

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-78862; File No. SR-OCC-2016-002)

September 16, 2016

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving Proposed Rule Change, as Modified by Amendment No. 1, Concerning Enhancements to The Options Clearing Corporation's Governance Arrangements

On July 15, 2016, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-OCC-2016-002 pursuant to Section 19(b)(1) of the Securities and Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder.<sup>2</sup> The proposed rule change was published in the Federal Register on August 3, 2016.<sup>3</sup> The Commission did not receive any comments on the proposed rule change. On August 24, 2016, OCC filed Amendment No. 1 to the proposed rule change.<sup>4</sup> This order approves the proposed rule change.

I. Description of the Proposed Rule Change

OCC is amending its Certificate of Incorporation, By-Laws, and Board of Directors ("Board") Charter to require that only one Management Director serve on

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

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

<sup>3</sup> Exchange Act Release 78438 (July 28, 2016), 81 FR 51220 (August 3, 2016) (SR-OCC-2016-002).

<sup>4</sup> In Amendment No. 1, OCC revised Item 2 of Form 19b-4 to confirm that holders of all OCC common stock unanimously consented to the amendments to OCC's Certificate of Incorporation and to Article III, Sections 1, 10, 12, and 15 of its By-Laws as approved by OCC's Board at a meeting held on May 4, 2016 and as contained within the proposed rule change. Amendment No. 1 clarified further that changes to OCC's Certificate of Incorporation would not take effect until filed with Delaware Secretary of State. Amendment No. 1 is not subject to notice and comment because it does not materially alter the substance of the proposed rule change or raise any novel regulatory issues.

OCC's Board (as opposed to the current requirement of two Management Directors). Moreover, OCC is proposing to amend its By-Laws and Rules to delete all references to the title and responsibilities of the Management Vice Chairman. In addition, OCC is amending its By-Laws to: (i) provide that the Compensation and Performance Committee ("CPC")<sup>5</sup> and the Audit Committee ("AC") each will be chaired by a Public Director; (ii) modify the composition requirements of the Risk Committee ("RC") to, among other things, provide that an Exchange Director be a member of the Risk Committee; (iii) provide for action by the OCC Board in the nomination process for Member Directors and Public Directors; (iv) eliminate term limits for Public Directors; and (v) consolidate By-Law sections that identify the committees of the Board into a single section of the By-Laws. Finally, OCC is amending the Charters of the Board and the AC, CPC, Governance and Nominating Committee ("GNC"), RC, and Technology Committee ("TC") (collectively, "Board Committees" or "Committees" and each a "Board Committee" or "Committee") that stem from scheduled reviews of such documents.

According to OCC, the amendments to the Board and Committee Charters are designed, in general, to provide more clarity and transparency around the oversight functions and responsibilities of the Board and each of its Committees and provide for a more comprehensive and robust oversight framework for the financial reporting, audit and compliance, compensation and performance, governance and nomination, risk, and technology functions at OCC.

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<sup>5</sup> As described below, the Performance Committee will be renamed the Compensation and Performance Committee.

The amendments to OCC's Certificate of Incorporation, By-Laws, Rules, Board and Committee Charters, and Amended and Restated Stockholders Agreement are described in detail below.

All capitalized terms not defined herein have the same meaning as set forth in the OCC By-Laws and Rules.

**(1) Amendments to OCC's Certificate of Incorporation**

OCC is amending its Certificate of Incorporation to state that the number of Management Directors serving on OCC's Board shall be such number as shall be fixed by or pursuant to OCC's By-Laws.<sup>6</sup> OCC stated that the purpose of this proposed change is ultimately to require that only one Management Director shall serve on OCC's Board. OCC will also amend its By-Laws to state that one Management Director shall serve on OCC's Board (as discussed in more detail below). The amendments will also ensure consistency among all of OCC's governing documents concerning the number of Management Directors on OCC's Board. OCC's Certificate of Incorporation and By-Laws currently state that OCC's Board shall be composed of Members Directors, Exchange Directors, Public Directors, and two Management Directors. Recently,

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<sup>6</sup> The number of Management Directors required to serve on OCC's Board will be stipulated by Article III, Section 1 of OCC's By-Laws. Article XI, Section 1 of OCC's By-Laws states that Article III of the By-Laws may not be amended by action of the Board without the approval of the holders of all of the outstanding Common Stock of the Corporation entitled to vote thereon. Accordingly, any proposed change in the number of Management Directors required to serve on OCC's Board will continue to be subject to stockholder approval.

OCC is also making conforming changes to Article III, Sections 10 (Resignations) and 12 (Filling of Vacancies and Newly Created Directorships) of the By-Laws to reflect that only one Management Director, the Executive Chairman, will be serving on OCC's Board.

however, there has been a vacancy for one Management Director position and only one Management Director is serving on the Board at this time.<sup>7</sup> OCC's Board continually evaluates the leadership structure at OCC, including the appropriate number of Management Directors for OCC's Board, and in light of recent experience since the vacancy of the second Management Director position, believes that amending the Board composition to require only one Management Director on OCC's Board will provide an appropriate level of management representation in the Board-level oversight of OCC. OCC stated that the Executive Chairman, as Management Director, continues to represent management's viewpoint on OCC's Board. Moreover, the Board has access to OCC's management team, which OCC believes ensures that the Board has continued access to management's perspectives on the business and affairs of OCC. Furthermore, OCC notes that, prior to the addition of a second Management Director seat in 2013, OCC has historically had only one Management Director serving on its Board.<sup>8</sup> Accordingly, OCC believes that the proposed amendments would continue to provide for prudent governance arrangements at OCC. OCC is also proposing conforming changes to the Board Charter as described below.

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<sup>7</sup> In 2014, the Commission approved a proposed rule change providing that OCC's President would not be considered a Management Director and, therefore, only one Management Director (the Executive Chairman) currently serves on the Board. See Securities Exchange Act Release No. 73785 (December 8, 2014), 79 FR 73915 (December 12, 2014) (SR-OCC-2014-18).

<sup>8</sup> In 2013, the Commission approved a proposed rule change by OCC to provide for the separation of the powers and duties combined in the office of OCC's Chairman of the Board of Directors into two offices, Chairman and President, and to create an additional directorship to be occupied by the President. See Securities Exchange Act Release No. 70076 (July 30, 2013), 78 FR 47449 (August 5, 2013) (SR-OCC-2013-09).

## **(2) Amendments to OCC's By-Laws and Rules**

### *(a) Number of Management Directors on OCC's Board*

Consistent with the amendments to the Certificate of Incorporation, described above, OCC is amending Article III, Section 1 of its By-Laws to state that only one Management Director will serve on OCC's Board (as opposed to the current requirement of two). As noted above, OCC's Board continually evaluates the leadership structure at OCC, including the appropriate number of Management Directors for OCC's Board, and believes that amending the Board composition to require one Management Director on OCC's Board will continue to provide an appropriate level of management representation in the Board-level oversight of OCC. OCC is also making conforming changes to Article III, Sections 10 (Resignations) and 12 (Filling of Vacancies and Newly Created Directorships) of the By-Laws to reflect that only one Management Director, the Executive Chairman, would be serving on OCC's Board.

### *(b) Elimination of Management Vice Chairman Role*

OCC is amending its By-Laws and Rules to eliminate the role of Management Vice Chairman. The office of Management Vice Chairman has been vacant for a number of years and has not been included in the Board's current discussions regarding management succession planning. During that time, OCC's thought process surrounding leadership roles at OCC has evolved. OCC believes that any of the responsibilities of the Management Vice Chairman have been appropriately handled by other officers of OCC, primarily the Executive Chairman and President (or where applicable, other officers such

as the Secretary or Directors such as the Member Vice Chairman<sup>9</sup>) and as a result, this role is being eliminated from OCC's By-Laws and Rules. OCC believes the amendments will more accurately reflect the current state of affairs regarding the office, ensure consistency across all of OCC's governing documents, and provide more clarity and transparency regarding OCC's intended governance arrangements.

In particular, OCC is amending (i) By-Laws Article I.A.(13); Article II, Section 4; Article III, Section 15; Article IV; Article V, Sections 1 and 3; Article VI, Section 17; Article VIII, Section 5; Article IX, Sections 12 and 14 and (ii) Rules 305, 309, 309A, 505, 609A, 801, 804, 805, 901, 903, 1104, 1106, 1309, 1402, 1405, 1604, 1610, 2104, 2110, and 2408 to remove all references to and responsibilities of the role of Management Vice Chairman.

*(c) Committee Descriptions and Other Conforming By-Law Amendments*

OCC is amending Article III of its By-Laws to provide descriptions of the AC, CPC, GNC, RC, and TC in a single section of the By-Laws. Specifically, OCC is amending its By-Laws to consolidate existing Article III, Section 4 (which concerns the GNC) and existing Article III, Section 9 (which concerns the RC,<sup>10</sup> the TC,<sup>11</sup> and the

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<sup>9</sup> For example, under proposed revisions to Article IV, Section 7, the Member Vice Chairman would preside over Board and stockholder meetings in the absence of the Executive Chairman.

<sup>10</sup> The description of the RC in proposed Article III, Section 4(d) of the By-Laws would reflect changes to OCC's existing policy regarding the composition of the RC in order to conform the By-Law provision to changes recommended as a result of the annual review of the RC Charter (as discussed below). See infra note 15, and related text.

