



RECEIVED
OCT 07 2015
OFFICE OF THE SECRETARY

FACSIMILE TRANSMITTAL SHEET

TO: **Brent Fields, Secretary**
 COMPANY: **Securities and Exchange Commission**
 FAX NUMBER: **202-772-9324**
 PHONE NUMBER:

FROM: **Eric Swanson, General Counsel**
 DATE: **10/07/2015**
 TOTAL NO. OF PAGES INCLUDING COVER:

RE: **SR-OCC-2015-02; Petitioners' Statement in Opposition to Action taken by Delegated Authority**

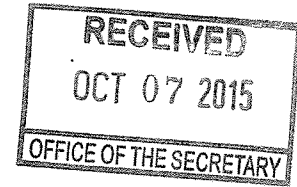
URGENT FOR REVIEW PLEASE COMMENT REPLY ASAP ORIGINAL MAILED

NOTES/COMMENTS:

PRIVILEGED AND CONFIDENTIAL The information contained in the pages of the following facsimile transmission is intended for the use of the addressee(s) named above. If the reader of this message is not the intended recipient(s) or their agent or employee, dissemination of this communication in any manner is strictly prohibited. Anyone who receives this communication in error should notify us immediately by telephone and return the original message to us at the address below, via U.S. Mail.

October 7, 2015

VIA COURIER AND FAX



Brent Fields
Secretary
Securities and Exchange Commission
100 F. Street N.E.
Washington, D.C. 20549-1090

RE: SR-OCC-2015-02, Statement in Opposition to Action Made by Delegated Authority

Dear Mr. Fields,

BATS Global Markets, Inc. ("BATS"), on behalf of its subsidiary options exchange, BATS Exchange, Inc., BOX Options Exchange, LLC, and Miami International Securities Exchange, LLC, hereby submit the enclosed original and three copies of Statement in Opposition to Action Made by Delegated Authority in relation to the above-captioned matter. Also enclosed, please find a Certificate of Service and facsimile confirmation sheet.

Any questions concerning this matter can be directed to:

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.
8050 Marshall Dr., Suite 120
Lenexa, KS 66214
(913) 815-7000 (phone)
(913) 815-7119 (fax)

Lisa J. Fall
President
BOX Options Exchange LLC
101 Arch Street, Suite 610
Boston, MA 02110
(617) 235-2235 (phone)
(617) 235-2253 (fax)

Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC
7 Roszel Road, Suite 5-A
Princeton, NJ 08540

(609) 897-7315 (phone)
(609) 987-2201 (fax)

Sincerely,



Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.


Lisa J. Fall
President
BOX Options Exchange, LLC

Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC

(609) 897-7315 (phone)
(609) 987-2201 (fax)

Sincerely,

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.



Lisa J. Fall
President
BOX Options Exchange, LLC

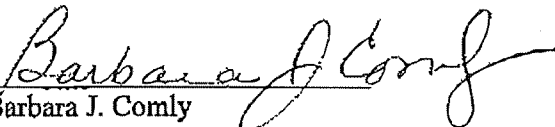
Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC

(609) 897-7315 (phone)
(609) 987-2201 (fax)

Sincerely,

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.

Lisa J. Fall
President
BOX Options Exchange, LLC



Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC

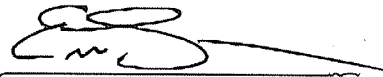
CERTIFICATE OF SERVICE

We, Eric Swanson, General Counsel and Secretary of BATS Global Markets, Inc., Lisa J. Fall, President of BOX Options Exchange, LLC, and Barbara J. Comly, Executive Vice President, General Counsel and Corporate Secretary of Miami International Securities Exchange, LCC, hereby certify that on October 7, 2015, we served copies of our Statement in Opposition to Action Taken by Delegated Authority on:

Brent Fields
Secretary
Securities and Exchange Commission
100 F. Street N.E.
500 Washington, D.C. 20549-1090

William J. Nissen
Sidley Austin, LLP
One South Dearborn Street
Wacker Drive, Suite
Chicago, IL 60603

Dated: October 7, 2015



Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.

Dated: October 7, 2015

Lisa J. Fall
President
BOX Options Exchange LCC

Dated: October 7, 2015

Barbara J. Comly
Executive Vice President, General Counsel and
Corporate Secretary
Miami International Securities Exchange, LLC

CERTIFICATE OF SERVICE

We, Eric Swanson, General Counsel and Secretary of BATS Global Markets, Inc., Lisa J. fall, President of BOX Options Exchange, LLC, and Barbara J. Comly, Executive Vice President, General Counsel and Corporate Secretary of Miami International Securities Exchange, LCC, hereby certify that on October 7, 2015, we served copies of our Statement in Opposition to Action Taken by Delegated Authority on:


Brent Fields
Secretary
Securities and Exchange Commission
100 F. Street N.E.
500 Washington, D.C. 20549-1090

William J. Nissen
Sidley Austin, LLP
One South Dearborn Street
Wacker Drive, Suite
Chicago, IL 60603

Dated: October 7, 2015

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.

