minimums.

In order to implement the foregoing within the new rules concerning the escrow deposit program, OCC is proposing to adopt Rules 610C(g) and 610C(h) that concern the initial and maintenance minimum escrow deposit values required by OCC as well as actions OCC's[sic] is permitted to take in the event an escrow deposit falls below a required amount. These proposed rules are based on existing Rules 1801(c) and 1801(e) as well as Sections 3.2, 4.2, 5.2, 3.7, 4.8 and 5.7 of the EDA.[21] With respect to the computation of initial and maintenance minimums, proposed Rules 610C(g) and 610C(h) would explain the formula through which OCC computes the initial and maintenance minimum for a given options position, with the specific percentage

[21] OCC is proposing to eliminate the concept of "substitutions" of escrow deposit collateral (located in Sections 4.7 and 5.6 of the EDA)—instead a given escrow deposit must at all times must meet the minimum amount (as set forth in proposed Rules 610(g)(1) and (2)) and OCC would permit any excess amount to be withdrawn.

applicable to such calculation provided to participants in the escrow deposit program in a schedule posted on OCC's website. With respect to the effects of a failure to meet maintenance minimums, proposed Rule 610C(h) sets forth the conditions under which OCC would close out a given escrow deposit should it fall below the requisite maintenance minimum. Proposed Rule 610C(h) would also provide OCC with the authority to use the cash and securities included within the escrow deposit to reimburse itself for costs incurred in connection with the close-out. OCC believes that by virtue of their proposed new location in the rules, as well as the additional detail provided in the proposed rules, all participants, and potential participants, in OCC's escrow deposit program would better understand the rules concerning initial and maintenance minimums, as they relate to escrow deposits, under the enhanced escrow deposit program (versus under the current escrow deposit program).

OCC's Rights to Collateral in the Escrow Deposit Program in the Event of a Clearing Member or Bank Default

The proposed Rules would enhance OCC's default management regime as it relates to the escrow deposit program by more specifically delineating the conditions under, and the process through which, OCC would take possession of collateral within the escrow deposit program should a clearing member or custodian bank default. Specifically, proposed Rules 610A(b), 610B(f), 610C(q) and 610C(r) provide that in the event of a clearing member or custodian bank default OCC would have the right to direct DTC to deliver the securities included in a member specific deposit, third-party specific deposit or escrow deposit to OCC's DTC participant account for the purpose of satisfying the obligations of the clearing member or reimbursing itself for losses incurred as a result of the failure, as applicable. Similarly, pursuant to proposed Rules 610C(q) and 610C(r) OCC would have the right in the event of a Tri-Party Custodian Bank default to take possession of cash included within an escrow deposit for the same purposes. In

the event of a custodian bank default, pursuant to proposed Rule 610C(r) OCC would have the right to remove the custodian bank from the escrow deposit program, prohibit the custodian bank from making new escrow deposits, disallow withdrawals with respect to existing deposits, close out short positions covered by escrow deposits at the defaulted custodian bank and use such escrow deposits to reimburse itself for the costs of the close-out, or disregard or require the withdrawal of existing escrow deposits.

Proposed Rules 610A(b), 610B(f) and 610C(q), concern OCC's rights to a member specific deposits, third-party specific deposits and escrow deposits, respectively, in the event of a clearing member default. They would provide a more specific description of OCC's rights to a third-party specific deposit during a default than existing Rule 610(k) and Section 18 of the EDA. However, the additional specificity that would be provided in proposed Rules 610A(b), 610B(f) and 610C(q) would not change OCC's nor clearing members' rights or obligations regarding member specific, third-party specific or escrow deposits in the event of a clearing member default. Proposed Rule 610C(r) addresses OCC's rights in the event of a custodian bank default and is based on existing Rules 613(h) and 1801(k). Proposed Rule 610C(r) would clarify OCC's existing operational practices when a custodian bank defaults (i.e., demand monies, not allow new deposits, etc…, as described immediately above), but does not change any of the rights of OCC, clearing members or custodian banks as they are set forth in existing Rules 613(h) and 1801(k).