<sup>11</sup> The Commission recently approved a proposed rule change by OCC to adopt a Technology Committee of the Board of Directors. See Securities Exchange Act

Board's ability to designate persons to serve on Committees, generally), into Article III, Section 4 and adding descriptions of the CPC and AC to Article III, Section 4 of its By-Laws in order to provide a more transparent, centralized, and unified statement describing all of the Board Committees.

In addition, OCC will make a non-substantive drafting clarification to existing language being relocated from Article III, Section 9 to the introductory section of Article III, Section 4 to clarify that the Board is required to designate persons to serve on the specifically enumerated Committees therein.

The amended By-Laws description of the AC will reflect existing requirements in the AC and GNC Charters that, on an annual basis, the Board of Directors shall appoint an AC selected from among the directors recommended by the then-constituted GNC after consultation with the Executive Chairman and shall serve at the pleasure of the Board, provided that no Management Director may serve on the AC. The description of the AC will also include a new requirement that the chairman of the AC shall be designated by the Board from among the Public Director member(s) of the Committee (as described further below).

The description of the CPC will reflect the existing requirement that, on an annual basis, the Board of Directors shall appoint a CPC and that the CPC generally consists of the Executive Chairman, the Member Vice Chairman, and at least one Public Director.<sup>12</sup>

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Release No. 77042 (February 3, 2016), 81 FR 6915 (February 9, 2016) (SR-OCC-2015-018).

<sup>12</sup> The description of the CPC in the By-Laws will include the general requirement that CPC shall include the Executive Chairman, the Member Vice Chairman, and at least one Public Director. The description is not intended to change the more specific CPC composition requirements in the CPC Charter that the committee

Consistent with the preceding sentence, all of the CPC members will be selected by the Board from among the directors recommended by the then-constituted GNC after consultation with the Executive Chairman and shall serve at the pleasure of the Board. The description will also include a new requirement that the chairman of the CPC shall be designated by the Board from among the Public Director member(s) of the Committee (as described further below). OCC believes that consolidating the descriptions of all Board Committees into Article III, Section 4 of its By-Laws will provide more clarity and transparency to OCC's participants regarding the existence and composition of such Committees.

OCC is amending Article IV, Section 1 of the By-Laws to provide that the Board will elect the Executive Chairman and Vice Chairman of the Board upon the nomination of the GNC and also elect the President of OCC (in addition to the Secretary and Treasurer). In addition, OCC is amending Article IV, Section 7 to delete a requirement that the Member Vice Chairman preside at the meetings of any Committee of the Board of Directors charged with the responsibility for evaluating the performance and compensation of officers as the CPC will now be chaired by a Public Director. In addition, OCC will make amendments to clarify that the Member Vice Chairman will preside over meetings of the Board and stockholders in the absence of the Executive Chairman because the President cannot preside over meetings of the Board.<sup>13</sup>

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consist of a Public Director Chair, the Executive Chairman, the Member Vice Chairman, and three or more other directors appointed annually by the Board.

<sup>13</sup> See OCC's By-Laws Article IV, Section 8.



*(d) Compensation and Performance Committee and Audit Committee*

*Independence*

In addition to the changes described above, OCC will also change the Board Committee descriptions in proposed Article III, Sections 4(a) and (b) of the By-Laws to reflect the requirement that a Public Director<sup>14</sup> chair the AC and the CPC. The GNC recently performed a review of governance trends and best practices among self-regulatory organizations as they relate to board-level compensation committees.<sup>15</sup> OCC undertook the review to further the Board's oversight of employee compensation and benefits, recognizing that the CPC primarily functions as a compensation committee (although it also has broad oversight responsibilities for financial and budget matters). OCC believes that having the CPC chaired by a Public Director (rather than a Member Director,<sup>16</sup> which is currently the case) will be more consistent with governance best practices and practices of other self-regulatory organizations. OCC believes that such a change will ensure that compensation and related decisions are undertaken in a way that is likely to support objective judgment and independence unfettered by potential conflicts that may exist by having a Member Director chair the CPC given OCC's self-regulatory responsibilities. The Board agreed with the GNC's recommendation.

Additionally, the GNC reviewed proposed regulatory standards for audit committees of self-regulatory organizations that will require such audit committees to be

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<sup>14</sup> See Article III Section 6A of OCC's By-Laws regarding Public Directors.

<sup>15</sup> The GNC Charter provides, in relevant part, that the purpose of the GNC is to review on a regular basis the overall corporate governance of OCC and recommend improvements to the Board when necessary.

<sup>16</sup> See OCC's By-Laws Article III, Section 3 and Section 5.

independent based on facts determined by a given self-regulatory organization's board of directors. Such review caused the GNC to recommend to the Board that a Public Director should be required to chair the AC in order to align with governance best practices for audit committees and to support the objectivity of the AC. The Board agreed with the GNC's recommendation. Moreover, and in furtherance of the goal of AC independence, any currently serving Management Director(s) will not be eligible to serve on the AC.

*(e) Risk Committee Membership*

OCC is amending Article III of its By-Laws to modify the composition requirements of OCC's RC. Existing Article III, Section 9 of OCC's By-Laws currently requires that the RC shall consist of the Executive Chairman, the Member Vice Chairman, at least three other Member Directors selected on a basis that shall not discriminate against any Exchange, and one or more Public Directors. OCC is replacing this description of the RC with new Article III, Section 4(d), which will modify the RC composition requirements to (i) provide that an Exchange Director<sup>17</sup> be a member of the RC and (ii) require that at least one Member Director serve on the RC (as opposed to the current minimum requirement of four Member Directors) and (iii) remove a specific requirement that one of the Member Directors on the RC be the Member Vice Chairman.

The GNC reviewed the membership composition of the RC and determined that one Exchange Director should be a member of the RC. Historically, the RC did not include Exchange Directors because Member Directors were much more directly concerned with the risk management and membership function of OCC due to the

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<sup>17</sup> See Article III Section 6 of OCC's By-Laws regarding Exchange Directors.

mutualization of risk among Clearing Members as well as the fact that Clearing Members are responsible for the contribution of margin and clearing fund deposits. Given the evolution of the markets for which OCC provides clearance and settlement services, OCC now believes that an Exchange Director should be a member of the RC. OCC believes that Exchange Directors have expertise and unique perspective on matters such as market risk as well as sophistication as to special risks arising from trading practices, strategies and new products.

In addition, the GNC recommended, and the Board approved, a reduction in the minimum composition requirement for Member Directors on the RC to allow for greater flexibility in the selection of Directors with the requisite skills and expertise to serve on the RC. OCC believes that Member Director participation on the RC is vital and will continue to require that at least one Member Director serves on the RC. OCC also believes, however, that it is necessary and appropriate to maintain flexibility to ensure that the RC comprises those Directors that have the appropriate mix of knowledge and expertise necessary to provide for the prudent oversight of risk matters at OCC.

*(f) Nomination Process for Member Directors and Public Directors*

OCC is amending Article III, Sections 5 and 6A; Article IV, Section 1; and adopting Amendment No. 1 to Amended and Restated Stockholders Agreement to provide for Board action in the nomination process for Member Directors, Public Directors, the Executive Chairman, and Member Vice Chairman in conformance with the

process set forth in the GNC Charter.<sup>18</sup> Currently, Board action is not a part of the annual election process for Member Directors and Public Directors as described in the By-Laws and the Amended and Restated Stockholders Agreement. The amendments will provide that such persons will be nominated by the GNC for purposes of the Board's annual election process and then confirmed by the Board. OCC believes that the rule change will help ensure an appropriate level of oversight and participation by the full Board in determining its own composition and that the composition of the Board fulfils its needs for particular skills and qualifications.

*(g) Elimination of Public Director Term Limits*

OCC is amending Article III, Section 6A of its By-Laws, Section IV.1. of the GNC Charter, and Section II.D. of the Board Charter to remove term limits for Public Directors. OCC believes it is appropriate to eliminate term limits for Public Directors because the learning curve for directors of OCC is significant. OCC also believes that it often takes several years for directors who come from outside the industry to achieve the particularized degree of knowledge and understanding about the business that is necessary to provide significant value. Additionally, the GNC reviewed OCC's term limit policy for Public Directors in light of benchmark data and governance trends and determined that the elimination of term limits for Public Directors is consistent with governance arrangements at large corporations. Therefore, OCC is proposing to remove its term limits for Public Directors in the interest of assuring that OCC has access to the

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<sup>18</sup> The GNC Charter had already been reviewed by OCC in 2014 and approved by the Commission. See Securities Exchange Act Release No. 72564 (July 8, 2014), 79 FR 40824 (July 14, 2014) (SR-OCC-2014-09).

full benefit of a Public Director's understanding and learning, with respect to OCC and the markets OCC serves, as it develops over time.

**(3) Amendments to Board and Board Committee Charters and the Fitness Standards**

OCC represents that its amendments to the Board Charter are intended to: (i) harmonize the description of the Board's obligations in the Board Charter with the description of the Board's obligations in OCC's By-Laws and Rules; (ii) better align the Board Charter with the Board's Corporate Governance Principles and By-Laws; (iii) reflect recent changes involving Board Committee Charters; (iv) in general, restate the Board's oversight responsibilities in a manner designed to provide for prudent governance arrangements in light of OCC's role as a systemically important financial market utility; and (v) make certain non-substantive administrative changes to the Charter.