Dated: October 7, 2015



Lisa J. Fall
President
BOX Options Exchange LCC

Dated: October 7, 2015

Barbara J. Comly
Executive Vice President, General Counsel and
Corporate Secretary
Miami International Securities Exchange, LLC

CERTIFICATE OF SERVICE

We, Eric Swanson, General Counsel and Secretary of BATS Global Markets, Inc., Lisa J. Fall, President of BOX Options Exchange, LLC, and Barbara J. Comly, Executive Vice President, General Counsel and Corporate Secretary of Miami International Securities Exchange, LCC, hereby certify that on October 7, 2015, we served copies of our Statement in Opposition to Action Taken by Delegated Authority on:

Brent Fields
Secretary
Securities and Exchange Commission
100 F. Street N.E.
500 Washington, D.C. 20549-1090

William J. Nissen
Sidley Austin, LLP
One South Dearborn Street
Wacker Drive, Suite
Chicago, IL 60603

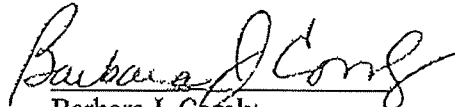
Dated: October 7, 2015

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.

Dated: October 7, 2015

Lisa J. Fall
President
BOX Options Exchange LCC

Dated: October 7, 2015



Barbara J. Comly
Executive Vice President, General Counsel and
Corporate Secretary
Miami International Securities Exchange, LLC

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

PETITION FOR REVIEW 1

Preliminary Statement 1

Background on OCC and Description of the Rule Filing..... 6

Applicable Legal Requirements 8

Deficiencies in Staff’s Approval of the Rule Filing 9

 A. The Proposed Capital Plan does not Provide for the Equitable Allocation of Reasonable Dues, Fees, and Other Charges Among its Participants 9

 B. The Proposed Capital Plan is not Designed to Protect Investors and the Public Interest...... 10

 C. The Proposed Capital Plan Creates an Undue Burden On Competition 11

 D. The Proposed Capital Plan was the Result of a Flawed Governance Process in Violation of the OCC’s By-Laws and Form 19b-4 13

CONCLUSION 19

TABLE OF AUTHORITIES

STATUTES

5 U.S.C. § 706(2)(A)	3
15 U.S.C. § 78(C)(f)	8
15 U.S.C. § 78w(a)(2)	8
15 U.S.C. § 80a-2(c)	8

CASES

<i>Business Roundtable v. Securities and Exchange Commission</i> , 647 F.3d 1144 (D.C. Cir. 2011)	3, 8
<i>Chamber of Commerce v. Securities and Exchange Commission</i> , 412 F.3d 133 (D.C. Cir. 2005)	3
<i>American Equity Inv. Life Ins. Co. v. Securities and Exchange Commission</i> 513 F.3d 166 (D.C. Cir. 2009)	8

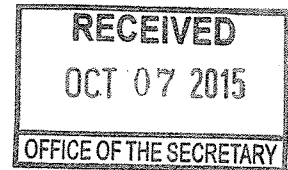
RULES

17 CFR 201.430	7
17 CFR 201.431	7
17 CFR 201.411(b)(2)	7

OTHER AUTHORITIES

Exchange Act Release No. 74452 (March 6, 2015), 80 FR 12058 (March 12, 2015)	1, 4, 10, 11, 12
Exchange Act Release No. 46469 (September 6, 2002), 67 FR 58093 (September 13, 2002)	7, 13, 14
OCC By-Laws, available at: http://www.theocc.com/ components/docs/legal/rules_and_bylaws/occ_bylaws.pdf	14
OCC Charter, available at: http://www.optionsclearing.com/components/ docs/about/corporate-information/board_of_directors_charter.pdf	17

OCC Board of Directors Corporate Governance Principles," *available at*
[http://www.theocc.com/components/docs/about/corporate-
information/board_corporate_governance_principles.pdf](http://www.theocc.com/components/docs/about/corporate-information/board_corporate_governance_principles.pdf) 17



Before the
SECURITIES AND EXCHANGE COMMISSION

_____)	
In the Matter of the Petitions of:)	File No. SR-OCC-2015-02
)	
)	
BATS Global Markets, Inc.,)	
BOX Options Exchange LLC, and)	
Miami International)	
Securities Exchange, LLC)	
_____)	

STATEMENT IN OPPOSITION TO ACTION MADE BY DELEGATED AUTHORITY

BATS Global Markets, Inc. ("BATS"), BOX Options Exchange, LLC ("BOX"), and Miami International Securities Exchange, LLC ("MIAX") (collectively, the "Petitioners"), hereby submit a statement in opposition to the action of the Division of Trading and Markets made by delegated authority on March 6, 2015, approving a rule change by the Options Clearing Corporation concerning a proposed capital plan ("the Capital Plan").¹

Preliminary Statement

Commission staff acting pursuant to delegated authority approved the OCC's Capital Plan authorizing the OCC to raise capital from its four shareholder exchange groups² and for the first time pay dividends, in perpetuity, to this select group of shareholder exchanges at a level

¹ See Securities Exchange Act Release No. 74452 (March 6, 2015), 80 FR 13058 (March 12, 2015) (SR-OCC-2015-02).