In addition to the above described proposed changes, OCC is proposing to amend Rule 1106 to set forth the treatment of deposits in the escrow deposit program in the event of a suspension of a clearing member. Rule 1106(b)(2) would be amended to provide that OCC may close out a short position of a suspended clearing member covered by a member specific, third-

party specific or escrow deposit, subject to the ability of the suspended clearing member or its representative to transfer the short position to another clearing member under certain circumstances. Further, current Rule 1106(b)(3) would be combined with Rule 1106(b)(2) and amended to set forth OCC's right to take possession of the cash and/or securities included within an escrow, member specific, or third-party specific deposit for the purpose of reimbursing itself for costs incurred in connection with the close-out of a short position covered by the deposit. These proposed amendments to Rule 1106 are consistent with proposed Rules 610B(f), 610C(q) and 610C(r).

Clearing Members' Rights to Collateral in the Escrow Deposit Program

Clearing members' rights to escrow deposits and third-party specific deposits would be clarified under the proposed rules. While clearing members have secondary lien rights on the escrow deposits of their customers under the current escrow deposit program, OCC is proposing to add several rules that would clarify these rights and provide additional guidance to clearing members regarding operational steps that would need to be taken in order to exercise their secondary lien rights. Specifically, OCC is proposing to add Rules 610B(c) and 610C(f) to delineate the rights of a clearing member as they relate to third-party specific deposits and escrow deposits. Proposed Rules 610B(c) and 610C(f) would provide for the grant of a security interest by the customer to the clearing member with respect to any given third-party specific deposit and escrow deposit, as applicable. The Rules would further provide that any such security interest of a clearing member in an escrow deposit would be subordinated to OCC's interest. For purposes of perfecting a clearing member's security interest under the UCC, OCC would obtain control over the security both on its own behalf and on behalf of the relevant clearing member, with clear subordination of the clearing member's interest to OCC's interest.

In the event OCC had to direct delivery of the security to the clearing member, OCC would do so on the clearing member's behalf. Proposed Rules 610B(c) and 610C(f) would better codify clearing members' secondary lien rights to third-party specific deposits and escrow deposit[sic] than they are currently codified in Section 21 of the EDA, without changing any clearing member rights or obligations. OCC believes that such a codification would provide more transparency regarding clearing member's secondary lien rights under the enhanced escrow deposit program because all users, and potential users, of OCC's escrow deposit program would be able to easily identify and understand the rules concerning clearing members' secondary lien rights in a single location within OCC's publically available Rulebook.

Additionally, OCC is proposing to add several procedural rules that would set forth the process by which clearing members could exercise their secondary lien rights in a given deposit in the escrow deposit program. Proposed Rules 610C(d), 610C(o), 610C(p) and 610C(s), relating to escrow deposits, and proposed Rules 610B(d) and 610B(e), relating to third-party specific deposits, would provide that, in the event of a customer default to a clearing member, the clearing member would have the right to request a "hold" on a deposit. The hold would prevent the withdrawal of deposited securities or cash by a custodian bank or the release of a deposit that would otherwise occur in the ordinary course. Subsequent to placing a hold instruction on a deposit, a clearing member would have the right to request that OCC direct delivery of the deposit to the clearing member through DTC's systems, in the case of securities, or an instruction to the Tri-Party Custodian Bank in the case of cash. Providing clearing members with transparent instructions regarding how to place a hold instruction on and direct delivery of a deposit in the escrow deposit program would significant enhancement to the current escrow deposit program.

OCC is also proposing to adopt Rules 610B(e) and 610C(s), which would protect OCC in the event that it delivers a third-party specific deposit or escrow deposit to a clearing member. Under proposed Rules 610B(e) and 610C(s) a clearing member making a request for delivery would be deemed to have made the appropriate representations to OCC that the clearing member has a right to take possession of the deposited securities or cash and would agree to indemnify OCC against losses resulting from a breach of these representations or the delivery of the deposit. A clearing member would also be required to provide documentation regarding its right to possession of the securities or cash as OCC may reasonably request.

SECTION 3: TECHINCAL AND CONFORMING CHANGES TO OCC'S RULES

OCC also proposes a number of technical, conforming and structural changes in order to move the majority of the terms governing the escrow deposit program into one section in its Rulebook. OCC believes that changes to proposed Rules 610, 610A, 610B and 610C, described in greater detail below, are either non-substantive or conforming changes that do not alter the current rights or obligations of OCC, clearing members or participants in the escrow deposit program.

