

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-72331; File No. SR-OCC-2014-13)

June 5, 2014

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Provide for the Calculation of Initial Margin Requirements for Segregated Futures Accounts Through the Use of the Standard Portfolio Analysis of Risk Margin Calculation System

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> notice is hereby given that on May 28, 2014, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by OCC. OCC filed the proposed rule change pursuant to Section 19(b)(3)(A)<sup>3</sup> of the Act and Rule 19b-4(f)(6)<sup>4</sup> thereunder.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

This proposed rule change by The Options Clearing Corporation (“OCC”) would provide for the calculation of initial margin requirements for segregated futures accounts through the use of the Standard Portfolio Analysis of Risk (“SPAN”) margin calculation

---

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

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

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(6). As required under Rule 19b-4(f)(6)(iii), OCC provided the Commission with written notice of its intent to file the proposed rule change, along with a brief description and the text of the proposed rule change, at least five business days prior to the date of filing the proposed rule change, or such shorter time as designated by the Commission.

system in place of OCC's System for Theoretical Analysis and Numerical Simulations ("STANS") margin calculation system.

II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. OCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.

(A) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

OCC is proposing to modify its rules to provide for the calculation of margin requirements for segregated futures accounts through the use of the SPAN margin calculation system in place of OCC's STANS margin calculation system, subject to OCC's collection of enhanced margin to be deposited in the segregated futures account in the event that the margin requirement as calculated under STANS would exceed the requirement calculated under SPAN.

**Compliance with CFTC Rule 39.13(g)(8)**

On April 25, 2012, and November 2, 2012, OCC implemented Rule 602(a) and Rule 601(c), respectively, in compliance with Commodity Futures Trading Commission ("CFTC") Rule 39.13(g)(8),<sup>5</sup> which, in relevant part, requires registered derivatives clearing organizations ("DCOs") such as OCC to (i) collect initial margin for customer

---

<sup>5</sup> 17 CFR 39.13(g)(8).

segregated futures accounts on a gross basis and (ii) have rules requiring clearing members to collect initial margin from their customers in an amount that is greater than the amount the DCO collects from clearing members.<sup>6</sup> Together, Rules 601(c) and 602(a) resulted in customer level margin requirements for segregated futures accounts that are calculated by clearing members using SPAN, but subject to a “floor” established by the clearing level margin requirements calculated by OCC using STANS.

### **Use of STANS Inputs in Calculation of Customer Level Margin Requirements**

In addition to implementing the above described changes to its systems to margin segregated futures accounts on a gross basis, OCC sought to bring customer level margin requirements into conformity with STANS risk parameters by changing the initial risk parameter inputs for particular cleared contracts in segregated futures accounts.<sup>7</sup>

Previously, OCC used SPAN risk parameters received from the futures exchange listing a particular cleared contract when preparing theoretical output files that clearing members used in SPAN calculations to calculate customer margin requirements.<sup>8</sup> In order to more closely align clearing level and customer level margin requirements, OCC replaced the SPAN risk parameters with STANS risk parameters in preparing these theoretical output files.<sup>9</sup> This alignment of clearing level and customer level margin requirements through

---

<sup>6</sup> See Securities Exchange Act Release No. 66841 (April 20, 2012), 77 FR 24999 (April 26, 2012) (SR-OCC-2012-06) and Securities Exchange Act Release No. 68148 (November 2, 2012), 77 FR 67036 (November 8, 2012) (SR-OCC-2012-17).

<sup>7</sup> *Id.*

<sup>8</sup> Securities Exchange Act Release No. 68148 (November 2, 2012), 77 FR 67036 (November 8, 2012) (SR-OCC-2012-17).

<sup>9</sup> *Id.*

the use of STANS risk parameters resulted in customers of clearing members being directly exposed to margin requirements based on STANS for the first time.