² The shareholder exchanges are: Chicago Board Options Exchange, Incorporated ("CBOE"), International Securities Exchange ("ISE"), NASDAQ OMX PHLX LLC ("NASDAQ"), and NYSE MKT LLC and NYSE Arca, Inc. (collectively, "NYSE").

that is significantly above market rates – estimated to be anywhere from 16% - 20% per year in the first few years and potentially significantly higher thereafter.³ The proposed Capital Plan would radically change the nature of the OCC, which has served for decades as a non-profit utility operating for the benefit of its clearing members and the investing public, by turning it into a for-profit monopoly operating for the benefit of the four shareholder exchanges. The effect of the proposed Capital Plan would be to significantly undermine competition among the various options exchanges and impose excessive costs on clearing firms and investors, which will degrade the quality of the options markets.

The proposed Capital Plan devised by the OCC would effectively allow its shareholder exchanges to monetize for their benefit the OCC's monopoly over options clearing. If not rejected, the proposed Capital Plan will create a massive wealth transfer from options investors to OCC's shareholder exchanges that will stifle future competition in the options market and will result in an ongoing and unnecessary increase in the costs of trading listed options. The extraordinary subsidy to this limited group of exchanges will be borne by clearing members and options investors who will ultimately fund the excessive payments.

When first proposed by the OCC, the Capital Plan appeared to reflect a legitimate attempt to increase the OCC's capital position through a flawed and costly process that served only to benefit the OCC's shareholder exchanges. Now, as time has passed and the OCC has amassed significant new capital without the Capital Plan in effect, the proposed Capital Plan appears to solely reflect an unconscionable effort by the OCC's shareholder exchanges to greatly enrich themselves at the expense of the industry.

³ The Capital Plan would permit the OCC to amend its By-Laws and certain other governing documents to effect the raising of additional capital from, and the paying of dividends to, the shareholder exchanges.

Commission staff approved the Capital Plan pursuant to delegated authority and committed numerous material errors in doing so. Significantly, the Commission staff conducted virtually no substantive analysis of the competitive – or anticompetitive – effects of the proposed Capital Plan. The Commission staff’s order approving the Capital Plan pursuant to delegated authority made no reference to any market studies, reviews, statistics, or economic analysis relating to how the Capital Plan would affect competition among options exchanges, fee structures and what the impact would be on investors or the quality of the options markets. The approval of such sweeping changes to the options markets without engaging in or considering such studies, is arbitrary and capricious manner and an abuse of discretion.⁴

The Commission staff also committed numerous material errors of fact and law. For example, the staff acknowledged the likely burden on competition presented by the OCC’s Capital Plan, but misanalysed both the facts and the law in concluding that such burden was not *undue*. In particular, the staff rejected arguments that the rate of return that will be realized by the shareholder exchanges is excessive and amounts to an improper subsidy. The staff relied heavily on the fact that OCC’s Board of Directors (the “Board”) approved the Capital Plan. In so doing, the staff failed to account for the unique nature of the OCC, including (i) the impact of its status as a monopoly, and (ii) the outsized influence the shareholder exchanges exert over the OCC’s affairs. Further, the staff’s analysis appears to be based on a false tradeoff between the OCC’s need to raise capital and the burden on competition created by the proposal, concluding

⁴ See Administrative Procedure Act, 5 U.S.C. §706(2)(A) (authorizing courts to set aside agency action that is “arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law”); *Business Roundtable v. Securities and Exchange Commission*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (holding that “the Commission acted arbitrarily and capriciously for having failed . . . adequately to assess the economic effects of a new rule”); *Chamber of Commerce v. Securities and Exchange Commission*, 412 F.3d 133, 144 (D.C. Cir. 2005) (finding Commission violated its obligations under the APA because it failed in its “statutory obligation to do what it can to apprise itself – and hence the public and the Congress—of the economic consequences of a proposed regulation before it decides whether to adopt the measure.”).

that “even if OCC’s Capital Plan may result in some burden on competition, such a burden is necessary and appropriate in furtherance in the purposes of the Act given the importance of OCC’s ongoing operations to the U.S. options market and the role of the Capital Plan in assuring its ability to facilitate the clearance and settlement of securities transactions in a wide range of market conditions.”⁵ This logic erroneously assumes that the only issue at stake is the OCC’s need to raise capital. In fact, the Petitioners - at least until now - have not disputed the OCC’s need to raise capital; rather, the Petitioners have taken issue with the means by which the OCC is raising that capital and fundamentally altering the nature of the OCC in the process. As discussed in more detail below, the Petitioners do now question the OCC’s conclusion regarding the amount of capital it needs to raise - not only is the record devoid of any evidence supporting the OCC’s conclusion that it needs \$247 million in immediate target capital and commitments for \$117 million in Replenishment Capital, other than the OCC’s conclusory representation that the amount was derived from a third party study, the OCC has over the past year dramatically enhanced its capital position through fee increases to nearly equal the amount it seeks to raise through the Capital Plan.

The Commission staff also erroneously dismissed concerns regarding the impact on future clearing fees, reasoning that any OCC fee increases will need to be filed with the Commission, despite the fact that such filings will be too attenuated, both temporally and substantively, from the dividend to allow for adequate review of their excessiveness by either the Commission or the public.

Significantly, the Commission staff also failed to adequately address the evidence in the record demonstrating that, in approving the Capital Plan, the OCC failed to comply with

⁵ Order, *supra* note 1, at 13068.