Proposed Rule 610-Deposits in Lieu of Margin (General Provisions)

Proposed Rule 610 contains general provisions applicable to the escrow deposit program. Specifically, proposed Rule 610(a) replaces existing Rule 610(a) and sets forth general provisions of the escrow deposit program including: (1) who may participate in the escrow deposit program, (2) the types of positions included in the escrow deposit program, (3) the types of deposits in the escrow deposit program, and (4) the collateral that is eligible for the escrow deposit program. Proposed Rule 610(b) replaces existing Rule 610(b) and provides further specificity with respect to the types of options positions included within OCC's escrow deposit

program.[22] This additional specificity clarifies OCC's existing rules and provides more transparency to users and potential users of OCC's escrow deposit program. Proposed Rule 610(c), which is not derived from an existing rule, clarifies OCC's existing practice that OCC will disregard a member specific deposit or a third-party specific deposit if such deposit is no longer eligible to be delivered upon the exercise of the associated stock option contract. Proposed Rule 610(d), which replaces existing Rules 610(c) and 1801(l), requires that deposits within the escrow deposit program be made in accordance with applicable laws and regulations, and be appropriately authorized. Proposed Rule 610(f), which replaces existing Rule 610(l), would clarify OCC's right to use deposits within the escrow deposit program until such deposits are withdrawn. Proposed Rule 610(f) is supplemented by proposed Rules 610A, 610B and 610C with respect to member specific, third-party specific and escrow deposits. Proposed Rule 610(g) codifies OCC's security interest in deposits within the escrow deposit program.

Proposed Rule 610A-Member Specific Deposits

Proposed Rule 610A clarifies many of the current rules concerning the escrow deposit program as they relate to member specific deposits. For example, proposed 610A(c) describes the process by which a clearing member may withdraw a member specific deposit (i.e., effecting a withdrawal or release through DTC's EDP Pledge System and ensuring that its margin requirement at OCC is met). While this issue is addressed in existing Rule 610(j) in general terms, OCC believes that the additional operational details regarding its existing process in proposed Rule 610A(c), along with its inclusion in proposed Rule 610A, further clarify how those existing processes apply to member specific deposits as opposed to other types of deposits

[22] As described in greater detail below, proposed Rules 610(a) and 610(b) are supplemented by proposed Rules 610A, 610B and 610C.

in lieu of margin in existing Rule 610.[23] Proposed Rule 610A(d) also establishes that member specific deposits may be "rolled-over," a concept that is not specifically set forth in existing Rule 610 but has historically applied in connection with member specific deposits (formerly specific deposits).

Proposed Rule 610B-Third-Party Specific Deposits

Proposed Rule 610B clarifies many of the current rules concerning third-party specific deposits. For example, proposed 610B(b), which addresses rollovers of a third-party specific deposit and replaces existing Rules 613(a) and Section 9 of the EDA, and articulates how to rollover third-party specific deposits by its inclusion within Rule 610B. Withdrawals and releases of third-party specific deposits are addressed in proposed Rule 610B(d), which is based on existing Rules 613(b) and 613(f). Specifically, releases and withdrawals of third-party specific deposits would be effected through DTC's EDP Pledge System, subject to the clearing member's margin requirement being met, the clearing member's approval of the release or withdrawal, and the absence of a "hold" instruction. In addition, proposed Rule 610B(g) seeks to provide a more detailed description of the effect of a release of a third-party specific deposit than existing Rule 613(i).

Proposed Rule 610C-Escrow Deposits

Proposed Rule 610C, which is based on existing Rule 1801(a), would clarify the current rules concerning escrow deposits. For example, the introductory paragraph of proposed Rule 610C would provide a more detailed overview of a custodian bank's role in the escrow deposit program, specifying such a bank's role in effecting escrow deposits, and would describe eligible positions as they relate to escrow deposits. Proposed Rules 610C(a) through 610C(e) and

[23] Proposed Rule 610A(c) supplements to proposed Rule 610(f).

proposed Rule 610C(t) concern eligible collateral, the manner in which escrow deposits are to be held, and withdrawing an escrow deposit and rolling over an escrow deposit. These operational rules are based on: (1) existing Rules 610(g) and 1801(b) and Sections 3.1, 4.1 and 5.1 of the EDA with respect to eligible collateral (proposed Rule 610C(a)); (2) existing Rules 610(j) and 1801(i), and Sections 10 and 20 of the EDA with respect to withdrawing an escrow deposit (proposed Rule 610C(d)); (3) existing Rule 613(i) with respect to the effect of a release or withdrawal of an escrow deposit (proposed Rule 610C(t)); and (4) existing Rule 613(a) and Section 9 of the EDA, with respect to rollovers of an escrow deposit (Proposed Rule 610C(e)).