*(a) Membership and Organization of the Board*

OCC is amending Section II of the Board Charter regarding membership and organization requirements to reflect the elimination of the role of Management Vice Chairman as described above. As a result, in the event that the Executive Chairman is absent or disabled, the Member Vice Chairman shall preside over meetings of the Board. OCC is also making amendments that will allow for additional meetings of the Board being called as the Board deems appropriate (such meetings shall be called by the Executive Chairman or his designee) and that specify that the Executive Chairman shall consult with the Corporate Secretary (in addition to other directors or officers) when establishing Board meeting agendas.

OCC is also making amendments intended to strengthen the Board's governance framework and practices surrounding meetings in executive sessions by providing added structure regarding the convening and attendance of executive sessions and promoting the enhanced recordation of important meeting events and discussions. In particular, the amendments will: (i) require that the Board meet in executive session at each regular meeting of the Board; (ii) allow the Board to determine who will participate in such sessions; (iii) provide for the exclusion of management, invited guests, and individual directors from executive sessions where discussions may involve certain sensitive matters or conflicts of interest; and (iv) require the Board to select a Director to chair executive sessions in the absence of the Executive Chairman. The amendments will also require that Board meeting minutes reflect, at least in summary fashion, the general matters discussed in an executive session. Specifically, the chair of the executive session will determine whether separate minutes of the executive sessions are to be recorded as well as the level of detail to be included in such minutes, provided that Board meeting minutes must, at a minimum, reflect that an executive session was convened and broadly describe the topic(s) discussed.

In addition, OCC is also amending the Board Charter to state that the Board comprises one Management Director, rather than two Management Directors, in conformance with the proposed Certificate of Incorporation and By-Laws changes described above. OCC is also amending the Board Charter to reflect an increase in the number of Public Directors serving on the Board from three to five.<sup>19</sup>

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<sup>19</sup> The Commission approved the increase in the minimum number of Public Directors on OCC's Board from three to five in July 2014. See Securities

To achieve a balanced representation on the Board among Member Directors, OCC is amending the Board Charter to state that the considerations involved in determining the nomination of Member Directors should include the volume of business transacted with OCC during the prior year and the mix of Member Directors that are primarily engaged in agency trading on behalf of retail customers or individual investors. OCC believes that the amendments reinforce the existing requirement in Article III, Section 5 of OCC's By-Laws that the GNC shall endeavor to achieve balanced representation among Clearing Members on the Board of Directors to assure that: (i) not all Member Directors are representatives of the largest Clearing Member Organizations based on the prior year's volume, and (ii) the mix of Member Directors includes representatives of Clearing Member Organizations that are primarily engaged in agency trading on behalf of retail customers or individual investors. OCC is removing geographic location of Clearing Members as a factor for consideration because OCC believes that location is no longer a significant consideration given modern technology and the evolution of the industry. OCC is also adding language to the Board Charter (as well as the Committee Charters) to discourage Directors from attending meetings of the Board by telephone as currently provided in the Code of Conduct for OCC Directors. Attendance by telephone will be generally discouraged because OCC believes the Board may be less likely to have the kind of interaction that leads to fully informed discussions and decisions than if Board members were to meet in person.

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Exchange Act Release No. 72564 (July 8, 2014), 79 FR 40824 (July 14, 2014)  
(SR-OCC-2014-09).

*(b) Responsibilities of the Board*

OCC is making amendments to the Board Charter that are primarily intended to:

(i) harmonize the description of the Board's obligations in the Board Charter with the description of the Board's obligations in OCC's By-Laws and Rules as well as the Board's Corporate Governance Principles<sup>20</sup> and (ii) restate the Board's oversight responsibilities in a manner designed to provide for prudent governance arrangements in light of OCC's position as a designated systemically important financial market utility.

In cases when an obligation of the Board is expressed in both the Board Charter and OCC's By-Laws and Rules, OCC is will remove the obligation from the Board Charter. OCC will replace these charter provisions with a general statement that the Board will perform those functions as the Board believes appropriate or necessary, or as otherwise prescribed by rule or regulation, including OCC's By-Laws and Rules.<sup>21</sup>

OCC is also making amendments to Section IV of the Board Charter designed to provide for prudent governance arrangements emphasizing that the Board's oversight role

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<sup>20</sup> OCC stated that the purpose of the Board's Corporate Governance Principles is to assist OCC's Board in monitoring the effectiveness of policy and decision making at the Board and management levels. In particular, OCC meant the Board's Corporate Governance Principles to address OCC's obligations as a systemically important financial market utility to have policies and procedures in place that promote sound governance, including those policies and procedures identified in the Principles for Financial Market Infrastructures published by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions.

<sup>21</sup> The change will remove from the Board Charter some of the more specific obligations of the Board as already set forth in the By-Laws and Rules in favor of a more general statement intended to reflect that the Board would perform such functions as necessary or appropriate under OCC's Rules, By-Laws and other rules or regulations. The Board Charter provisions in question can generally be identified by footnote citations to By-Law provisions included in the Board Charter in Exhibit 5C.



should operate in a manner consistent with its responsibilities as a designated systemically important financial market utility. Specifically, OCC is amending the Charter to state that the responsibilities of the Board include: (i) overseeing management's activities in managing, operating and developing OCC and evaluating OCC management's performance in executing its responsibilities; (ii) selecting, overseeing and, where appropriate, replacing the Executive Chairman of the Board and the President, providing counsel and advice to the Executive Chairman and the President as well as oversight of the performance of each such officer and of OCC in order to evaluate whether the business is being appropriately managed; (iii) setting expectations about the tone and ethical culture of OCC, and reviewing management's efforts to instill an appropriate tone and culture throughout OCC; (iv) providing oversight of risk assessment and risk management monitoring processes, including with respect to systemic risk and reviewing risk tolerances submitted to the Board for approval by its Risk Committee; (v) performing an annual self-evaluation of its performance, the performance of its Committees, the performance of individual directors and Committee members; and evaluating the Corporate Governance Principles and Fitness Standards; (vi) reviewing the amount of compensation for the Board's Public Directors (*i.e.*, directors who are not affiliated with any national securities exchange or national securities association or with any broker or dealer) as well as reviewing the annual study and evaluation of OCC's system of internal accounting controls; (vii) providing oversight of internal and external audit processes and financial reporting, including approving major changes in auditing and accounting principles and practices; and (viii) oversight of OCC's information technology strategy, infrastructure, resources and risks.

In addition, OCC is modifying certain existing Board Charter provisions related to the responsibilities of the Board. Specifically, OCC is making amendments that will specify that, in addition to overseeing major capital expenditures and approving the annual budget and corporate plan, the Board is responsible for reviewing and approving OCC's financial objectives and strategies, capital plan and capital structure, OCC's fee structure, and major corporate plans and actions, as well as periodically reviewing the types and amounts of insurance coverage available in light of OCC's clearing operations. OCC is also making amendments to specify that the Board's responsibility for fostering OCC's compliance with applicable laws and regulations includes compliance with banking, securities and corporation laws and other applicable regulatory guidance and standards. Additionally, OCC is amending provisions related to the oversight of succession planning and executive compensation to state more specifically that the Board is responsible for evaluating and fixing the compensation of the Executive Chairman and President; overseeing succession planning, human resource programs, and talent management processes; and overseeing the development and design of employee compensation, incentive and benefit programs.<sup>22</sup> The amendments will also remove a statement that OCC's Board is responsible for overseeing OCC's processes and framework for assessing, managing and monitoring strategic, financial and operational risk as this function is performed by the RC (as reflected in its Charter) with oversight from the Board.

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<sup>22</sup> OCC noted that a deleted reference to the evaluation of senior management is now covered by point (i) described in the paragraph above.

OCC is also making non-substantive organizational changes in Section IV of the Board Charter. Specifically, OCC will combine provisions related to the Board's responsibilities for approving and overseeing OCC's business strategies and monitoring OCC's performance of clearance and settlement services.

*(c) Other Administrative Changes*

In addition to the changes described above, OCC meant certain of the amendments to the Board Charter to address non-substantive, administrative issues. For example, certain amendments are being proposed to Section III of the Board Charter to reflect the adoption of the TC the GNC, and renaming of the Performance Committee to the CPC, as described herein. In addition, OCC is also amending Section I of the Board Charter to more accurately state that the Board is responsible for providing direction to and overseeing the conduct of the affairs of OCC (as opposed to just managing the business and affairs) and to remove an unnecessarily specific list of OCC stakeholders. OCC is also making amendments to require an annual (as opposed to the less specific "periodic") review of the Board Charter, including the Corporate Governance Principles and Fitness Standards.

*(d) Fitness Standards for Directors, Clearing Members and Others*

OCC is also amending the Fitness Standards to remove descriptions of the categories of directors represented on the Board and the process by which they are nominated for Board service as these descriptions are already maintained in Article III of OCC's By-Laws and the relevant Committee Charters. Eliminating these redundant descriptions in the Fitness Standards will promote efficiency and clarity by eliminating the need to ensure consistency of the same information across multiple documents. OCC

believes that the amendments will underscore that the Fitness Standards are intended to facilitate the performance of OCC's role as a systemically important financial market utility.