Commission-required provisions of the OCC's By-Laws and Charter designed to prevent conflicts of interest and to give non-shareholder exchanges, like Petitioners, fair representation in the affairs of the OCC through express notice of the type of action taken here and an opportunity to be heard. Commission staff acknowledged that "[s]everal commenters raised concerns that OCC's Capital Plan was not approved in accordance with OCC's By-Laws due to vacancies on the Board, that certain Board directors (*i.e.*, Stockholder Exchanges) were 'interested parties' and therefore should have recused themselves from any decision to approve or disapprove OCC's proposal, and OCC failed to promptly inform non-Stockholder Exchanges of the proposed change."⁶ But, in rejecting these arguments, the Commission staff merely cited to representations from the OCC that it complied with its By-Laws, stating that the staff has no basis to dispute the OCC's representations. In so doing, the Commission staff failed to articulate how the OCC complied with its By-Laws and, critically, the Commission staff ignored the specific representations from Petitioners, the exact parties the Commission was concerned about when it required the OCC to insert certain protections into its By-Laws, that the OCC failed to promptly notify the Petitioners of this matter of competitive significance as expressly required by the OCC's By-Laws, in order to enable Petitioners to exercise their rights to address the Board on the topic as further required by the OCC's By-Laws. The net result of OCC's conduct was to deny the Petitioners their rights to fair representation in the OCC's affairs.

Finally, in April 2014, the OCC increased its clearing fees by 60%-70%, which resulted in an increase in the OCC's capital from \$25 million to \$130 million by year-end 2014, which includes \$33 million the OCC set aside to pay a discretionary rebate to the industry. By year-end 2015, less than three months from now, Petitioners estimate OCC's capital will increase to \$235

⁶ *Id.*

million, which includes the \$33 million of set-aside but unpaid industry rebates for 2014, and \$33 million of set-aside unpaid rebates for 2015. Hence, without the Capital Plan in place, in less than two years the OCC has been able to raise 95% of the capital it alleges it still needs to raise through the proposed Capital Plan, without the onerous requirement to pay excessive dividends in perpetuity to the exchange shareholders. With respect to the additional \$117 million in Replenishment Capital committed by the exchange shareholders in the Capital Plan, Petitioners submit that the likelihood of the OCC needing to call that capital is extremely low, but in any case, there are a multitude of less expensive ways to secure that capital without imposing the unnecessary and perpetual burden on the industry created by the proposed Capital Plan.

For these reasons, and as discussed in more detail below, the Petitioners respectfully request that the Commission reject the proposed Capital Plan.

Background on OCC and Description of the Proposed Capital Plan

Founded in 1973, the OCC is the sole clearing house for exchange-listed options in the U.S. Transactions in listed options are required to occur through an OCC clearing member broker-dealer. In addition, all options transactions are required to occur on a registered national securities exchange; unlike in equities, there is no off-exchange trading, or internalization, permitted in exchange-listed options. While the OCC serves as the sole centralized clearing house for listed options transactions, pursuant to the market structure established by the Commission, the various options exchanges directly compete with one another for order flow through pricing and execution services.

All options exchanges are required to be OCC "participants," which had historically been achieved by options exchanges becoming equity shareholders of the OCC. In 2002, the OCC

amended its By-Laws to foreclose additional equity ownership by new options exchanges.⁷

Options exchanges launched since this rule change became participants of the OCC by becoming noteholders. Thus, this rule change had the effect of permanently limiting equity ownership of the OCC to the following exchange groups – CBOE, NYSE, NASDAQ, and ISE. Consequently, the Petitioners, formed after the 2002 rule change, are only noteholders.

Since its founding, the OCC has operated as a non-profit industry utility monopoly for the benefit of its clearing members and the options industry as a whole. As such, the OCC set fees to its clearing members at a level that was designed to cover its operating expenses and maintain capital reserves as the OCC deemed necessary to meet its obligations. To the extent the OCC collected fees each year in excess of its operating expenses and capital needs, the OCC historically refunded that excess to its clearing members.

Under the rule filing approved by the Order, the OCC would amend its By-Laws and other governing documents to allow the OCC to raise significant new capital and pay dividends for the first time to its shareholder exchanges. The existing OCC shareholder exchanges would contribute \$247 million of immediate capital, and commit to contributing additional Replenishment Capital under certain dire circumstances. In exchange for the contribution, those shareholder exchanges would receive an annual dividend (subject to the OCC's compliance with its capital requirements) for so long as those exchanges continued to be equity shareholders. As a result of the dividend proposed to be paid to the shareholder exchanges, the amount of any refunds of excess capital to clearing members will be reduced, and could be permanently

⁷ See Securities Exchange Act Release No. 46469 (September 6, 2002), 67 FR 58093 (September 13, 2002) (SR-OCC-2002-02) ("2002 By-Laws Amendment Order").

eliminated under certain circumstances if the shareholder exchanges are required to contribute replenishment capital.

The exact amount of the dividend to be paid to the shareholder exchanges is not known because it is redacted from the rule filing. However, based on the information disclosed in the rule filing, estimates of the rate of return to the shareholder exchanges range from 16%-20% per year in the first few years, and possibly significantly higher than that in later years.