In order to provide additional transparency concerning representations that custodian banks are deemed to make when effecting an escrow deposit, OCC is proposing to move several contractual provisions of the EDA into proposed Rules 610C(i), 610C(j), and 610C(k). Specifically: (1) proposed Rule 610C(i), which concerns agreements and representations an escrow bank is deemed to have made when effecting an escrow deposit, is based upon Sections 1.6 and 4.6 of the EDA; (2) proposed Rule 610C(j), which concerns representations and warranties a custodian bank is deemed to make when giving an instruction to OCC and is based upon Sections 1.3, 1.4, 1.5, 1.6, 1.7 and 1.8 of the EDA; and (3) proposed Rule 610C(k), which concerns agreements a custodian bank is deemed to make when giving an instruction to OCC and is based upon Sections 4, 5 and 21 of the EDA. Moreover, and in addition to locating deemed representations of custodian banks in the Rules, proposed Rules 610C(i), 610C(j) and 610C(k) contain language that perfects OCC's security interest in escrow deposits under Section 9 of the UCC, and replace Sections 3.3, 3.4, 4.3, 4.4, 5.3 and 5.4 of the EDA.[24] OCC believes

[24] The primary UCC-related provisions in the proposed Rules include Rules 610C(j)(1), 610C(j)(9) and 610C(k)(1), which provide for the perfection of OCC's security interest in deposits consisting of securities under UCC Sections 9-106 and 9-314; Rules 610C(j)(1),

that by locating the above described provisions in the Rules, all users and potential users of OCC's escrow deposit program would better understand the relationship between OCC and custodian banks.

Proposed Rules 610C(m), 610C(n), 610C(o) and 610C(p) concern the exercise of options positions collateralized by escrow deposits and the release of escrow deposits upon expiration. As with other parts of proposed Rule 610C, OCC believes that the location of proposed Rules 610C(m), 610C(n), 610C(o) and 610C(p) provides all users and potential users of OCC's escrow deposit program with a more transparent understanding of how exercises of options positions affect escrow deposits as well as the manner in which OCC would release an escrow deposit upon the expiration of an options position. Similar to other parts of Rule 610C, proposed Rules 610C(m), 610C(n), 610C(o) and 610C(p) are based on existing Rules of OCC as well as the EDA.[25] Proposed Rule 610C(m) concerns reports OCC provides regarding escrow deposits and is based upon existing Rules 613(d) and 613(e) as well as Sections 11, 12 and 13 of the EDA. Proposed Rules 610C(n), 610C(o) and 610C(p), which concern assignments of exercises and releases of escrow deposits upon expiration is based upon existing Rules 613(f) and 1801(j) and Section 14 of the EDA.

SECTION 4: TRANSITION PERIOD

For the administrative convenience of clearing members, custodian banks and customers, the existing Rules governing deposits in lieu of margin would remain in effect, in parallel with

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610C(j)(10), and 610C(k)(2), which provide for the perfection of OCC's security interest in deposits consisting of cash under UCC Sections 9-104, 9-312 and 9-314; and Rules 610C(i)(1), 610C(i)(2) and 610C(j)(3), which support the first priority of OCC's security interest by preventing competing liens or claims.

[25] As discussed in Section 3 above, Rules 610C(n) and 610C(p) contain language that prevents the release of an escrow deposit in the event such deposit is subject to a hold instruction, which is a proposed enhancement to the escrow deposit program.

the proposed Rules, for a transition ending November 30, 2017. During this transition period, deposits in lieu of margin could be made under either the existing Rules or the proposed Rules. This will eliminate the need of all clearing members to provide new collateral on a single date in the absence of a transition period. After the transition period, proposed Rules 610, 610A, 610B and 610C would provide the sole means of making deposits in lieu of margin and existing Rules 613 and 1801 would be removed from the Rulebook. In connection with the transition, existing Rule 610 would be re-designated as 610T to indicate that it is a temporary rule, and would become ineffective and removed after the transition period. Furthermore, following the transition period, existing Rule 503, which addresses instructions that call for the payment of a premium by or to the clearing member for whose account the deposit is made, would be removed from the Rules because these instructions would no longer be permitted under the revised escrow deposit program since this aspect of the program has not been used for a number of years.[26] In addition, Government securities would be given full market value under the revised escrow deposit program and therefore existing Rule 610(h) would be removed from the Rules after the transition period.