STANS is a data driven system using market data to model risk correlations and distributions in order to calculate appropriate margin coverage for each cleared contract. STANS was designed to have risk parameters adjusted on a monthly basis, when new data is made available, and on a daily basis, to take into account changes in market volatility. OCC believes that these frequent recalibrations are critical to its risk management capabilities with respect to clearing member accounts. However, as a result of the changes to OCC's rules described above, these recalibrations result in frequent changes to the margin requirements applicable to customers of clearing members. Clearing members are well capitalized entities with significant access to financing and are able to absorb frequent changes to margin requirements caused by STANS risk parameter recalibration.<sup>10</sup> However, certain customers of clearing members may not have the same capital requirements or access to financing as clearing members, and frequent changes to their margin requirements are more disruptive, causing uncertainty and adding unforeseen financing costs to their operations.<sup>11</sup>

---

<sup>10</sup> OCC's By-Laws and Rules require clearing members to maintain minimum net capital of \$2 million. *See*, OCC By-Laws, Article V, Section 1, Interpretation and Policy .01, OCC Rule 301 and OCC Rule 302. Notwithstanding the minimum net capital requirement, most OCC clearing members maintain net capital (and margin) in excess of the minimum and are able to readily satisfy margin increases that may occur from day-to-day.

<sup>11</sup> Clearing members' customers include individual retail customers who do not have the same financial resources as clearing members and, unlike clearing members, will not be able to easily satisfy margin increases that occur from day-to-day.

## **SPAN System for Calculating Initial Margin**

SPAN is used universally by all the major domestic futures clearing houses, other than OCC, to calculate clearing and customer level margin requirements, as well as by the major domestic futures exchanges. SPAN is a market simulation-based methodology that calculates initial margin requirements for a wide variety of financial instruments including futures, options, physical commodities, equities, or any combination of these instruments. SPAN assesses the risk of a portfolio by calculating the maximum likely loss that could be suffered by the portfolio based on SPAN risk parameters set by an exchange or DCO. These risk parameters, known as “scan ranges,” include ranges of prices, volatility and other variables. Using these scan ranges, SPAN simulates a certain number of market scenarios, known as “risk scenarios,” as determined by the exchange or DCO, and calculates a “SPAN risk array,” which is a set of numerical values that indicate how a particular contract is expected to gain or lose value under the various risk scenarios. The risk array representing the maximum likely loss to a portfolio is then used to set margin requirements by the exchange or DCO.

## **Proposed By-Law and Rule Changes**

OCC proposes to amend Rule 601 by adding new paragraph (1) to Rule 601(e) to provide for the calculation of initial margin for segregated futures customer accounts pursuant to SPAN.<sup>12</sup> Proposed Rule 601(e)(1) will retain the requirement that initial margin for segregated futures accounts be calculated on a gross basis, but will calculate the initial margin requirement pursuant to the SPAN methodology in order to reduce the

---

<sup>12</sup> OCC has previous experience operating OCC’s Theoretical Intermarket Margining System (TIMS), a margin calculation system that similar to SPAN, and does not anticipate any operational issues in implementing SPAN.

disruption experienced by customers of clearing members due to the frequent recalibration of STANS risk parameters. OCC believes this change will provide market participants with greater certainty regarding the funding costs associated with their futures positions. Additionally, calculating initial margin requirements for segregated futures accounts pursuant to SPAN will conform OCC's margin calculation methodology for futures and options on futures with the methodology primarily used by other DCOs, futures exchanges and participants in the futures and options on futures markets.

OCC intends to set the SPAN scan ranges for cleared contracts held in segregated futures accounts based on two years of daily returns that will be analyzed for each tenor of cleared contract. In the event that two years of daily returns are unavailable, OCC will use the model two-year daily returns produced by STANS to set the SPAN scan ranges. Scan ranges will be initially set to provide coverage for a minimum 99% confidence level. OCC intends to use the price history from the futures exchange that lists a particular contract to establish the minimum margin threshold. In the event that a contract is listed by a futures exchange that is economically equivalent to another futures exchange's contract, OCC intends to use the SPAN parameters from the primary market to establish the minimum margin threshold.

OCC will reset minimum SPAN scan ranges on a quarterly basis. Margin rates, including any changes, will be posted on OCC's public website and implemented within five business days of the quarterly rate setting date. This schedule will be provided to all market participants via a posting on OCC's public website. OCC believes these measures will promote transparency and provide clearing members and their futures customers adequate time to prepare for any changes in margin rates.