Applicable Legal Requirements

Pursuant to Section 19(b)(2)(C) of the Exchange Act of 1934 (“the Act”), the Commission must find that a proposed rule change of a self-regulatory organization is consistent with Act before it can approve such rule change. Section 17A of the Act contains the requirements applicable to the rules of clearing agencies such as the OCC. Of relevance to the Petitioners’ grievances, Section 17A(b)(3)(D) of the Act requires that the rules of a clearing agency provide for the equitable allocation of reasonable dues, fees, and other charges among its participants, Section 17A(b)(3)(F) of the Act requires that the rules of a clearing agency must be designed to, among other things, “protect investors and the public interest”, and Section 17A(b)(3)(I) requires that the rules of a clearing agency “not impose any burden on competition not necessary or appropriate in furtherance of the purposes of this title.”

Additionally, under the Act, “the Commission has a unique obligation to consider the effect of a new rule upon efficiency, competition and capital formation.”⁸ Finally, pursuant to Form 19b-4, “[t]he Commission will not approve a proposed rule change . . . before the self-

⁸ *Business Roundtable*, 647 F.3d at 1148 (quoting 15 U.S.C. §§ 78(C)(f), 78w(a)(2), 80a-2(c)). See *American Equity Inv. Life Ins. Co. v. Securities and Exchange Commission*, 513 F. 3d 166, 177 (D.C. Cir. 2009) (finding Commission’s consideration of the effect of a rule on efficiency, competition and capital formation was arbitrary and capricious because the SEC did not disclose a reasoned basis for its conclusion that the rule would increase competition).

regulatory organization has completed all action required to be taken under its constitution, articles of incorporation, bylaws, rules, or instruments corresponding thereto.”⁹

The Proposed Capital Plan does not Provide for the Equitable Allocation of Reasonable Dues, Fees, and Other Charges Among its Participants

The OCC will be required to fund the excessive dividends to the shareholder exchanges in perpetuity through excessive and unreasonable fees on market participants. In approving the Capital Plan pursuant to delegated authority, Commission staff dismissed these concerns stating that “[f]uture changes to OCC’s fee schedule as well as future changes to the Fee Policy, Refund Policy, and Dividend Policy, are subject to Section 19(b)(1) of the Act and Section 806(e) of the Payment, Clearing, and Settlement Supervision Act, as applicable, both of which require OCC to (i) submit appropriate regulatory filings with the Commission, (ii) provide an opportunity for public comment, and (iii) require the Commission to review and ultimately disapprove, object to, or require modification or rescission, as applicable, if these future proposed changes do not meet regulatory requirements.”¹⁰ The flaw with the staff’s finding is that the OCC sets fees each year and throughout the year based on its forecasts of operating costs, capital needs, and options volumes, while the dividends are only paid after year-end when the OCC can determine the extent that it collected fees in excess of these forecasts. Hence, at the moment in time when fee increases are filed with the Commission, the impact on the dividend will be too attenuated, both temporally and substantively, from the payment of the dividend itself.

⁹ <https://www.sec.gov/about/forms/form19b-4.pdf> (emphasis added).

¹⁰ See Order, *supra* note 1, at 13067 (citations omitted).

The Petitioners submit that neither the Commission staff nor the public will be adequately equipped to determine the extent to which fees were set in anticipation of funding an excessive dividend at year-end, and by the time the dividend can be determined with precision it will be too late for the Commission to act to suspend or abrogate a fee increase from months earlier that in retrospect was excessive.¹¹ As such, the rule filing process regarding future OCC fee increases is not an adequate protection against a massive transfer of wealth from clearing members and the investing public to the shareholder exchanges, and the proposed Capital Plan fails to meet the requirements of Section 17A(b)(3)(D) of the Act.

The Proposed Capital Plan is not Designed to Protect Investors and the Public Interest

The proposed Capital Plan fundamentally changes the nature of the OCC from a non-profit industry utility operated for the benefit of its clearing members and options investors, into a for-profit monopoly operating for the benefit of its exclusive group of shareholder exchanges. While there is nothing unique today about an SRO operating as a for profit business, with respect to the OCC, this transition is not designed to protect investors and is not in the public interest in light of the unique role of the OCC, its ownership, and its governance, including the following:

- The OCC is a monopoly – unlike other SROs (*i.e.* registered national securities exchanges), there is no competition for the OCC's services and, hence, no competitive pressures on fees.
- There is no over-the-counter market for listed options transactions. As such, every execution of a listed options contract *must* be cleared through the OCC subject to the

¹¹ One need look no further than the history of the OCC's payments of rebates to OCC clearing members to see the futility of the Commission fee filing process on identifying excessive fees. Historically, since the OCC was founded it has paid annual rebates to its member clearing firms, sourced from overpayments in fees, in amounts in the aggregate equal to tens of millions of dollars per year. While that has not been a problem in as much as the overpayments were being passed back to the clearing members responsible for paying the fees, it does highlight that the fee setting process at the OCC and the Commission review of that process has not resulted in an effective constraint on the OCC charging excessive fees.

OCC's fees; broker-dealers cannot engage in internal compression or netting to reduce their exposure to OCC's fees.