Consistency with the Payment, Clearing and Settlement Supervision Act

OCC believes that the proposed change concerning deposits in lieu of margin described above is consistent with Section 805(b)(1) of the Payment, Clearing and Settlement Supervision Act[27] because the proposed change would promote robust risk management. OCC collects

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[26] For the purposes of clarity, existing Rules 613(c), 613(g), 613(h), 613(j) address the same topic and would be removed from OCC's Rulebook following the transition period without being migrated into a proposed Rule.

[27] 12 U.S.C. 5464(b)(1).

margin, or deposits in lieu of margin, in order to protect OCC and market participants from risks resulting from default of a clearing member. As described above, this proposed change would enhance OCC's control over and visibility into deposits in lieu of margin. By increasing OCC's transparency and control over deposits in lieu of margin the change would enable OCC to better ensure that it maintains adequate financial resources in the event of a default of a clearing member and thereby promote robust risk management.

The proposed change also provides clarity to clearing members, their customers and potential users of OCC's escrow deposit program regarding the manner in which OCC would risk manage a clearing member default or the default of a customer of a clearing member using the escrow deposit program. By implementing changes that better describe OCC's risk management regime as it relates to use of the deposits of a clearing member, or customer of a clearing member, within the escrow deposit program, OCC would provide all users, or potential users, of its services with additional certainty and predictability concerning actions OCC would take in the event of a clearing member default that would, in turn, promote robust risk management by making it less likely that such a default would have a have a substantive impact on the ongoing operations of OCC or on the markets OCC serves.

Anticipated Effect on and Management of Risk

OCC believes that the proposed change would reduce the nature and level of risk presented to OCC because OCC would enhance its control over and visibility into deposits in lieu of margin that are made to OCC and thereby enhance OCC's default management practices. As described above, OCC collects margin, or deposits in lieu of margin, in order to protect OCC and market participants from risks associated with the default of a clearing member and such deposits can be in cash or non-cash. The proposal would ensure that all non-cash deposits in lieu

of margin would be pledged to OCC through DTC, which would enable OCC to (1) better validate its control over such deposits and (2) ensure that it is properly valuing such deposits in real-time. In addition, OCC would have greater visibility into deposits in lieu of margin consisting of cash, and Tri-Party Custodian Banks would contractually agree to only release such deposits in lieu of margin upon the approval of OCC. These processes would ensure that OCC could verify that deposits in lieu of margin sufficiently collateralize germane short options position(s) and OCC would be able to use its existing functionality with DTC to more quickly take possession of such deposits in the event of a clearing member default that would, in turn, protect OCC and market participants from risks associated with a clearing member default. Accordingly, OCC believes the proposed change would reduce the nature or level of risk presented to OCC.

III. Date of Effectiveness of the Advance Notice and Timing for Commission Action

The proposed change may be implemented if the Commission does not object to the proposed change within 60 days of the later of (i) the date the proposed change was filed with the Commission or (ii) the date any additional information requested by the Commission is received. OCC shall not implement the proposed change if the Commission has any objection to the proposed change.

The Commission may extend the period for review by an additional 60 days if the proposed change raises novel or complex issues, subject to the Commission or the Board of Governors of the Federal Reserve System providing the clearing agency with prompt written notice of the extension. A proposed change may be implemented in less than 60 days from the date the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the

proposed change and authorizes the clearing agency to implement the proposed change on an earlier date, subject to any conditions imposed by the Commission.

OCC shall post notice on its website of proposed changes that are implemented.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the advance notice 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-2016-802 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-2016-802. 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 advance notice that are filed with the Commission, and all written communications relating to the advance notice 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, N.E., Washington, DC

20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_16_802.pdf. 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-2016-802 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

By the Commission.

Robert W. Errett
Deputy Secretary