OCC staff will continuously assess the current SPAN scan ranges by comparing changes in settlement values to the established SPAN scan ranges on a daily basis. If there is a change in settlement values that exceeds the established SPAN scan ranges, OCC will reset the SPAN scan ranges in between the scheduled quarterly reset no later than five business days after the observed change in settlement values that exceeded the established SPAN scan ranges and the revised ranges will be left in place for a minimum of ten business days and, if no further breaches have been observed, OCC will reset the margin rates based on its standard approach. OCC believes that this adjustment process promotes safety and soundness in its risk management practices by implementing an ongoing monitoring process to ensure that margin levels are maintained at appropriate levels.

Proposed Rule 601(e)(1) will apply to all segregated futures accounts, including segregated futures professional accounts, internal non-proprietary cross-margining accounts and non-proprietary cross-margining accounts. For cross-margining accounts with other DCOs, OCC will use the SPAN scan ranges set by the participating DCO. For OCC internal cross-margining accounts, OCC will calculate the SPAN scan ranges as described above.

Although proposed Rule 601(e)(1) proposes to use SPAN to calculate initial margin requirements for segregated futures accounts on a gross basis, OCC believes that margin requirements calculated on a net basis, i.e., permitting offsets between different customers' positions held by a clearing member in a segregated futures account, using STANS affords OCC additional protections at the clearinghouse level against risks associated with liquidating a clearing member's segregated futures account.

Accordingly, OCC proposes in new Interpretation and Policy .07 to Rule 601 to also calculate on a net basis initial margin requirements for each segregated futures accounts using STANS. If at any time OCC staff observes a segregated futures account where initial margin calculated pursuant to STANS on a net basis exceeds the initial margin calculated pursuant to SPAN on a gross basis, OCC will collateralize this risk exposure by applying an enhanced margin requirement in the amount of such difference to the account. Proposed Interpretation and Policy .07 to Rule 601 therefore would ensure that STANS, which produces the best estimate of OCC's liquidation risk, continues to be utilized in connection with the risk management process for segregated futures accounts.

### **Impact of Change**

OCC performed an evaluation of the impact of using SPAN in place of STANS to calculate initial margin requirements for segregated futures accounts and has concluded that the impact will be minimal.<sup>13</sup> For 78 business days between January 15, 2014 and May 7, 2014, OCC used SPAN to calculate initial margin requirements on a gross basis for all 68 segregated futures accounts carried at OCC. The change to initial margin requirements across all individual accounts ranged between an increase of \$557.5 million and a decrease of \$180.4 million. The average individual account increase was \$18.8 million and the average account decrease was \$15.4 million. When reviewing the aggregated daily impact, the change across all accounts ranged between an increase of

---

<sup>13</sup> The only futures products sets that OCC expects to clear following the adoption of SPAN margining will be: Volatility Futures, Variance Futures, Eurodollar Futures and Security Futures. NYSE Liffe U.S. precious metal futures and MSCI broad based index futures products will also be subject to SPAN margining as long as they are cleared by OCC. However, such NYSE Liffe U.S. futures products are scheduled to transfer to another derivatives clearing organization in the second quarter of 2014.



\$390.1 million and a decrease of \$764.7 million. The average aggregate increase across the 50 activity dates when an overall increase in margin was observed was \$150.7 million while the average aggregate on the 28 activity dates when an overall margin decrease was observed was \$267.7 million.

During the above 78 business day period, 29 of the segregated futures accounts would have been subject to the enhanced margin requirement pursuant to proposed Interpretation and Policy .07 to Rule 601 because the initial margin calculated pursuant to STANS on a net basis exceeded the initial margin calculated pursuant to SPAN on a gross basis on at least one activity date.<sup>14</sup> The majority of the days on which the enhanced margin would have been required of a large number of accounts were during the last week of January and the first week of February when emerging markets experienced substantial volatility.