- The OCC is owned by four exchange groups (*i.e.* CBOE, NYSE, NASDAQ, and ISE) and, by rule, the OCC has prohibited any other options exchange from becoming a shareholder.
- Each of the existing shareholder exchanges possesses a veto right over certain aspects related to the OCC's affairs, including the issuance of equity that could dilute its ownership.¹²

The proposed Capital Plan is not designed to protect investors or the public interest but is instead designed to benefit the shareholder exchanges at the expense of investors by paying the shareholder exchanges an outsized dividend, or more aptly, subsidy, in perpetuity. To fund this perpetual subsidy, the OCC will impose excessive and unreasonable costs on the options industry; costs that will ultimately be borne by investors in the form of higher fees, wider spreads, and reduced liquidity. As such, the proposed Capital Plan fails to meet the requirements of Section 17A(b)(3)(F) of the Act.

The Proposed Capital Plan Creates an Undue Burden on Competition

The proposed Capital Plan would result in an undue burden on competition by unfairly discriminating between the Petitioners and the shareholder exchanges. The OCC holds a unique position in the options market – it is a utility monopoly that clears all transactions in listed options executions. All options exchanges are required to be participants of the OCC, but the

¹² Petitioners understand that the private shareholder agreements between each of the four OCC shareholder exchanges and the OCC include a provision requiring unanimity of the shareholder exchanges in order for the OCC to take certain actions, including, at a minimum, actions that would have the effect of diluting each of those shareholder's equity stake in the OCC.

OCC amended its By-Laws in 2002 such that no subsequent options exchange is allowed to own equity in the OCC. As such, although similarly situated in terms of their status, function in, and contribution to, the options industry, not all options exchanges are treated similarly vis-à-vis their relationship with this industry utility monopoly. While this has been historically acceptable because the OCC acted in the best interests of its clearing members and the industry at-large, it will be unacceptable if the OCC is allowed to use the fees charged on options transactions – fees to which all exchanges contribute equally – to fund excessive subsidies solely to the select group of shareholder exchanges. The net result of the proposed Capital Plan would be to create and undue burden on the Petitioners' ability to compete with the shareholder exchanges.

In approving the Capital Plan pursuant to delegated authority, Commission staff recognized that a dividend to the shareholder exchanges that does not accurately reflect the true risk of the investment may result in a burden on competition. However, the staff erred in concluding that because the OCC is a unique entity that is not publicly traded, determining the cost of capital is subjective and, hence, the "OCC's Board of Directors *must* use its judgment to determine the appropriate or competitive rate of return and the dividend policy that appropriately reflects the risk of the Stockholder Exchanges' equity investment."¹³ To the contrary, private companies routinely raise capital through competitive processes that are not left solely to the judgment of a board of directors and that result in a competitive rate of return. Here especially, where the governance process was so heavily biased in favor of the shareholder exchanges that stand to accrue excess monopoly rents from the proposed Capital Plan, a competitive process would have informed the Board's judgment to ensure it was, in fact, fulfilling its fiduciary obligations to the OCC.

¹³ Order, *supra* note 1, at 13068 (*emphasis added*).

Moreover, while in approving the Capital Plan pursuant to delegated authority Commission staff recognized that the Capital Plan may result in some burden on competition, the staff rejected the idea that that burden was undue, finding that “such a burden is necessary and appropriate in furtherance of the purposes of the Act given the importance of OCC’s ongoing operations to the U.S. options market and the role of the Capital Plan in assuring its ability to facilitate the clearance and settlement of securities transactions in a wide range of market conditions.”¹⁴ But, the question of whether the competitive burden is “undue” is necessarily determined by reference to the extent of the anticompetitive subsidy that will be paid solely to the shareholder exchanges (the precise amounts of which have been redacted in the record).¹⁵ Taken to its logical conclusion, the staff’s finding suggests that regardless of the amount of the subsidy, the resulting competitive burden would never be considered undue but would always be considered necessary and appropriate in furtherance of the Act. Again, where, as here, the proposed Capital Plan was the result of a confluence of unique factors associated with the OCC’s monopoly status and governance structure that inured to the benefit of the shareholder exchanges, the staff’s findings that any dividend paid is appropriate and necessary, regardless of its amount and its impact on competition, constitutes an erroneous conclusion of law.

¹⁴ Order, *supra* note 1, at 13068.

¹⁵ Petitioners have estimated that a \$30 million annual dividend to the shareholder exchanges would enable those shareholder exchanges, depending on the market share of each, to reduce fees by between 7% and 22%. See Petitioners Response to Motion of the OCC to Lift Automatic Stay, dated April 8, 2015.

