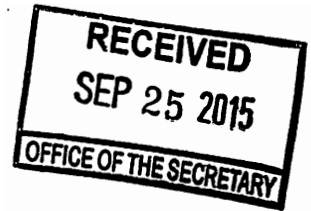


**MURPHY &  
McGONIGLE**  
A Professional Corporation



September 25, 2015

**VIA COURIER AND FAX**

Mr. Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549-1090

Re: Susquehanna International Group, LLP *et al.* Memorandum in Further Support of  
Motion to Reinstitute Automatic Stay

Dear Mr. Fields:

Petitioners BATS Global Markets, Inc., BOX Options Exchange LLC, KCG Holdings, Inc., Miami International Securities Exchange Group, and Susquehanna International Group, LLP and its affiliated and related entities, (collectively "Petitioners"), hereby file the enclosed Memorandum in Further Support of Motion to Reinstitute Automatic Stay. The original and three copies are enclosed.

The enclosed Memorandum in Further Support of Motion to Reinstitute Automatic Stay has been served by facsimile on each party of the proceeding in accordance with 17 C.F.R. § 201.150, and as reflected in the Certificate of Service attached.

Very truly yours,

A handwritten signature in black ink, appearing to read "J. Lombard".

Joseph C. Lombard  
*Counsel for Susquehanna International  
Group, LLP*

Enclosures

cc: Division of Trading and Markets (*by facsimile, w/ encl.*)  
Petitioners and OCC (*by facsimile, w/ encl.*)



**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	)	
KCG Holdings, Inc.	)	
Miami International Securities Exchange, LLC and	)	
Susquehanna International Group, LLP	)	
	)	

**MEMORANDUM IN FURTHER SUPPORT  
OF MOTION TO REINSTITUTE AUTOMATIC STAY**

Petitioners BATS Global Markets, Inc., BOX Options Exchange LLC, KCG Holdings, Inc., Miami International Securities Exchange, LLC, and Susquehanna International Group, LLP and its affiliated and related entities, (collectively “Petitioners”) respectfully submit this reply in further support of their motion to reinstitute the automatic stay provided for by Rule 431(e) of the Rules of Practice. The stay should be reinstated to preserve the status quo pending the Commission’s review of the Division of Trading and Markets’ March 6, 2015 order (the “Approval Order”) approving, pursuant to delegated authority, a capital plan (the “Plan”) proposed by the Options Clearing Corporation (“OCC”).<sup>1</sup>

**INTRODUCTION**

If the present motion is not granted and OCC is free to implement its Plan during the pendency of the Commission’s review, the result will be serious and irrevocable damage to the

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

industry and public. It is telling in this regard that not a single commenter supported adopting the proposed Plan.

The Commission has already determined that the proposed Plan presents important issues warranting review of the Approval Order. The Commission granted that review after Petitioners objected that (1) the Plan is the product of an obvious conflict of interest that will produce an exorbitant annual return of 17-30% to the five exchanges that control OCC in return for what is essentially a risk-free investment; (2) this exorbitant return will cause options clearing costs to increase significantly over the already dramatic increases initiated in April 2014, the unnecessary and inappropriate burden of which will be paid by the investing public and options trading and clearing firms, but not by the five exchanges that control OCC; and (3) the Plan is in reality a scheme on the part of the five owner exchanges to monetize the monopoly and SRO status of the OCC, effectuated through a closed and anti-competitive process, including a veto (or threatened veto) by the exchanges controlling OCC of more favorable financing proposals.

OCC opposes the instant motion by asserting that it is a needless waste of the Commission's time, and the Commission should simply accept without scrutiny OCC's conclusory assertions that it needs immediate capital. But moving forward with the Plan at this juncture will cement the conflicted, sweetheart financial arrangement enriching the five owner exchanges that control OCC – at the expense of industry participants and the investing public. Indeed, in their moving brief, Petitioners presented undisputed financial data demonstrating that OCC is already close to reaching the very capital levels the Plan was designed to achieve. In light of the perverse and self-serving incentives of the OCC exchange owners, the injury to investors and market participants, and the financial data that Petitioners offered, the Commission should not credit OCC's vague, conclusory assertions concerning its need to implement the Plan

now, and should reinstitute the automatic stay while the Commission completes its review of the Plan.