*(e) Common Amendments to Each Committee Charter*

OCC is making conforming amendments to the Committee Charters as a result of the Commission approving certain changes to the GNC Charter. Specifically, OCC is amending each Committee Charter to confirm that each Board Committee has access to all books, records, facilities and personnel of OCC in carrying out the respective Board Committee's purpose and responsibilities. OCC stated that this amendment to the Committee Charters will make explicit a longstanding principle under which each Committee has operated. Additionally, references to the "Governance Committee" in each Committee Charter will be changed to the "Governance and Nominating Committee" to reflect the formation of the GNC.

Furthermore, OCC will delete a provision from each Committee Charter that grants the Chair of each Board Committee the authority to act on behalf of the respective Board Committee in situations in which immediate action is required and convening a Board Committee meeting is impractical. Although this provision also requires each Chair to report such actions to the respective Board Committee for ratification as soon as practicable, OCC believes that removing this provision is appropriate from a governance perspective because it supports deliberation and action by a Board Committee as a whole rather than action by a Chair. In addition, OCC represented that, historically, each Board Committee has been able to convene when necessary.

OCC is changing each Committee Charter to strengthen OCC's Board Committee governance framework and practices surrounding meetings in executive sessions by providing added structure regarding the convening and attendance of executive sessions and promoting the enhanced recordation of important meeting events and discussions. Specifically, each Committee Charter will be amended to: (i) require that each Committee meet in executive session at each regular meeting of the Committee; (ii) allow the Committee to determine who will participate in such sessions; and (iii) provide for the exclusion of management, invited guests, and individual directors from executive sessions where discussions may involve certain sensitive matters or conflicts of interest. The amendments will also require that each Committee's meeting minutes reflect, at least in summary fashion, the general matters discussed in an executive session. In particular, the Chair (or Acting Chair) will determine whether separate minutes of the executive sessions are to be recorded as well as the level of detail to be included in such minutes, provided that Committee meeting minutes must, at a minimum, reflect that an executive session was convened and broadly describe the topic(s) discussed.

Additionally, the Committee Charters will be amended to permit any Board Committee to engage specialists or advisors to assist it in carrying out its delegated responsibilities without prior Board approval. Generally speaking, Committees must obtain pre-approval from the Board to hire advisors. OCC's understanding is that public company board committees frequently are authorized to engage advisors without board pre-approval at the company's expense to preserve autonomy and independence and to assist them in the execution of their responsibilities as deemed necessary. Under the amended charters, each Committee's engagement of an advisor, including fees and

expenses, will be referenced in its annual report to the Board. OCC intends these amendments to foster Committee independence as well as timely Committee access to expertise relevant to the discharge of its delegated responsibilities while preserving Board oversight via the application of existing reporting mechanisms.

OCC is also amending its Committee Charters to specify that each Committee should evaluate its own and its individual members' performances on an annual basis (as opposed to regularly) to provide more clarity and specificity regarding the timing of each Committee's self-assessment process.

#### **(4) Amendments to the Audit Committee Charter**

OCC is making amendments to the AC Charter intended to, among other things: (i) reinforce the independence of the AC; (ii) more accurately memorialize and expand upon the activities of the AC with respect to the oversight of OCC's financial reporting processes and enhance the independence and objectivity in connection therewith; and (iii) in general, provide more explicit descriptions of the AC's functions and responsibilities.

##### *(a) Purpose, Membership and Authority*

OCC is changing Sections I, II and III of the AC Charter related to the purpose, membership and organization, and authority of the AC. In Section I of the AC Charter, OCC is making organizational changes to certain statements regarding the AC's responsibility to serve as an independent and objective party to oversee OCC's system of internal control, compliance environment and processes. OCC stated that these changes are non-substantive in nature. OCC is also making various textual clarifications, which OCC believes are non-substantive, in Section I, including, for example, replacing the term "independent accountants" with "external auditors" and replacing "Corporation"

with “OCC,” which will extend throughout the entire AC Charter. OCC does not intend for the amendments to change the term “independent accountants” to “external auditors” to signify a change in roles or responsibilities.

OCC is also amending Section II of the AC Charter to reinforce the independence of the AC. Specifically, the amendments provide that all members of the AC be independent from OCC’s management, as determined by the Board from time to time, and that the Chair of the AC be a Public Director.<sup>23</sup> Additionally OCC is making amendments to clarify that the Management Director, as described in Section 7 of Article III of OCC’s By-Laws, is ineligible to serve on the AC.<sup>24</sup> OCC is also revising the AC Charter to state that the AC will meet regularly, and no less than once annually (as opposed to “at least annually”), with management, OCC’s Chief Financial Officer, Chief Audit Executive (“CAE”) and Chief Compliance Officer (“CCO”) in executive sessions to discuss certain private matters. According to OCC, the purpose of this change is to signify that these meetings and interactions occur more than once per year. Section II of the AC Charter is amended to explicitly provide the authority for the CAE and CCO to communicate directly with the Chair of the AC, with respect to any of the responsibilities of the AC, outside of regular meetings to further underscore their independence. Further, OCC is amending Section II of the AC Charter to state that attendance at an AC meeting by telephone is discouraged because OCC believes the Committee may be less likely to

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<sup>23</sup> The change concerning the AC Chair will conform the AC Charter to proposed Article III, Section 4(a) of OCC’s By-Laws, as described above.

<sup>24</sup> In the event OCC has a Non-Executive Chairman, such individual will not be considered a Management Director.

have the kind of interaction that leads to fully informed discussions and decisions than if Committee members were to meet in person.

OCC is also amending the AC Charter to provide that the AC shall make such reports to the Board as deemed necessary or advisable for the purpose of promoting effective communication between the AC and the Board, in line with requirements in other Committee Charters.

OCC is amending Section III of the AC Charter to confirm that the AC's authority to hire advisors includes the authority to approve the related fee and retention terms<sup>25</sup> In addition to more accurately reflecting current Committee practice, it would conform the AC charter to OCC's other Committee Charters (i.e., the CPC, GNC, RC and TC Charters) with respect their authority to hire advisors and approve related fees and retention terms. As noted above, each of OCC's Committee Charters will be amended to permit any Board Committee to engage specialists or advisors to assist it in carrying out its delegated responsibilities without prior Board approval in order to foster Committee independence as well as timely access to relevant expertise from outside specialists or advisors. The amendments will clarify that this authority also extends to the approval of related fee and retention terms.

*(b) Functions and Responsibilities*

OCC is also making a number of amendments to Section IV of the AC Charter intended to reinforce and expand upon the activities of the AC with respect to the oversight of OCC's financial reporting processes, to enhance the independence and

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<sup>25</sup> OCC will also remove a statement concerning the AC's authority to obtain advice from independent counsel, accountants or others as such statement would be replaced by a broader expression of the AC's authority to hire advisors.



objectivity in connection therewith, and to more explicitly describe the AC's functions and responsibilities.

#### Oversight of External Auditor and Financial Reporting

OCC is amending the AC Charter regarding the AC's oversight of financial reporting and external auditors. OCC intends the amendments to the AC Charter to more accurately memorialize and expand upon the AC's role with respect to financial reporting at OCC. With respect to financial statements and financial reporting, the amendments state that the AC is responsible for: (i) discussing with management and external auditors OCC's audited and unaudited financial statements; (ii) upon management's recommendation, approving OCC's financial statements after reviewing with management and external auditors prior to issuance;<sup>26</sup> (iii) reviewing with management, external auditors and OCC's Internal Audit Department significant financial reporting issues and judgments made in connection with the preparation of financial statements, critical accounting policies and estimates, any major issues regarding accounting principles and financial statement presentation and the effect of regulatory and accounting initiatives; (iv) approving material changes to OCC's accounting policies; (v) resolving disagreements between management and external auditors regarding financial reporting; and (vi) reviewing and discussing with external auditors any audit problems or difficulties, and management's response thereto.

Additionally, to improve the AC's oversight and evaluation of external auditors, OCC is amending the AC Charter to require the AC to: (i) discuss with management the

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<sup>26</sup> OCC intends the amendment to restate, clarify, and expand on an existing statement in the AC Charter regarding the AC's review of annual audited financial statements, which OCC will delete.

timing and process for implementing a rotation of the engagement partner of the external auditor and any other active audit engagement team partner; (ii) monitor and evaluate the qualifications of both the external auditor and engagement partner; (iii) consider whether there should be a regular rotation of the audit firm itself; and (iv) pre-approve all services provided by the external auditor (as opposed to only non-audit services).

#### Oversight of Internal Audit, Compliance and Compliance-Related Matters

OCC is amending Section IV of the AC Charter in order to more clearly articulate the AC's responsibility for the oversight of Internal Audit. Specifically, OCC is making amendments stating that the AC's responsibilities include reviewing and approving the Internal Audit Policy on an annual basis and monitoring ongoing internal audit activities. OCC is also making amendments stating that the AC is responsible for approving OCC's annual internal audit plan and approving any CAE recommendations for removing or deferring any audits from a previously approved internal audit plan to explicitly codify these existing AC practices in the AC Charter. OCC believes that the AC, which serves as an independent and objective party tasked with the oversight of OCC's system of internal control, auditing, accounting, and compliance processes, is the appropriate body to approve OCC's internal audit plan and any CAE recommendations for removing or deferring any audits from a previously approved internal audit plan. OCC believes that the amendments will provide more clarity and transparency regarding OCC's governance arrangements by codifying these responsibilities found in the AC Charter.