**The Capital Plan was the Result of a Flawed Governance Process in Violation of the OCC's
By-Laws and Form 19b-4**

In 2002, the OCC amended its By-Laws so that it could provide clearing services to new options exchanges without having those exchanges become shareholders of the OCC.¹⁶ In so doing, the OCC created a new category of non-shareholder exchange participants. To ensure fair representation in the OCC's affairs by the non-shareholder exchanges and to address concerns that the non-shareholder exchange participants could be disadvantaged vis-à-vis the exchange shareholder participants, the Commission required the OCC to insert requirements into its By-Laws to ensure that non-shareholder exchange participants "will be entitled under that [By-Laws] provision to 'fair representation . . . in the selection of [OCC's] directors *and administration of its affairs.*'"¹⁷ In connection with the adoption of these changes, the OCC made the following additional representations to the SEC:

OCC has represented to the Commission that OCC management will (1) provide non-equity exchanges with the opportunity to make presentations to the OCC board or the appropriate board committee upon request and (2) will promptly pass on to non-equity exchanges any information that management considers to be of competitive significance to such exchanges disclosed to exchange directors at or in connection with any meeting or action of the OCC board or any board committee. Letter from William H. Navin, Executive Vice President, General Counsel, and Secretary, OCC (July 8, 2002).¹⁸

Ultimately, the OCC adopted the following language as Interpretation and Policy .01 to Article VIIB of its By-Laws¹⁹:

¹⁶ See 2002 By-Laws Amendment Order, *supra* note 5.

¹⁷ See 2002 By-Laws Amendment Order, *supra* note 5, at 58094 (emphasis added).

¹⁸ *Id.*

¹⁹ OCC By-Laws, available at http://www.theocc.com/components/docs/legal/rules_and_bylaws/occ_bylaws.pdf

.01 Non-Equity Exchanges will be promptly provided with information that the Executive Chairman considers to be of competitive significance to such Non-Equity Exchanges that was disclosed to Exchange Directors at or in connection with any meeting or action of the Board of Directors or any Committee of the Board of Directors.

As previously stated, the proposed Capital Plan creates an undue competitive burden on the Petitioners' ability to compete with the shareholder exchanges because the proposed Capital Plan allows the shareholder exchanges to extract an excessive subsidy from the OCC at the expense of both the non-shareholder exchanges and the industry at-large. This excessive subsidy will be used to subsidize the shareholder exchanges' provision of execution services, which in turn provides the shareholder exchanges with a significant and unfair competitive advantage over the Petitioners. It was precisely these types of potential competitive concerns that led to the adoption of the above-referenced By-Laws provisions and the explicit representations the OCC made to the Commission regarding disclosure of information to Petitioners and their opportunity to be heard.

However, in developing the proposed Capital Plan, the OCC failed to comply with either the By-Laws provisions or the explicit representations it made to the Commission in July 2002. In particular, although the proposed Capital Plan is indisputably a matter of competitive significance to the Petitioners, the OCC failed to inform Petitioners – “promptly” or otherwise – that the proposed Capital Plan was under consideration by the OCC. Petitioners were thus not given an opportunity to exercise their rights to request to make presentations regarding the matter to the Board or to the appropriate committee of the Board. By virtue of being denied the information to which they were entitled, Petitioners were unable to exercise their rights at all, let alone in a timely fashion, before the Board approved the Capital Plan.

In approving the Capital Plan pursuant to delegated authority, the staff summarily rejected Petitioners' arguments in this regard, stating nothing more than that the "OCC represents that OCC and its Board of Directors have conducted its business in conformity with applicable state laws and its own By-Laws" and that "[t]he Commission has no basis to dispute OCC's position on this matter."²⁰ Accordingly, the Commission staff simply accepted the OCC's false representation that it had complied with its By-Laws without regard to the record that had been developed by the Petitioners comment letters demonstrating that the OCC did not comply with these important By-Laws provisions.

Since the initiation of this petition process, the OCC has conceded that it failed to notify the Petitioners about the Capital Plan prior to bringing it to a Board vote.²¹ The OCC defended its failure to notify the proposed Petitioners by stating that it did not believe the proposed Capital Plan had any material competitive consequence on the Petitioners. Such a view is unsustainable because, as described in detail above, excessive subsidies paid to the shareholder exchanges under the proposed Capital Plan would create an undue burden on the Petitioners' ability to compete with the shareholder exchanges. It defies all logic and common sense to conclude that the payment to the exclusive group of shareholder exchanges of an excessive dividend – one not commensurate with the risk assumed in their capital investment – in perpetuity, and funded by the clearing of options transactions across the industry, regardless of whether those transactions occurred on an OCC shareholder exchange or Petitioners' exchanges, would not be a matter of competitive significance to the Petitioners. And, in fact, in approving the Capital Plan pursuant to delegated authority Commission staff acknowledged the competitive significance to the

²⁰ See Order, *supra* note 1, at 13068.

²¹ See OCC Motion to Lift Stay and Brief in Support of Motion to Lift Stay, dated April 2, 2015.

Petitioners. Accordingly, the Petitioners submit that the OCC failed to comply with its By-Laws and the requirements of Form 19b-4. As such, the Commission must reject the proposed Capital Plan.