Finally, OCC fails to even address Petitioners' argument that, once the Plan is implemented, it will be extremely impracticable to reverse, resulting in a *fait accompli* for the industry and investors. Indeed, implementing the Plan would result in increased costs to the public that cannot be reversed. Specifically, under the Plan, OCC will needlessly assume costs that do not currently exist – the need to set aside revenues to pay an excessively high dividend to its stockholder exchanges together with the associated tax liabilities. These funds will come at the expense of the clearing members and their customers and encourage wasteful budget expenditures – because the Plan perversely entails that bigger OCC budgets translate into bigger dividend payments to the stockholder exchanges. To offset these costs, market makers will be forced to maintain wider spreads, thereby increasing the trading costs borne by the investing public. These costs cannot be recouped, even if the Commission ultimately reverses the Approval Order. The burden of these added costs will not fall on OCC's owner exchanges who will instead reap a windfall profit in the form of an annual dividend check.

In short, given OCC's current adequate capital position and the significant, irreversible damage to the investing public that will occur when OCC begins to implement the Plan, the automatic stay should be reinstated during the relatively short review period to allow the Commission to conduct the full review of the Approval Order that the Exchange Act requires.

### **ARGUMENT**

#### **I. The Petitioners' Motion is Procedurally Proper**

OCC attempts to sidestep the merits of Petitioners' motion by arguing that it is procedurally improper. Specifically, OCC urges the Commission to disregard the motion

because “Petitioners point to no authority in the Commission’s Rules of Practice or precedent in support of their position that an ‘automatic’ stay that has been lifted may be reinstated.”<sup>2</sup> But this motion is necessary only because the Commission granted OCC’s motion to lift the automatic stay, which itself was not a motion expressly authorized by the Rules of Practice. In fact, both the Petitioners’ current motion and OCC’s motion to lift the stay were filed “pursuant to Rule 154 of the Rules of Practice,” the rule providing generally for filing of motions. OCC cannot have it both ways. It cannot argue that it was proper for the Commission to grant its motion to lift the automatic stay, but it is improper for the Commission to even consider Petitioners’ motion to reinstitute that same stay.

OCC also erroneously argues that the Petitioners’ motion is procedurally improper because it “provides nothing new that is material” and is “merely repetitive” of arguments Petitioners already advanced.<sup>3</sup> In support, OCC states that the Standard & Poor’s report that Petitioners cite in their moving brief is based on information that predates OCC’s motion to lift the stay. But OCC does not dispute that the report itself was not issued until May 20, 2015, *after* OCC’s motion to lift the automatic stay was fully briefed. Accordingly, at the time of OCC’s motion, neither the Petitioners nor the Commission had the benefit of the report’s conclusions – issued by a reputable, independent third-party – that support Petitioners’ position that OCC’s capital target is inflated in light of OCC’s “excellent business risk profile,” “exceptional” liquidity position, and “**minimal financial risk**”<sup>4</sup> even before the infusion of any capital pursuant to the proposed Plan. OCC does not aver that its fiscal circumstances diminished at all

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<sup>2</sup> OCC Opp. at 5.

<sup>3</sup> *Id.* at 6.

<sup>4</sup> Standard & Poor’s Rating Services, Ratings Direct, Options Clearing Corp., May 20, 2015, at pp. 3,4, 7, available at [http://www.optionsclearing.com/components/docs/about/sp\\_rating.pdf](http://www.optionsclearing.com/components/docs/about/sp_rating.pdf).

by the time the report was published. Moreover, OCC does not dispute that in deciding whether to reinstitute the automatic stay, the Commission should consider OCC's *current* capital position, which has significantly improved in the six months since OCC filed its motion to lift the stay.