OCC is also amending to Section IV of the Charter to more clearly articulate the AC's responsibility for oversight of compliance and compliance-related matters, including: (i) annually reviewing and approving OCC's Compliance Policy and

employee Code of Conduct; (ii) reviewing and approving the Compliance Department’s process for establishing the risk-based annual Compliance Testing Plan, monitoring progress against the annual Compliance Testing Plan, and approving changes to the Compliance Testing Plan recommend by the CCO; and (iii) monitoring ongoing compliance activities by reviewing reports and other communications prepared by the Compliance Department, including updates from the CCO, and inquiring of management regarding steps taken to address items raised.

In addition, OCC is clarifying the AC’s responsibilities with respect to: (i) reviewing on a regular basis the significant deficiencies and material weaknesses in the design or operation of OCC’s internal controls (as such issues are identified by or presented to the AC); (ii) reviewing fraud involving OCC’s management or other employees; and (iii) reviewing and approving (as opposed to just establishing) OCC’s “whistleblower” procedures that govern reporting of illegal or unethical conduct, accounting irregularities and similar matters and discussing any substantive issues identified through such procedures with relevant parties.

#### Oversight of OCC’s Chief Audit Executive and Chief Compliance Officer

OCC is amending Section IV of the AC Charter to provide that the CAE and CCO will each report functionally to the AC and administratively to the Executive Chairman.<sup>27</sup> According to OCC, the amendments will make more explicit the reporting lines for these functions and underscore the independence of the CAE and CCO. In addition, OCC is eliminating provisions of the AC Charter that relate to the AC’s assessment of the

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<sup>27</sup> This change explicitly notes existing reporting lines in the AC Charter, but does not revise those reporting lines. These provisions mirror a comparable provision in the RC Charter with respect to the Chief Risk Officer.

performance of the CAE and Internal Audit Department, the AC's approval of the compensation of the CAE, and the AC's assessment of the Compliance function and replace them with provisions that take into account the involvement of the Executive Chairman in those functions. As amended, the AC Charter will state that the AC, in consultation with the Executive Chairman, will review the performance of the Internal Audit function and the CAE, the Compliance function and the CCO, and determine whether to accept or modify the Executive Chairman's recommendations with respect to the performance assessment and annual compensation for each. OCC intends the changes related to the performance and compensation setting regime for the CAE and CCO to reflect the fact that the CAE and CCO report administratively to the Executive Chairman while reporting functionally to the AC.

**(5) Amendments to the Compensation and Performance Committee Charter**

OCC is changing its CPC Charter to explicitly describe the Committee's functions and responsibilities with respect to OCC's human resources, compensation and employee benefit programs, and insurance programs. The amendments will also provide for CPC oversight of OCC's Capital Plan in recognition of the importance of providing for Board-level oversight to ensure OCC's capital and Capital Plan meet or exceed minimum regulatory standards.

*(a) Purpose, Membership, and Authority*

OCC is renaming the Performance Committee to the CPC to reflect its role more accurately. OCC is also amending Section I of the CPC Charter to articulate that the CPC is tasked with assisting the Board in the oversight of OCC's overall performance in promptly and accurately delivering clearance, settlement and other designated industry

services and in the accomplishment of other periodically-established corporate goals and objectives in light of OCC's systemically important status. The CPC Charter will further delineate that the CPC is tasked with (i) recommending the compensation of OCC's Executive Chairman and President and approving the compensation of certain other officers, as appropriate; (ii) overseeing OCC's Capital Plan and financial performance; (iii) overseeing OCC's Human Resources program; (iv) overseeing the structure and design of the employee compensation, incentive and benefit programs; and (v) assisting the Board in reviewing OCC's leadership development and succession planning.

Additionally, OCC is amending Section II of the CPC Charter related to the membership and organization of the CPC to conform the CPC Charter to proposed Article III, Section 4(b) of OCC's By-Laws to state that the Chair of the CPC shall be a Public Director. In addition, OCC is changing Section II of the CPC Charter to elaborate on the CPC's responsibility to discuss and review the performance and compensation levels (including benefits and perquisites such as sign-on bonuses, retention arrangements, relocation arrangements and other financial commitments of OCC) of members of the Management Committee and certain other key officers, as appropriate.

OCC is also amending Section II to clarify that the CPC will meet at least four times per year, which reflects the minimum number of regular meetings in a year in a manner consistent with the charters of other Board Committees, and to delete a provision of the CPC Charter that requires the CPC Chair to meet in private session with the GNC Chair to discuss performance of key officers as well as a provision stating that the Chairs of the AC and RC will be invited to attend the annual meeting to discuss compensation of

key officers, including the Chief Risk Officer (“CRO”) and CAE.<sup>28</sup> The CPC Charter is amended to require that minutes of Committee meetings be circulated to the Board in conformance with general requirements applicable to all Board Committees.<sup>29</sup>

OCC is also amending the CPC Charter to discourage attendance at a CPC meeting by telephone because OCC believes the Committee may be less likely to have the kind of interaction that leads to fully informed discussions and decisions than if Committee members were to meet in person. In addition, other clarifying and textual changes will be made including, for the reasons stated above, removal of references to the Management Vice Chairman.

Additionally, OCC will make organizational changes in Section III regarding the delegation of authority to the Administrative Committee that do not change the meaning of the rule text.

*(b) Functions and Responsibilities*

OCC is amending Section IV of the CPC Charter to explicitly describe the Committee’s responsibilities with respect to OCC’s capital structure, financial planning and corporate goals and objectives; human resources and compensation programs; and employee benefits programs in order to provide a more robust framework for the CPC’s oversight functions. Additionally, OCC will remove explicit requirements in Section IV that the CPC review the Corporate Plan and Budget and OCC’s performance under the Corporate Plan at each regularly scheduled meeting in favor of more general descriptions

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<sup>28</sup> These changes are being made to reflect a consultative process as between the Executive Chairman and, as applicable, the RC and Board to discuss the performance of key officers including the CRO and CAE.

<sup>29</sup> This requirement is already included in the AC, GNC, RC, and TC Charters.

regarding the CPC's responsibilities for the oversight of the corporate financial planning process, including the corporate budget, and corporate goals and objectives. OCC intends the amendments to accommodate CPC review of annual Corporate Plans and Budgets and performance thereunder (as currently contemplated by the CPC Charter) as well as consideration of longer-term horizons and implications in the strategic planning process.

#### Oversight of OCC's Capital Plan

OCC is amending Section IV of the CPC Charter to explicitly provide for the CPC's responsibilities in connection with overseeing OCC's capital structure, financial planning, and corporate goals and objectives. Specifically, the amendments will state that the CPC's responsibilities include oversight of management's processes for determining, monitoring and evaluating OCC's Capital Plan,<sup>30</sup> including maintenance of required regulatory capital, and recommending approval of such plan to the Board. These amendments will also specify that the CPC is responsible for the annual review of OCC's Fee, Refund and Dividend Policies and making recommendations to the Board for changes to such policies and payments, if any, under the Refund and Dividend Policies. In addition, OCC is making amendments to provide that the CPC's responsibilities include the review and approval of fee changes pursuant to the Capital Plan, review and recommendation to the Board of changes to OCC's fee structure, and oversight of OCC's corporate financial planning process (including reviewing the corporate budget).

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<sup>30</sup> See Securities Exchange Act Release No. 74387 (February 26, 2015), 80 FR 12215 (March 6, 2015) (SR-OCC-2014-813). See also Securities Exchange Act Release No. 74452 (March 6, 2015), 80 FR 13058 (March 12, 2015) (SR-OCC-2015-02).

Moreover, the amendments will provide for the CPC's responsibility to review OCC's annual corporate goals and objectives and recommend approval thereof to the Board and routinely receive reports regarding progress in achieving such goals and objectives. The amendments will also provide that the CPC is responsible for the periodic review of OCC's insurance program.

#### Oversight of Human Resources and Compensation Programs

OCC is amending Section IV of the CPC Charter to explicitly state that the CPC's responsibilities include review of OCC's Human Resources programs and policies, including OCC's talent acquisition, performance management, training, benefits and succession planning processes and review and approval of the structure, design, and funding as applicable, of employee compensation, incentive and benefit programs. OCC believes that this amendment will ensure that Board Committee oversight for management's processes for hiring, retaining and developing qualified staff and is consistent with the CPC's oversight of overall succession planning processes. Additionally, OCC is amending the CPC Charter to clarify that the CPC annually reviews and approves the goals and objectives of the Executive Chairman and President.

Further, OCC is making amendments to the CPC Charter that will require the CPC to periodically (not less than annually) review and approve the general strategy, policies and programs with respect to salary compensation (including management compensation) and incentive compensation and seek to ensure compensation policies meet evolving compensation practices so that such policies remain effective to attract, motivate and retain executive officers and other key personnel. The amendments will also require the CPC to review and approve the performance and compensation of key



employees, such as members of OCC's Management Committee, at the end of each year and to make recommendations to the Board regarding the compensation of the Executive Chairman and the President. Additionally the amendments will require the CPC to review proposed material changes to executive management benefits and to periodically review the compensation of Public Directors and make recommendations to the Board with respect thereto.