Moreover, the Board process was tainted by conflicts of interest in violation of the OCC's Charter and Code of Conduct. In particular, none of the five directors representing the shareholder exchanges recused themselves from either the deliberations or the vote, despite the obvious conflict of interest associated with their financial interest in the outcome. Pursuant to Article V of the OCC's Charter, "[e]ach Director is required to act in good faith in the best interests of OCC and with due regard to the fiduciary responsibilities owed to OCC as a business and systemically important financial market utility. In addition, each Director is required to comply with the provisions of the Code of Conduct for OCC Directors, including, without limitation, the provisions relating to conflicts of interest and confidentiality."²² While the actual Code of Conduct is not publicly available, the OCC does publish its Corporate Governance Principles, which summarize the relevant portions of the Code of Conduct as follows:

The Board has adopted a Code of Conduct for OCC Directors that includes a Conflict of Interest Policy. The Conflict of Interest Policy incorporates various provisions of applicable corporate law and other standards adopted by OCC to ensure that Board and committee decisions are not impacted by conflicts of interest. Directors are expected to avoid any action, position or interest that conflicts with an interest of OCC, or gives the appearance of a conflict, in accordance with the Conflict of Interest Policy. OCC annually solicits information from directors in order to monitor potential conflicts of interest and directors are expected to be mindful of their fiduciary obligations to OCC as set forth in the Code of Conduct.²³

²² OCC Charter, available at: http://www.optionsclearing.com/components/docs/about/corporate-information/board_of_directors_charter.pdf.

²³ OCC Board of Directors Corporate Governance Principles, available at http://www.theocc.com/components/docs/about/corporate-information/board_corporate_governance_principles.pdf.

In the present case, each of the five shareholder exchange directors acting on behalf of the shareholder exchanges had a direct and significant interest in the outcome of the Board's consideration of the Capital Plan that was in conflict with the OCC. That is, each shareholder exchange had an interest in extracting the highest rate of return from the OCC in exchange for their capital investment. Yet, none of these directors recused themselves from the deliberations or the vote, which unalterably tainted the governance process.

In addition, the Board failed to maintain the requisite number of public directors on its Board as required by the OCC's By-Laws, which could have impacted both the quality of the deliberations on the matter as well as the outcome of the Board vote. By failing to maintain the requisite number of public directors on the Board while this matter was deliberated and voted on, the process was deprived of key input from disinterested directors who would be most likely to argue for an outcome that is objectively in the best interest of the OCC and the options industry. In addition, with respect to the three public directors who did participate in the deliberations and vote, the record is unclear with respect to what they did to ensure that the proposed Capital Plan was fair and appropriately in the interests of the OCC. In light of the OCC's position as an SRO and a monopoly, the role of public directors takes on acute importance, particularly as it relates to ensuring the SRO does not act in an anticompetitive fashion as the OCC has here. The Commission has previously recognized the importance of public directors in this regard, stating the following in connection with the NASDAQ's application to become a registered national securities exchange:

[P]ublic representatives help to ensure that no single group of market participants has the ability to systematically disadvantage other market participants through the exchange governance process. The Commission believes that public directors can provide unique, unbiased perspectives, which should enhance the ability of the

Exchange Board to address issues in a non-discriminatory fashion and foster the integrity of the Nasdaq Exchange.²⁴

Petitioners are not arguing that every board action that precedes an SRO rule filing must be scrutinized by the Commission prior to Commission action. However, where, as here, the record contains representations from parties in a position to have actual knowledge of governance failures associated with a rule filing, Petitioners believe it is incumbent on the Commission to conduct a reasonable level of inquiry to satisfy itself on the question of the appropriateness of the board governance. Based on the available record, it does not appear the staff conducted such inquiry in approving the Capital Plan pursuant to delegated authority.

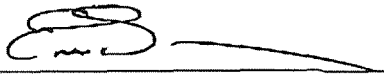
Conclusion

The proposed Capital Plan reflects an unprecedented attempt by four shareholder exchange groups to monetize an industry utility monopoly to their exclusive benefit. Because of the unique nature of the OCC, including its monopoly status, and discriminatory governance that favors the shareholder exchanges, the resulting impact of this effort is to significantly undermine competition among the various options exchanges and ultimately impose excessive costs on clearing firms and investors. The detrimental impact of the proposed Capital Plan on the U.S. options markets cannot be overstated, and the staff made numerous errors of fact and law in approving it. For these reasons, the Petitioners respectfully request that the Commission reject the proposed Capital Plan.

²⁴ *In the Matter of the Application of The Nasdaq Stock Market LLC for Registration as a National Securities Exchange*, Exchange Act Release No. 34-53128; File No. 10-131 (January 13, 2006).

DATED: October 7, 2015

Respectfully Submitted,



Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.
8050 Marshall Ave, Suite 120
Lenexa, KS 66214


Lisa J. Fall
President
BOX Options Exchange LLC
101 Arch Street, Suite 610
Boston, MA 02110

Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC
7 Roszel Road, Suite 5-A
Princeton, NJ 08540

DATED: October 7, 2015

Respectfully Submitted,

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.
8050 Marshall Ave, Suite 120
Lenexa, KS 66214



Lisa J. Fall
President
BOX Options Exchange LLC
101 Arch Street, Suite 610
Boston, MA 02110


Barbara J. Comfy
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC
7 Roszel Road, Suite 5-A
Princeton, NJ 08540

DATED: October 7, 2015

Respectfully Submitted,

Eric Swanson
General Counsel and Secretary
BATS Global Markets, Inc.
8050 Marshall Ave, Suite 120
Lenexa, KS 66214

Lisa J. Fall
President
BOX Options Exchange LLC
101 Arch Street, Suite 610
Boston, MA 02110



Barbara J. Comly
Executive Vice President, General Counsel and Corporate Secretary
Miami International Securities Exchange, LLC
7 Roszel Road, Suite 5-A
Princeton, NJ 08540