Finally, OCC also argues that Petitioners' motion "only acts to create a distraction and thereby delay the Commission's review of the Approval Order."<sup>5</sup> But OCC ignores the Commission's September 10, 2015 Order granting the Petitions for Review, which allows statements in support or opposition to the Approval Order to be submitted until October 7, 2015, well after the briefing on this motion will be complete. There will thus be no "delay" of the review, nor does OCC plausibly explain how as a result of this motion, the Commission will be "distracted" from considering the merits of the Approval Order.

## **II. OCC'S Current Capital Level is Already Sufficiently Strengthened Without Implementing the Capital Plan Pending the Commission's Full Review**

OCC next attempts to challenge Petitioners' assertion that OCC will have sufficient capital to essentially achieve its capital target by year-end without implementing the Plan. In doing so, OCC simply states that "OCC's adjusted shareholders' equity would be \$149,613,874" as of August 31, 2015,<sup>6</sup> apparently omitting the \$33.3 million of accrued but unpaid rebates for 2014 and any accrued but unpaid rebates for 2015 that are accounted for on the "Refundable clearing fees" line of OCC's balance sheet.<sup>7</sup> At best, OCC's omission of the rebates as available capital – without making that clear in its opposition – is disingenuous; at worst, it is an

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<sup>5</sup> OCC Opp. at 5.

<sup>6</sup> OCC Opp. at 11.

<sup>7</sup> OCC's Statements of Income and Comprehensive Income in its 2014 Annual Report supports this conclusion, as OCC determined its shareholders' equity after deducting "refundable clearing fees" from its clearing fee revenue, with a mere footnote reference to the source of the associated declared current liability on the balance sheet. See OCC 2014 Annual Report, at 24-25, 33, available at [http://www.optionsclearing.com/components/docs/about/annual-reports/occ\\_2014\\_annual\\_report.pdf](http://www.optionsclearing.com/components/docs/about/annual-reports/occ_2014_annual_report.pdf) (listing \$97 million in shareholders' equity and \$33 million in "refundable clearing fees" as a liability).

intentional attempt to obfuscate its financial wherewithal in an effort to mislead the Commission into believing that it needs immediate capital.<sup>8</sup> In any event, if the unpaid rebates are included in available capital (as they should be), by year-end 2015, OCC will have more than \$230 million of available capital, essentially reaching its inflated capital target level without implementing the Plan. Further, OCC will have reached its target capital level in just several months through higher fees and suspended rebates rather than the “several years” OCC claimed in its original January 26, 2015 filing.

During 2014, OCC’s shareholders’ equity grew by \$72 million (from \$25 million as of December 31, 2013 to \$97 million as of December 31, 2014). The growth is primarily the result of OCC’s 60%-70% fee increase effective as of April 1, 2014. In addition, although OCC’s motion fails to disclose this important fact, OCC’s capital increased by an additional \$33.3 million, which are the funds that it set aside in 2014 for fee rebates to clearing firms. Essentially, OCC’s available capital increased by approximately \$105 million in 2014. OCC’s volume and budget projections for 2015 have not materially changed since 2014, and its fee increase remains in effect. Accordingly, as the 60%-70% fee increase for 2014 was only in place for nine months, it is reasonable to expect that OCC’s 2015 financial performance will be greater than its 2014 performance (*i.e.*, conservatively speaking, shareholders’ equity will grow by at least another \$72 million to \$169 million, and OCC will be able to set aside at least another \$33.3 million for rebates (which will be reflected in the “Refundable clearing fees” line item of its financial statement rather than Shareholders’ Equity) – for a total of \$66.6 million in rebates for 2014 and 2015). Moreover, if the accrued and unpaid rebates are instead used by OCC as capital if the