OCC is amending the CPC Charter to remove certain statements regarding the review of OCC's performance under the Corporate Plan and the oversight of the administration of OCC's compensation plans as these responsibilities will be covered under the amended descriptions contained therein. OCC believes that it is prudent and appropriate to provide for CPC oversight in the areas of human resources, performance, and compensation and that the amendments will enhance OCC's overall governance arrangements with respect to the oversight and review of performance and compensation at OCC.

#### Oversight of Employee Benefit Programs and Other Responsibilities

OCC is also making amendments to Section IV of the CPC Charter related to the CPC's oversight responsibilities for employee benefit programs. Specifically, OCC is amending the CPC Charter to specify the CPC's responsibilities for oversight, administration, and operation of employee benefit, retiree and welfare benefit plans, including the review of funding plan obligations. The amendments will also specify the scope of employee welfare plans that the CPC reviews and the CPC's right to adopt new compensation, retirement and welfare benefit plans or to terminate existing plans other than such plans that require Board action to amend or terminate. In addition, the

amendments will provide more clarity regarding the CPC's responsibilities for monitoring the Administrative Committee's duties in connection with retirement and retirement savings plans, investment strategy and performance, plan design and compliance, prudent selection of investment managers and compensation and benefits consultants, and performing such other oversight duties as called for in retirement, retirement and savings, and welfare plan documents.

OCC is making further amendments that state that the CPC is responsible for providing updates to the Board periodically regarding: (i) actions taken by the CPC with respect to its review of OCC's compensation, retirement and employee welfare plans; (ii) the financial position and performance of these plans; and (iii) adherence to investment guidelines, in each case, where applicable.

#### **(6) Amendments to the Risk Committee Charter**

OCC is amending its RC Charter primarily to enhance OCC's governance arrangements with respect to the RC's oversight functions and responsibilities. OCC is also making amendments to better align the RC Charter with the OCC By-Laws, including changes in the composition requirements of the RC (as described above) and to reflect the adoption of the TC.

##### *(a) Purpose, Membership and Authority*

OCC is amending Section I of the RC Charter to provide that the RC will be responsible for coordinating risk oversight with other Board Committees tasked with overseeing certain risks (e.g., the TC, which assists the Board in overseeing OCC's information technology risks) to achieve comprehensive and holistic oversight of OCC's

risk-related matters. The amendments will also provide that the RC is responsible for the review of material policies and processes associated with risks related to new initiatives.

OCC is amending Section II of the RC Charter to provide that attendance at a RC meeting by telephone is discouraged because OCC believes the Committee may be less likely to have the kind of interaction that leads to fully informed discussions and decisions than if Committee members were to meet in person. OCC is also removing from the RC Charter, and by extension its rules, a requirement that a RC member shall recuse himself from any matter in which his firm has an interest, other than a common interest shared with Clearing Members generally or a particular class of Clearing Members. Currently, none of the Committee Charters, other than the RC Charter, contain a such recusal provision.<sup>31</sup> OCC believes that the identification and handling of conflicts of interest are already appropriately addressed in its Code of Conduct for OCC Directors, which governs the conduct of all directors regardless of category or committee assignment. OCC noted that, as a corporation incorporated in the state of Delaware, OCC's Directors have a fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders<sup>32</sup> and are bound by a duty of loyalty to OCC, which demands that there be no conflict between duty and self-interest and that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director.<sup>33</sup>

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<sup>31</sup> The current CPC Charter includes a narrower provision regarding recusal of the Executive Chairman from discussions of his individual compensation, benefits, and prerequisites.

<sup>32</sup> See *Cede & Co. v. Technicolor*, 634 A.2d 345, 360-361 (Del. 1993)

<sup>33</sup> See *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939).

With respect to RC meetings, OCC is amending the RC Charter to state that the RC shall meet regularly, and no less than once annually, (rather than “at least annually”) with the CRO and members of management (as opposed to other appropriate corporate officers) in separate executive sessions to discuss certain private matters. OCC stated that the purpose of the change is to signify that these meetings occur more frequently than once per year. The changes will also specifically require that the RC meet in executive session regularly with members of management. The RC will continue to have the discretion to invite any other officers it deems appropriate to meetings in executive session pursuant to the common charter amendments described above. Moreover, and in order to enhance the independence and functional reporting relationship of the CRO to the RC, OCC will make revisions to explicitly state that the CRO is authorized to communicate with the RC Chair outside of regular meetings. OCC is also amending the RC composition requirements in Section II to conform to the By-Law changes discussed above. Specifically, the RC Charter will be revised to state that the RC shall consist of the Executive Chairman, at least one Exchange Director, at least one Member Director, and at least one Public Director. OCC is also amending Section II to require that the RC meet at least six times a year (as opposed to seven) in recognition of the fact that the time allotted for each individual RC meeting has been expanded. Furthermore, OCC is amending Section II of the RC Charter to state that, unless a Chair is elected by the full Board, the members of the RC shall designate a Chair by majority vote. OCC stated that this amendment is in conformance with OCC’s current practices for electing Committee Chairs and as described in other Committee Charters.

OCC is also amending Section III of the RC Charter to provide that, in addition to RC subcommittees, the RC may also delegate authority to OCC's Management Committee or Enterprise Risk Management Committee. As described herein, the RC is responsible for assisting the Board in overseeing OCC's policies and processes for identifying and addressing strategic, operational, and financial risks and for overseeing the overall enterprise risk management framework implemented by management. The amendment will allow the RC to delegate authority to the Management Committee and Enterprise Risk Management Committee to carry out certain tasks and responsibilities in the day-to-day risk management of OCC and to implement proposals that the RC has approved in concept where the RC deems such delegation of authority to be appropriate.

*(b) Functions and Responsibilities*

OCC is amending Section IV of the RC Charter to enhance its governance arrangements in connection with the oversight of membership requirements, margin requirements, the Enterprise Risk Management Program, and a number of other responsibilities.

Oversight of Membership and Margin Requirements

OCC is amending the RC Charter to provide a broader description of the RC's oversight of the adequacy and effectiveness of OCC's framework for clearing membership. OCC stated that, in general, these changes are not intended to substantively change or eliminate any of the RC's existing responsibilities with respect to its oversight of OCC's clearing membership framework and will continue to encompass the

responsibilities currently enumerated in the charter.<sup>34</sup> Specifically, the RC Charter provisions related to the RC's oversight role with respect to clearing membership issues will be replaced with a more general statement that the RC is responsible for the oversight of OCC's framework for clearing membership, including: (i) periodically reviewing and revising, as appropriate, OCC's initial and ongoing requirements for clearing membership;<sup>35</sup> (ii) overseeing the processes established for reviewing and monitoring clearing membership (including in respect of the continuance of potentially problematic members);<sup>36</sup> and (iii) making recommendations to the Board, as applicable, for final determination in respect the foregoing.

In addition, OCC is modifying certain provisions related to the surveillance of Clearing Members and contingency planning for Clearing Member failures. Specifically, OCC will consolidate these provisions to restate that the RC is responsible for the oversight of the adequacy and effectiveness of OCC's contingency plan for Clearing Member failures, including: (i) reviewing Clearing Member surveillance criteria; (ii)

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<sup>34</sup> For example, individual provisions related to specific types of membership categories and requirements will be replaced by a broader restatement of the RC's responsibilities, which is intended to capture all of the responsibilities enumerated in the delete provisions.

<sup>35</sup> The provision is a restatement of an existing RC responsibility for periodically reviewing and recommending changes to the initial and ongoing requirements for membership and will also replace and encompass the responsibilities in an existing provision of the RC Charter stating that the RC is responsible for recommending to the Board membership requirements for non-broker-dealers.

<sup>36</sup> The provision this amendment will replace and encompass the RC's responsibilities contained in existing RC Charter provisions related to the conducting of hearings for applicants proposed to be disapproved by the RC, the review and approval/disapproval of requests to participate in the Stock Loan Programs, and the approval/disapproval of the continued membership of managed Clearing Members.

overseeing the management processes for managing Clearing Members that are subject to closer than normal surveillance or are otherwise in or approaching financial or operational difficulty; (iii) imposing and modifying restrictions and requirements already imposed on Clearing Members in a manner consistent with the By-Laws and Rules;<sup>37</sup> and (iv) making recommendations to the Board in respect of the foregoing.

OCC is making similar amendments to the RC Charter to restate the RC's responsibilities in connection with its oversight of margin and clearing fund requirements. OCC will remove certain existing provisions related to the oversight of margin and clearing fund requirements and replace them with a more high level description that will provide that the RC oversees OCC's processes for establishing, monitoring and adjusting margin consistent with the protection of OCC, Clearing Members, or the general public, including: (i) reviewing and modifying OCC's margin formula, the methodologies used for determining margin and clearing fund requirements, and making recommendations to the Board, as applicable, in respect thereof;<sup>38</sup> (ii) evaluating (including increasing) the amount of margin required in respect of any contract or position; (iii) establishing and reviewing guidelines for requiring the deposit of additional margin; and (iv) reviewing and approving determinations about assets

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<sup>37</sup> The provision will replace and encompass the responsibilities in an existing RC Charter provision related to the RC's responsibility for reviewing and modifying or reversing restrictions or additional requirements imposed on Clearing Members pursuant to OCC Rule 305.

