SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-82309; File No. SR-OCC-2017-017)

December 13, 2017

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving Proposed Rule Change Concerning Liquidity for Same Day Settlement

On October 13, 2017, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-OCC-2017-007 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder.[2] The proposed rule change was published for comment in the Federal Register on November 1, 2017.[3] The Commission did not receive any comments on the proposed rule change. This order approves the proposed rule change.

I. Description of the Proposed Rule Change

A. Background

OCC filed the proposed rule change to modify the tools available to OCC to provide a mechanism for addressing the risks of liquidity shortfalls, specifically, in the extraordinary situation where OCC faces a liquidity need to meet its same-day settlement obligations resulting from the failure of a bank or securities or commodities clearing organization ("Settlement Entity") to achieve daily settlement. As stated in the Notice,

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 Securities Exchange Act Release No. 34-81956 (Oct. 26, 2017), 82 FR 50705 (Nov. 1, 2017) (SR-OCC-2017-017) ("Notice"). OCC also filed an Advance Notice with the Commission in connection with the proposed change. See Securities Exchange Act Release No. 82056 (Nov. 13, 2017), 82 FR 54430 (Nov. 17, 2017) (SR-OCC-2017-806).

OCC's By-Laws currently grant OCC the authority to borrow against its Clearing Fund where a Settlement Entity fails to make timely settlement with OCC due to bankruptcy, insolvency, resolution, suspension of operations, or a similar event of such Settlement Entity.[4] The proposed rule change seeks to expand this borrowing authority to circumstances that include a temporary failure of a Settlement Entity to achieve daily settlement.

Article VIII, Section 5(e) of OCC's By-Laws provides OCC with the authority to borrow against the Clearing Fund in two circumstances. First, the By-Laws provide OCC the authority to borrow where OCC "deems it necessary or advisable to borrow or otherwise obtain funds from third parties in order to meet obligations arising out of the default or suspension of a Clearing Member or any action taken by the Corporation in connection therewith pursuant to Chapter XI of the Rules or otherwise." Second, the By-Laws provide OCC the authority to borrow against the Clearing Fund where OCC "sustains a loss reimbursable out of the Clearing Fund pursuant to [Article VIII, Section 5(b) of OCC's By-Laws] but [OCC] elects to borrow or otherwise obtain funds from third parties in lieu of immediately charging such loss to the Clearing Fund." In order for a loss to be reimbursable out of the Clearing Fund under Article VIII, Section 5(b) of OCC's By-Laws, the loss must arise from a situation in which any Settlement Entity has failed "to perform any obligation to [OCC] when due because of its bankruptcy, insolvency, receivership, suspension of operations, or because of any similar event."[5]

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4 OCC By-Laws, Article VIII, Section 5.

5 To the extent that a loss resulting from any of the events referred to in Article VIII, Section 5(b) is recoverable out of the Clearing Fund pursuant to Article VIII, Section 5(a), the provisions of Article VIII, Section 5(a) control and render the provisions of Article VIII, Section 5(b) inapplicable.

Under either of the circumstances above, OCC is authorized to borrow against the Clearing Fund for a period not to exceed 30 days, and during this time, the borrowing would not affect the amount or timing of any charges otherwise required to be made against the Clearing Fund pursuant to Article VIII, Section 5 of the By-Laws. However, if any part of the borrowing remains outstanding after 30 days, then at the close of business on the 30th day (or the first Business Day thereafter) the amount must be considered an actual loss to the Clearing Fund, and OCC must immediately allocate such loss among its Clearing Members in accordance with Article VIII, Section 5.

B. The Proposed Rule Change to OCC's By-Laws

The proposed rule change seeks to expand OCC's authority to borrow against its Clearing Fund to instances where a Settlement Entity suffers an event relatively less extreme than bankruptcy, insolvency, or a similar event, but is still temporarily unable to timely make daily settlement with OCC. Such an event might include a scenario where the ordinary operations of a settlement bank are disrupted in a manner that temporarily prohibits the bank from timely effecting settlement payments in accordance with OCC's daily settlement cycle. OCC believes that such authority would only be used in extraordinary circumstances, and any funds obtained from any such transaction could only be used for the stated purpose of satisfying a need for liquidity for same-day settlement.

Pursuant to the proposed change, any ability to borrow under this expanded authority would not exceed thirty (30) days. During this period, the funds obtained would not be deemed to be charges against the Clearing Fund and would not affect the amount or timing of any charges otherwise required to be made against the clearing fund under Article VIII of OCC's By-Laws.[6] Should the borrowing unexpectedly remain outstanding after thirty (30) days, at the close of business on the 30th day (or the first Business Day thereafter), the amount outstanding would be considered an actual loss to the Clearing Fund. However, OCC would also have discretionary authority to declare a borrowing outstanding for less than thirty (30) days as an actual loss chargeable against the Clearing Fund to be collected from Clearing Members.[7] If the amount outstanding becomes an actual loss to the Clearing Fund, OCC, in accordance with its By-Laws, would then charge all of its Clearing Members to make pro rata contributions to the Clearing Fund to cover the deficit arising from the loss.

