

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-82311; File No. SR-OCC-2017-008)

December 13, 2017

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving Proposed Rule Change Related to The Options Clearing Corporation's Collateral Risk Management Policy

I. Introduction

On October 27, 2017, the Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change (SR-OCC-2017-008) to formalize and update OCC’s Collateral Risk Management Policy. The proposed rule change was published for comment in the Federal Register on November 9, 2017.<sup>3</sup> The Commission received one comment letter regarding the proposed change.<sup>4</sup> For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description of the Proposed Rule Change

This proposed rule change would formalize and update OCC’s Collateral Risk Management Policy (“CRM Policy”). The CRM Policy describes the categories of risk that are considered by OCC in determining which asset classes should be acceptable forms of collateral as margin assets and Clearing Fund contributions. OCC’s assessment of an asset class generally

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

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Securities Exchange Act Release No. 82009 (Nov. 3, 2017), 82 FR 52079 (Nov. 9, 2017) (SR-OCC-2017-008) (“Notice”).

<sup>4</sup> Letter from Michael Kitlas, dated November 3, 2017. See comments on the proposed rule change (SR-OCC-2017-008), <https://www.sec.gov/comments/sr-occ-2017-008/occ2017008.htm>.

includes an evaluation of credit risk, liquidity risk, and market risk.<sup>5</sup> With respect to credit risk, the CRM Policy requires OCC staff to evaluate the creditworthiness of counterparties, including custodial agents and settlement banks and to monitor the health of such counterparties on an ongoing basis.<sup>6</sup> Regarding liquidity risk, OCC gives no value to a participant for its own (or its affiliate's) debt or equity securities, and limits the amount of a particular asset type that a participant may pledge under the CRM Policy.<sup>7</sup> With respect to market risks, the CRM Policy provides that eligible asset classes are accepted after consideration of their liquidity, price transparency, price volatility, offset potential with contracts cleared by OCC, modeling implications and projected inventories.<sup>8</sup>

The CRM Policy describes OCC's approach to valuing collateral and setting and applying haircuts. OCC's pricing information, as described in the CRM Policy, feeds into OCC's processes for establishing haircuts, daily mark-to-market valuation of collateral, and intraday valuation of collateral. Given the importance of pricing data to inform these processes, OCC maintains redundant information feeds from multiple sources to help ensure accuracy and quality.<sup>9</sup>

The CRM Policy also summarizes OCC's two approaches for valuing collateral: Collateral in Margins ("CiM") and haircuts.<sup>10</sup> Under the CiM approach, the current market value of margin

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<sup>5</sup> Notice, 82 FR at 52080.

<sup>6</sup> Id.

<sup>7</sup> Id.

<sup>8</sup> Id.

<sup>9</sup> Notice, 82 FR at 52080-81.

<sup>10</sup> Notice, 82 FR at 52081.

assets is included as a positive asset value in the calculation of a portfolio's net asset value within OCC's System for Theoretical Analysis and Numerical Simulations ("STANS"). OCC then offsets this positive asset value based on, among other things, the expected shortfall and stress test charges associated with an account, resulting in a net excess or net deficit.<sup>11</sup> For collateral that is not managed using the CiM process, the CRM Policy provides that OCC subjects such collateral to percentage haircuts established at the time the collateral is accepted by OCC and that are monitored regularly to help ensure the haircuts remain adequate.<sup>12</sup>

Additionally, the CRM Policy provides that OCC's Credit and Liquidity Working Group must review the policy's performance and adequacy on at least an annual basis, including with respect to collateral eligibility, concentration limits, collateral haircuts and monitoring processes.<sup>13</sup>

### III. Summary of Comment Received

The Commission received one comment letter in response to the proposed rule change.<sup>14</sup>

The commenter stated that the proposed rule change is consistent with the Act.<sup>15</sup>

### IV. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act 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

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<sup>11</sup> Notice, 82 FR at 52081, note 23.

<sup>12</sup> Notice, 82 FR at 52081.