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<sup>8</sup> Conservatively assuming that rebates for 2015 will also total \$33.3 million (with \$22.2 million accrued as of August 31, 2015), OCC in effect concedes that it had \$204.5 million in available capital as of August 31, 2015 (\$149 million admitted shareholder s’ equity plus \$55.5 million in accrued rebates).

stay is reinstated, OCC would have at least \$235.6 million (\$169 million plus \$66.6 million) in capital at year-end. Stated another way, simply by relying on fees and without implementing the Plan and subjecting OCC to dividend and associated tax obligations into perpetuity, OCC will achieve its (inflated) \$247 million target capital requirement in a matter of months, rather than OCC's claimed years.

OCC argues that "Petitioners engage in pure speculation" by providing an "estimate", without any basis, that OCC's capital will grow to 'nearly \$250 million' by the end of 2015." To the contrary, Petitioners rely on hard financial data, such as OCC's 2014 Annual Report, in estimating OCC's capital level as of year-end 2015.<sup>9</sup> OCC does not dispute any of the financial data on which Petitioners rely, nor challenge Petitioners' assertion that "OCC's 2015 volume and budget projections have not materially changed from 2014."<sup>10</sup> To that end, if nothing has changed materially in OCC's business from 2014 to 2015, it follows that OCC will perform substantially the same (or better) in 2015, resulting in OCC essentially reaching its capital target by year-end. OCC's true capital position may be even stronger, but we do not know because OCC has not disclosed the relevant data.

OCC also argues that "Petitioners completely ignore" the separate \$117 million in "Replenishment Capital" provided for by the Plan, which OCC asserts increases its target capital from \$247 million to \$364 million. OCC is wrong and disingenuous. Its own rule filing clearly and repeatedly identifies its Target Capital Requirement as \$247 million. Moreover, Petitioners

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<sup>9</sup> An estimate was necessary because OCC has failed to provide any current, meaningful financial information. It is concerning that OCC has not provided more transparency into its financial claims and has instead selectively proffered narrow data points in a manner that hinders the questioning of its self-serving characterizations. Given its monopoly status, there is no competitive reason for OCC not to provide comprehensive year-to-date financial statements as evidence of its financial position. Indeed, its very claim for a \$247 million capital requirement is purportedly based on an undisclosed report of an unnamed consultant. OCC has provided no substantiation for this bald claim of such grand proportions.

<sup>10</sup> Petitioners' Br. at 4.



argued that “during the anticipated period of the Commission’s review of the Plan, there is no reasonably foreseeable scenario in which OCC’s (estimated) more than \$200 million of capital will be dissipated at a rate that will require OCC to issue a capital call.”<sup>11</sup> This is especially true considering that OCC’s current capital is eight times OCC’s historic levels, which was more than sufficient during the country’s worst financial crisis since the Great Depression, and the issue here is operating expenses (rent, salaries, etc.), not trading or clearing risk. OCC provides no plausible scenario, particularly given its current capital levels, under which the Replenishment Capital will be required during the pendency of the Commission’s review.<sup>12</sup> And while OCC repeatedly refers to the need to protect against “unexpected market developments” (presumably much worse than the 2008 financial crisis), OCC itself concedes that any such developments are “unlikely” and would occur “only as a result of a significant, unexpected event.”<sup>13</sup> The Replenishment Capital commitment’s predominant purpose is window dressing to sweeten the return of the owner exchanges.

Finally, OCC disputes Petitioners’ argument that OCC is exchanging “cost-free” capital for capital on which it will have to pay dividends at a usurious rate, effectively weakening OCC’s capital position and undermining the Commission’s stated “compelling public interest” to

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<sup>11</sup> Petitioners’ Br. at 5, n. 4.