To implement the proposed change, OCC proposed to amend Sections 1(a), 5(b) and 5(e) of Article VIII of its By-Laws to give effect to the expanded borrowing authority. First, Article VIII, Section 5(e) of the By-Laws would be amended to permit OCC to borrow against the Clearing Fund if it reasonably believes such borrowing is necessary to meet its liquidity needs for same-day settlement as a result of the failure of

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6 Assets contained in the Clearing Fund, including those assets pledged by OCC pursuant to its authority under this proposed expansion of borrowing authority, would remain in OCC's possession.

7 OCC states that such discretionary authority could be exercised in a circumstance where, depending on the size of the borrowing, OCC must ensure that it maintains financial resources necessary to meet a "Cover 1" liquidity resource standard. OCC must establish, implement, maintain and enforce written policies and procedures reasonably designed to, as applicable, effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by maintaining sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence, and, to the extent not already maintained pursuant to the foregoing, maintaining additional financial resources at the minimum to enable it to cover a wide range of foreseeable stress scenarios that include, but are not limited to, the "default of the participant family that would potentially cause the largest aggregate credit exposure for the covered clearing agency in extreme but plausible market conditions." 17 CFR 240.17Ad-22(e)(4)(iii).

any Settlement Entity to achieve daily settlement. Second, Article VIII, Section 1(a) of the By-Laws would be amended to include conforming changes stating that the purpose of the Clearing Fund includes borrowing against the Clearing Fund as permitted under Article VIII, Section 5(e).

Next, Article VIII, Section 5(b) of the By-Laws would be amended to include conforming changes that would declare that any borrowing remaining outstanding for less than 30 days may be considered, in OCC's discretion, an actual loss to the Clearing Fund to be charged proportionately against all Clearing Members' computed contributions. Further, any borrowing remaining outstanding on the 30th day shall be considered an actual loss to the Clearing Fund and the amount of any such loss shall be charged proportionately against all Clearing Members' computed contributions to the Clearing Fund as fixed at the time.

II. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act[8] directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. The Commission finds that the proposal is consistent with Section 17A(b)(3)(F) of the Act[9] and Rule 17Ad-22(e)(7)(viii)[10] thereunder, as described in detail below.

A. Consistency with Section 17A(b)(3)(F) of the Act

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8 15 U.S.C. 78s(b)(2)(C).

9 15 U.S.C. 78q-1(b)(3)(F).

10 17 CFR 240.17Ad-22(e)(7)(viii).

The Commission finds that the proposed change is consistent with Section 17A(b)(3)(F) of the Act,[11] which requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions. The Commission understands that the proposed rule change constitutes a limited expansion of OCC's ability to address liquidity needs that arise from scenarios that, while relatively less extreme than a Settlement Entity suffering a bankruptcy, insolvency, resolution, suspension of operations, or similar event, nevertheless can prevent daily settlement from occurring. The Commission therefore believes that the proposed rule change is designed to enhance OCC's ability to access liquid resources under such circumstances, which, in turn, would allow OCC to continue to meet its settlement obligations to its Clearing Members in a timely fashion, thereby promoting prompt and accurate clearance and settlement of securities transactions.

Specifically, the Commission believes that the proposed rule change is designed to expand OCC's existing borrowing authority in a scenario where a Settlement Entity is temporarily unable to achieve daily settlement, but is not facing bankruptcy, insolvency, resolution, suspension of operations, or similar event. Therefore, the proposed rule change is designed to provide OCC with an alternative tool with which to address what OCC describes as an "extraordinary circumstance" that would enable OCC to borrow against the Clearing Fund in order to avoid disrupting its ordinary settlement cycle. The Commission believes that the authority to take such action is designed to avoid imposing a disruption on Clearing Members and reduce the need to extend the settlement window, which could allow OCC to settle transactions in a more timely fashion. Accordingly, the

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[11] 15 U.S.C. 78q-1(b)(3)(F).

Commission finds that the proposed rule change is designed to promote the prompt and accurate clearance and settlement of securities transactions, and is therefore consistent with Section 17A(b)(3)(F) of the Act.[12]

B. Consistency With Rule 17Ad-22(e)(7)(viii) under the Act

The Commission further believes that the proposed rule change is consistent with Rule 17Ad-22(e)(7)(viii), which requires that a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to, as applicable, effectively measure, monitor, and manage liquidity risk that arises in or is borne by the covered clearing agency, including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, addressing foreseeable liquidity shortfalls that would not be covered by its liquid resources and seek to avoid unwinding, revoking, or delaying the same-day settlement of payment obligations.[13]

The Commission believes that the proposed rule change is designed to improve OCC's ability to address a temporary liquidity need resulting from the failure of a Settlement Entity to achieve timely settlement. The Commission believes that the proposed rule change is designed to provide OCC with additional tools to address a foreseeable, temporary liquidity shortfall to prevent the unwinding, revoking, or delaying of same-day settlement should that scenario materialize, and is therefore consistent with Rule 17Ad-22(e)(7)(viii) under the Act.

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[12] Id.

[13] 17 CFR 240.17Ad-22(e)(7)(viii).

III. Conclusion

On the basis of the foregoing, the Commission finds that the proposed change is consistent with the requirements of the Act, and in particular, with the requirements of Section 17A of the Act[14] and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[15] that the proposed rule change (SR-OCC-2017-017) be, and it hereby is, approved.

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

Eduardo A. Aleman
Assistant Secretary

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14 In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

15 15 U.S.C. 78s(b)(2).

16 17 CFR 200.30-3(a)(12).