<sup>38</sup> This provision will include language from an existing Charter provision stating that the RC will review methodologies used for calculating margin and clearing fund requirements.

eligible for deposit as margin or clearing fund as provided in the By-Laws and Rules.<sup>39</sup> OCC stated that, in general, the amendments are not intended to substantively change the RC's responsibilities in the deleted provisions but will instead replace them with a broader description intended to encompass those responsibilities. OCC will, however, delete an existing RC Charter provision specifically requiring the RC to periodically review the inputs to OCC's margin formula and modify them to the extent it deems such action to be consistent with the protection of OCC, Clearing Members, or the general public. While this specific requirement is being removed from the Charter, OCC believes that the Charter continues to provide an adequate and appropriate oversight framework for the monitoring and development of OCC's margin formula and would provide the RC with continued authority to modify margin formula inputs if it deems such modification to be appropriate.<sup>40</sup>

OCC is also deleting a provision stating that the RC is responsible for making determinations regarding approval of non-U.S. institutions to issue letters of credit as a form of margin asset because this provision does not accurately reflect the RC's responsibilities. While the RC is responsible for overseeing standards used to admit non-U.S. institutions, OCC's President and Executive Chairman have general responsibility

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<sup>39</sup> This provision will replace and encompass the RC's responsibilities contained in existing Charter provisions related to the oversight of acceptable margin and clearing fund assets, including the approval of classes of GSE securities for deposit as margin, prescribing intervals for revaluing debt securities deposited as margin of clearing fund, and specifying haircuts for securities provided as margin.

<sup>40</sup> As noted above, the amendments to the RC Charter will provide that the RC is responsible for overseeing the processes established for establishing, monitoring and adjusting margin consistent with the protection of OCC, Clearing Members, or the general public, including reviewing and modifying OCC's margin formula.



for approving financial institutions seeking to become non-U.S. letter of credit banks and that meet the requirements of OCC Rule 604, Interpretation and Policy .01 (with the exception of certain “equivalent country” and “equivalent institution” determinations that are required to be made by the RC pursuant to OCC Rule 604, Interpretations and Policies .01(b)(3) and .01(b)(4)(b)).

#### Oversight of OCC’s Enterprise Risk Management Program and Risk Tolerances

OCC is making amendments to restate and expand upon the RC’s responsibility for overseeing OCC’s Enterprise Risk Management program. Currently, the RC is responsible for overseeing the structure, staffing and resources of the Enterprise Risk Management program, reviewing periodic reports regarding the Enterprise Risk Management program, and annually reviewing and assessing the overall program. OCC is amending the RC Charter to restate these existing responsibilities and add new responsibilities designed to enhance the risk oversight framework for the Enterprise Risk Management program. Specifically, the amendments will state that the RC is responsible for overseeing OCC’s Enterprise Risk Management program, including (in addition to the existing responsibilities noted above), reviewing the systems and procedures that management has developed to manage the risks to OCC’s business operations and regularly discussing these systems and procedures with management, reviewing with management the interrelated nature of OCC’s risks, and annually approving the Enterprise Risk Management program’s goals and objectives. OCC believes that explicitly incorporating these responsibilities into the RC Charter will provide for a more comprehensive oversight framework for the Enterprise Risk Management program.

OCC is also making amendments to restate and expand upon the RC's responsibility for the oversight of OCC's risk appetite and risk tolerances. Currently, the RC Charter provides that the RC is responsible for reviewing and recommending for Board approval the OCC Risk Appetite Statement and reviewing and monitoring OCC's risk profile for consistency with OCC's Risk Appetite Statement. The amendments to the RC Charter will state that, in addition to these responsibilities, the RC will be responsible for reviewing and monitoring determinations regarding appropriate risk tolerances, including reviewing with management on a regular basis management's view of appropriate risk tolerances and assessing whether this view is appropriate, and recommending risk tolerance parameters to the Board. OCC believes that explicitly incorporating these responsibilities into the RC Charter will provide for a more comprehensive oversight framework for OCC's risk appetite and risk tolerances.

#### Other Oversight Responsibilities

Section I of the RC Charter currently provides that the RC is responsible for the oversight and review of material policies and processes relating to member and other counterparty risk exposure assessments. OCC is amending Section IV to further specify that the RC oversees the adequacy and effectiveness of OCC's processes for setting, monitoring and acting on risk exposures to OCC presented by banks, depositories, financial market utilities and trade sources. OCC believes that the oversight of such risk exposures is critical to ensuring the safety and soundness of OCC and that specifically including this responsibility in the RC Charter will provide for greater clarity and transparency regarding the RC's role in overseeing these risks. Section I of the RC Charter also currently provides that the RC is responsible for the oversight and review of

material policies and processes (i) for identifying liquidity risks and (ii) relating to liquidity requirements and the maintenance of financial resources. The amendments to Section IV will further specify that the RC oversees the processes established by OCC for setting, monitoring and managing liquidity needs necessary for OCC to perform its obligations as a systemically important financial market utility. OCC believes that comprehensive oversight of liquidity risks and liquidity risk management is critical to ensuring the safety, soundness, and resilience of OCC and that providing more specificity regarding the RC's responsibilities with respect to liquidity risk will provide for greater clarity and transparency regarding the RC's role in such oversight. In addition, OCC is amending the RC Charter to provide that the RC and management discuss, on a regular basis, the impact on systemic stability that may arise as a result of OCC's actions in responding to an extraordinary market event, including the impending or actual failure of a Clearing Member, and the development of strategies to mitigate these effects. OCC believes it is prudent for management and the RC to engage in regular discussions concerning OCC's actions in extreme market events and the potential impacts on systemic stability given OCC's role as a systemically important financial market utility.

OCC will also elaborate on the statement that the RC will perform the responsibilities delegated to it by the Board under OCC's By-Laws and Rules by specifying that this will include the authorization of the filing of regulatory submissions pursuant to such delegation. Additionally, OCC is making amendments to state that the RC will oversee management's responsibility for handling financial (i.e., credit, market, liquidity and systemic) risks, including the structure, staffing and resources of OCC's Financial Risk Management department. In addition, OCC is making amendments to

state that the RC's oversight responsibilities include: (i) identifying issues relating to strategic, credit, market, operational, liquidity and systemic risks that should be escalated to the Board for final action and (ii) reviewing, approving and reassessing reporting metrics reflecting the risks for which the RC has oversight.

Further, the amendments will specify that the RC oversees OCC's model risk management process, policies and controls, including: (i) overseeing model risk governance; (ii) reviewing the findings of any third party engaged by management to evaluate OCC's risk models; and (iii) annually reviewing and approving the Model Validation Plan and receiving periodic reports thereunder. Moreover, the amendments provide that the RC is responsible for reviewing the results of any audits (internal and external), regulatory examinations and supervisory examination reports as to significant risk items or any other matter relating to the areas that the RC oversees, as well as management's responses pertaining to matters that are subject to the oversight of the RC.

*(c) Administrative Changes*

Consistent with the GNC Charter and AC Charter, OCC is amending the RC Charter to eliminate provisions under which the RC Chair attends the year-end CPC meeting to discuss the performance and compensation levels of the CRO. Rather, the RC, in consultation with the Executive Chairman, will review the performance of the Enterprise Risk Management and Model Validation programs as well as the CRO and determine whether to accept or modify the Executive Chairman's recommendations with respect to the performance assessment and annual compensation for the CRO.<sup>41</sup> This

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<sup>41</sup> This change is consistent with comparable changes to the AC Charter with respect to the annual compensation of the CAE and CCO, respectively.

change reflects the reporting of the CRO to the Executive Chairman for administrative purposes, while preserving functional reporting to the Committee.

Further, the amendments will confirm that the RC has the responsibility for ratifying, modifying, or reversing action taken by OCC officers that have been delegated authority to consider requests by Clearing Members to expand clearing activities to include additional account types and/or products. Moreover, OCC is amending the RC Charter to clarify that the RC has the authority to authorize the filing of a regulatory submission pursuant to authority delegated to it by the Board.

**(7) Amendments to the Governance and Nominating Committee Charter**

OCC is amending the GNC Charter to reflect the elimination of term limits for Public Directors as discussed above and to state that attendance of GNC meetings by telephone is discouraged because OCC believes the Committee may be less likely to have the kind of interaction that leads to fully informed discussions and decisions than if Committee members were to meet in person. OCC will also delete a provision stating that a designated officer of management shall serve to assist the Committee and act as a liaison between staff and the Committee because OCC believes based on its experience that designating a formal role for a liaison was unnecessary. Deleting this requirement will also maintain uniformity across all Committee Charters, as no other Committee has a formally designated liaison.

OCC is also amending the GNC Charter to specify that the Chair (or the Chair's designee) shall consult with the Corporate Secretary, in addition to management, to prepare an agenda in advance of each GNC meeting as the Corporate Secretary is responsible for coordinating the preparation and distribution of Board and Board

Committee meeting agendas. In addition, OCC is making non-substantive drafting changes regarding: (i) the numbering of certain provisions in Section I of the GNC Charter and (ii) the requirements for GNC Committee reports to the Board in Section II of the Charter.