<sup>12</sup> Moreover, contrary to the “comprehensive process” OCC asserts took place to determine its capital target, OCC provides no support for its purported need for an additional \$117 million in Replenishment Capital, nor is any contained in the Commission’s Notice of No Objection. *See* Securities Exchange Act Release No. 74387, 80 FR 12215 (Mar. 6, 2015) (SR-OCC-2014-813). Despite OCC’s apparent attempt to infuse the “no objection” notice with significance, it is not relevant to the current proceeding. Advance Notice filings by clearing agencies pursuant to Rule 19b-4(n) deal exclusively with “the level of risks presented by a designated clearing agency” and do not require findings on the issues that are currently before the Commission on this motion. Specifically, in conjunction with the Notice of No Objection, the Commission found only that the proposal was consistent with Section 805 of the Payment, Clearing and Settlement Supervision Act and provided no guidance on whether the proposal was consistent with the requirements of the Exchange Act.

<sup>13</sup> 80 FR at 12219.

strengthen OCC's capitalization. OCC argues that the current capital "is not cost free, as it is being borne by OCC's clearing members and the trading public, who will be relieved of this burden when OCC ... redistribute[s] capital" under the Plan.<sup>14</sup> However, this response side-steps the point that OCC's current capital base is free to OCC – the systemically important entity whose financial security is the premise for the proposed Plan. It also ignores that the Plan cuts into clearing members' rebates, which increases clearing costs that will likely be passed on to the investing public. Indeed, OCC's Plan received no commentary support from any of the clearing members who would purportedly benefit from the Plan. Any short-term benefit would be more than offset by the Plan's long-term cost that will ultimately result in increased fees, negative market impact, and competitive imbalance among the exchanges.

In short, allowing OCC to implement the Plan now undermines the Commission's goal of "strengthening the capitalization" of the OCC. Indeed, OCC's current capital position will be weakened by implementing the Plan, given that the Plan allows OCC to (i) refund tens of millions of dollars as rebates that it could otherwise use as available capital; (ii) exchange cost-free capital for capital on which it will have to pay tens of millions of dollars in perpetuity in annual dividends to the exchange owners; and (iii) pay significant taxes on the income required to pay those dividends.

### **III. It Would be Extremely Impracticable to Reverse the Plan Once Implemented**

Petitioners demonstrated in their moving brief that it would be "extremely impracticable" to reverse the Plan once OCC implements it. Among other things, the logistical issues would include: (1) reversing and reclaiming dividends paid to the Exchange Owners; (2) resolving issues associated with taxes paid on those dividends; (3) clawing back rebates from clearing

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<sup>14</sup> OCC Opp. at 13.

members that OCC stated it would pay if the stay were lifted – leading those members to impose additional costs on the investing public to offset the loss of the rebates; and (4) reversing fee decreases that OCC stated it would implement if the stay were lifted. The third point is particularly important because there is **no** means by which the additional costs imposed on the investing public, in the form of wider spreads and increased trading costs, can be recouped, even if the Commission ultimately reverses the Approval Order. OCC does not dispute any of these points. Nor does OCC refute Petitioners' assertion that it will now aggressively move forward to implement the Plan, resulting in a *fait accompli* for the industry and investors before the Commission conducts the meaningful review that the Exchange Act requires.<sup>15</sup> The Commission can avoid these difficult issues, including potentially significant and irreversible costs that will be borne by the investing public, simply by reinstating the automatic stay provided for by the Rules for the relatively short time period during which the Commission conducts the review that it has deemed necessary.

### **CONCLUSION**

For all the foregoing reasons, Petitioners request that the Commission reinstate the automatic stay pending resolution of the Commission's review of the Approval Order.

Respectfully submitted,

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<sup>15</sup> OCC's prior actions demonstrate the likelihood that it would move forward during the Commission's review to implement the Plan. Indeed, in March 2015, OCC exploited the brief (several-day) delay in the operation of the automatic stay to rush to begin implanting the Plan despite the uniform opposition thereto and the strong likelihood of the impending stay. SIG Opp. to Motion to Lift Stay (April 9, 2015) at 4.

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Dated: September 25, 2015

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