<sup>13</sup> Id.

<sup>14</sup> See supra note 4.

<sup>15</sup> Id.

organization.<sup>16</sup> After carefully considering the proposed rule change and the comment letter, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to OCC. More specifically, the Commission finds that the proposal is consistent with Section 17A(b)(3)(F) of the Act and Rule 17Ad-22(e)(5) under the Act.

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

Section 17A(b)(3)(F) of the Act requires that the rules of a registered clearing agency be designed to do, among other things, the following: (1) promote the prompt and accurate clearance and settlement of securities transactions; (2) assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible; and (3) in general protect investors and the public interest.<sup>17</sup>

The CRM Policy describes OCC's process for limiting the collateral that it accepts to assets with low credit, liquidity, and market risk. The acceptance of only low-risk collateral increases the likelihood that such collateral can be liquidated in a timely manner, thereby enhancing OCC's ability to continue to perform its critical services for the financial markets while also managing a default. The CRM Policy also describes how OCC haircuts such collateral, and requires review of such haircuts at least annually. Ensuring that collateral haircuts are appropriately set and reviewed on a regular basis increases the likelihood that OCC will collect and hold collateral that can be liquidated at a value at or above the value attributed to it. This approach thereby increases the likelihood that OCC will be able to continue to meet its

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<sup>16</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>17</sup> 15 U.S.C. 78q-1(b)(3)(F).

settlement obligations and manage the default of a clearing member by liquidating the defaulting clearing member's collateral in a timely and effective manner.

The timely liquidation of collateral at or above the expected value would, therefore, support OCC's ability to continue to meet settlement obligations on time, promoting the prompt and accurate clearance and settlement of securities transactions. In addition, being able to successfully liquidate collateral in a timely and effective manner would reduce the likelihood of OCC having to draw on mutualized resources, including Clearing Fund contributions. As such, the Commission believes that the proposal would help assure the safeguarding of securities and funds which are in the custody or control of OCC, or for which OCC is responsible. As a result, the Commission also finds that the proposed rule change, in general, protects investors and the public interest. Accordingly, the Commission finds that the proposed rule change is consistent with Section 17A of the Act.<sup>18</sup>

B. Consistency with Rule 17Ad-22(e)(3) of the Act

Rule 17Ad-22(e)(5) requires that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to limit the assets it accepts as collateral to those with low credit, liquidity, and market risks; set and enforce appropriately conservative haircuts and concentration limits if the covered clearing agency requires collateral to manage its or its participants' credit exposure; and, require a review of the sufficiency of its collateral haircuts and concentration limits to be performed not less than annually.<sup>19</sup>

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<sup>18</sup> 15 U.S.C. 78q-1.

<sup>19</sup> 17 CFR 240.17Ad-22(e)(5).

As discussed above, the proposed CRM Policy would address each component of Rule 17Ad-22(e)(5).<sup>20</sup> First, the proposed CRM Policy requires that, in determining forms of collateral as margin assets and Clearing Fund contributions, OCC evaluates the market, credit, and liquidity risk of an asset class. Second, the CRM Policy provides for the maintenance of redundant pricing information feeds from multiple sources to ensure the availability of information that is critical to OCC's daily and intraday processes for collateral valuation. The CRM Policy further describes OCC's processes for setting haircuts either via the use of STANS or percentage-based haircuts. Third, the proposed CRM requires at least annual review of concentration limits and collateral haircuts. The Commission finds, therefore, that the proposed rule change is consistent with Rule 17Ad-22(e)(5).<sup>21</sup>

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<sup>20</sup>

Id.

<sup>21</sup>

17 CFR 240.17Ad-22(e)(5).

V. 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<sup>22</sup> and the rules and regulations thereunder.

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act that the proposed rule change (SR-OCC-2017-008) be, and hereby is, approved.

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.<sup>23</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>22</sup> 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).

<sup>23</sup> 17 CFR 200.30-3(a)(12).