## 2. Statutory Basis

OCC believes the proposed rule change is consistent with Section 17A of the Act,<sup>15</sup> and the rules and regulations thereunder, because the proposed modifications

---

<sup>14</sup> Of these 29 accounts, 18 accounts incurred an enhanced margin charge on fewer than 10 activity dates during the 78 day period, while 6 accounts incurred an enhanced margin charge between 10 and 40 activity dates, and 5 accounts incurred an enhanced margin charge on greater than 40 activity dates. OCC staff noted that accounts incurring the enhanced margin charge on a large number of activity dates are accounts comprised of a small number of positions or positions concentrated in a small number of product types. Specifically, more than half of all observed enhanced margin charges were in accounts comprised of only NYSE Liffe Metals or NYSE Liffe MSCI products. Of the 78 activity dates, on 47 activity dates fewer than 5 accounts incurred an enhanced margin charge, on 26 activity dates between 6 and 10 clearing member accounts incurred an enhanced margin charge, and on 5 activity dates 11 to 15 clearing member accounts incurred an enhanced margin charge.

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

would help ensure that OCC is able to perform clearing services for products that are subject to either the exclusive or joint jurisdiction of the CFTC<sup>16</sup> and is designed to promote “the prompt and accurate clearing and settlement of securities transactions”<sup>17</sup> and will “require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation”<sup>18</sup> in OCC. The proposed rule change would provide greater certainty to clearing members’ customers regarding funding costs associated with their futures positions and align OCC’s margin methodology for segregated futures accounts with other DCOs while allowing OCC to continue to use margin requirements to limit its credit exposures to clearing members under normal market conditions and use risk-based models and parameters to set margin requirements.<sup>19</sup> The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended or any advance notice filings pending with the Commission.

(B) Clearing Agency’s Statement on Burden on Competition

OCC does not believe that the proposed rule change would impose any burden on competition. Changes to the rules of a clearing agency may have an impact on the participants in a clearing agency and their customers and the markets that the clearing agency serves. This proposed rule change primarily affects clearing members and their customers by changing the margin calculation system used to compute initial margin

---

<sup>16</sup> Securities futures are subject to the joint jurisdiction of the Commission and the CFTC.

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

<sup>18</sup> 17 CFR 240.17Ad-22(d)(2).

<sup>19</sup> 17 CFR 240.17Ad-22(b)(2).

requirements for segregated futures accounts from STANS to SPAN. OCC believes that the proposed change would facilitate competition among clearing members, their customers and market participants because the rule change would affect all clearing members with segregated futures accounts equally, and bring OCC's margin system for futures in line with other DCOs. Specifically, all clearing members with segregated futures accounts would be subject to having the initial margin calculation for such accounts computed under SPAN, and all affected customers would be subject to having their customer level margin requirements calculated on the basis of SPAN. With respect to any burden on competition among clearing agencies, OCC is one of several clearing agencies that perform central counterparty services for the futures markets and all such clearing agencies, except for OCC, currently use SPAN to calculate customer level margin requirements. The proposed rule change would not impede other clearing agencies from clearing futures contracts.

For the foregoing reasons, OCC believes that the proposed rule change is in the public interest and would not impose any burden on competition among clearing members, among market participants or among clearing agencies.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments on the proposed rule change were not and are not intended to be solicited with respect to the proposed rule change and none have been received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

- (i) significantly affect the protection of investors and the public interest;

(ii) impose any burden on competition; and

(iii) become operative for 30 days from the day on which it was filed, or

such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(a) of the Act and Rule 19b-4(f)(6) thereunder.<sup>20</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment for (<http://www.sec.gov/rules/sro.shtml>);

or

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-OCC-2014-13 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange

Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-OCC-2014-13. This file number should

---

<sup>20</sup> 17 CFR 240.19b-4(f)(6)(iii). Notwithstanding the foregoing, OCC has represented that implementation of this rule change will be delayed until this rule change is deemed certified under CFTC Regulation §40.6.

be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method of submission. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Section, 100 F Street, N.E., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at [http://www.theocc.com/components/docs/legal/rules\\_and\\_bylaws/sr\\_occ\\_14\\_13.pdf](http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_14_13.pdf). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-OCC-2014-13 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>21</sup>

Kevin M. O'Neill  
Deputy Secretary

---

<sup>21</sup> 17 CFR 200.30-3(a)(12).