#### **(8) Amendments to the Technology Committee Charter**

OCC is amending its TC Charter to require that the TC meet regularly, and no less than once annually, with OCC's Chief Security Officer ("CSO") and to provide that the CSO is authorized to communicate directly with the Chair of the TC in between meetings of the Committee in order to strengthen the autonomy and independence of the CSO role at OCC. OCC is also amending the TC Charter to provide that the TC shall make such reports to the Board as deemed necessary or advisable. This change promotes effective communication between the TC and the Board is in line with requirements in other Committee Charters.

OCC is also making non-substantive amendments to Section III of the TC Charter to eliminate a provision that referenced approval of non-audit services, which appeared to be an inadvertent carry-over from the Audit Committee Charter and to Section IV of the Charter to change the term "the Company" to "OCC" and "Board of Directors" to "Board."

#### **II. Discussion**

Section 19(b)(2)(C) of the Act<sup>42</sup> directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that the rule change, as proposed,

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<sup>42</sup> 15 U.S.C. 78s(b)(2)(C).

is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization.

Section 17A(b)(3)(F) of the Act requires, inter alia, that the rules of a clearing agency be designed, in general, to protect investors and the public interest.<sup>43</sup> Further, Rule 17Ad-22(d)(8) of the Act requires that a clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to, as applicable, have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Act applicable to clearing agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures.<sup>44</sup>

OCC's proposal relates to OCC's governance arrangements. The proposal comprises changes to OCC's Certificate of Incorporation, By-Laws and Rules, Amended and Restated Stockholders Agreement, Board Charter, AC Charter, CPC Charter, RC Charter, GNC Charter, TC Charter, and Fitness Standards (collectively, "Governing Documents"), as described in greater detail above in section I, Description of the Proposed Rule Change. These changes fall broadly into the following categories: (1) Board and Committee composition; (2) Committee authority and procedures; (3) Board and Committee meeting management; (4) Board and Committee responsibilities and functions; and (5) administrative textual changes.

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<sup>43</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>44</sup> 17 CFR. 240.17Ad-22(d)(8).

### **(1) Board and Committee Composition**

OCC will revise its By-Laws, Amended and Restated Stockholders Agreement, and Board Charter to reduce the number of Management Directors on its Board from two to one and remove references to the Management Vice Chairman. OCC stated that the position of the second Management Director, which is meant to be filled by the Management Vice Chairman, recently has been vacant. According to OCC, all of the Management Vice Chairman's obligations have been appropriately managed in the absence of a Management Vice Chairman. Further, OCC historically operated with only one Management Director until 2013.

OCC will also amend its By-Laws, AC Charter, and CPC Charter to require that the AC and the CPC each be chaired by Public Directors. The role of Public Director Chairs is to contribute to the objectivity and independence of the AC and CPC. The Commission believes that the changes to OCC's governing documents facilitating inclusion of the perspectives provided by OCC's Public Directors should support the protection of the public interest because such Public Directors are not affiliated with and therefore should not have conflicts obligating them to represent the views of any national securities exchange, association, broker, or dealer. Further, OCC is revising certain Governing Documents, as described in section I above, to remove term limits for Public Directors in recognition of the time necessary to develop the knowledge and understanding of OCC's business and because OCC believes that such directors provide significant value in the governance process. Therefore, the Commission finds that the changes described in section I above relating to the removal of the second Management Director, requiring that the AC and CPC each be chaired by Public Directors, and the



removal of term limits for Public Directors, are consistent with the requirement under Section 17A(b)(3)(F) of the Act that the rules of a clearing agency be designed, among other things, to protect the public interest.<sup>45</sup>

To enhance the independence of the oversight of OCC's control functions, OCC will revise the By-Laws and the AC Charter to provide that no Management Director may serve on the AC. Additionally, OCC will revise the By-Laws and RC Charter to require that at least one Exchange Director serve on the RC and to reduce the minimum number of Member Directors on the RC. These changes to the RC composition are intended to incorporate the expertise and perspective of OCC's owner Exchanges while allowing for greater flexibility in the selection of directors with the requisite skill and expertise to serve on the RC. The Commission believes that independence and expertise are important in the composition of the committees responsible for overseeing OCC's control and risk management functions. Therefore, the Commission finds that the changes to OCC's governing documents described above providing that no Management Director may serve on the AC, requiring at least one Exchange Director to serve on the RC, and reducing the minimum number of Member Directors on the RC, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>46</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements in Section 17A of the Act applicable to clearing

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<sup>45</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>46</sup> 17 CFR 240.17Ad-22(d)(8).

agencies and to promote the effectiveness of the clearing agency's risk management procedures.

As described in section I above, OCC intends to describe more clearly in its By-Laws, Amended and Restated Stockholders Agreement, Board Charter, and Fitness Standards the process for nominating Member Directors, Public Directors, the Executive Chairman, and the Member Vice Chairman. These changes are designed to provide for a consistent description across OCC's Governing Documents, as applicable, of the nomination process and the Board's participation in the process. The Commission finds that the changes described above to OCC's Governing Documents regarding the process for nominating Member Directors, Public Directors, and Executive Chairman, and the Member Vice Chairman are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>47</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Act applicable to clearing agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures.

Additionally, OCC will make changes to certain Governing Documents, as described in section I above, related to the composition of the RC. Specifically, the changes will provide that the RC shall consist of the Executive Chairman, at least one Exchange Director, at least one Member Director, and at least one Public Director. In addition, the changes will provide for the election of the RC Chair by the RC members in the event that the Board does not designate a Chair. The Commission finds that changes

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<sup>47</sup> Id.

to OCC's Governing Documents to clearly provide for the composition of the RC and for eventualities such as the failure of OCC's Board to designate the Chair of the RC, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>48</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to support the objectives of owners and participants and to promote the effectiveness of the clearing agency's risk management procedures.

As described in section I(7) above, OCC will also remove the requirement for a management liaison to the GNC from its GNC Charter because OCC believes that no such position is necessary based on its experience and because no other Board Committee has a formal management liaison. The Commission finds that revising the design of a clearing agency's policies and procedures related to its governance arrangements by removing an unnecessary position from the composition requirements of its governing bodies is consistent with the requirement in Rule 17Ad-22(d)(8)<sup>49</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements in Section 17A of the Act applicable to clearing agencies and to support the objectives of owners and participants.

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<sup>48</sup> Id.

<sup>49</sup> Id.

## **(2) Committee Authority and Procedures**

As described in section I(3)(e) above, OCC will remove language from each Board Committee's Charter regarding the authority of the Chair of each Board Committee to act on behalf of its respective Board Committee in situations in which immediate action is required and convening a Board Committee meeting is impractical. OCC stated that it has been able to convene committee meetings when necessary and that the change will promote fully informed, deliberate decision making. Removing the authority of a Chair to act on behalf of a committee in this manner should support the incorporation of various stakeholder perspectives, which may include OCC's owners and participants as well as the public. The Commission finds the changes to each Board Committee's Charter to remove the authority of each Chair to act on behalf of its respective Board Committee, as described in greater detail in section I(3)(e) above, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>50</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to support the objectives of owners and participants, because such changes should support the incorporation of stakeholder perspectives that may include OCC's owners and participants.

OCC will also make changes to certain Governing Documents that are intended to enhance generally the quality of its governance arrangements. As described in section I(3)(e) above, changes to each Committee's Charter will allow each Committee to hire specialists without prior Board authorization, and have access to all books, records,

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<sup>50</sup> Id.

facilities and personnel of OCC. As described in greater detail in sections I(4), I(5), and I(8) above, the charters of the AC, TC, and GNC will be revised to provide for more reporting to the full Board, and the CPC Charter will be revised to require the CPC to provide its full minutes to the Board. The Commission believes that providing the authority to hire specialists should enhance committee independence, while enhanced reporting requirements should support Board oversight. The Commission finds that the changes to the Committee Charters (i) to provide authority for Board Committees to hire specialists and access OCC books, records, facilities and personnel, and (ii) to provide for enhanced reporting requirements to the Board are consistent with the requirement of Rule 17Ad-22(d)(8)<sup>51</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act applicable to clearing agencies.

Revisions to the RC Charter, described in greater detail in section I(6)(a) above, will permit the RC to delegate authority to the Management Committee and Enterprise Risk Management Committee while specifying that the RC is responsible for ratifying the actions taken under such delegated authority. Additionally, revisions to the RC Charter, described in section I(6)(c) above, will confirm the RC's authority to file certain regulatory submissions pursuant to delegations of authority from the Board. The Commission believes that the delegation of day-to-day risk management and implementation of RC-approved proposals may better support the clearing agency's risk management procedures by allowing the RC to better utilize its time and expertise.

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<sup>51</sup> Id.

Therefore, the Commission finds that the changes to the RC Charter to allow the RC to delegate authority while requiring RC ratification of delegated actions and to confirm the RC's authority to authorize the filing of certain regulatory submissions pursuant to delegated authority from the Board, as described in sections I(6)(a) and (c) above, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>52</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to promote the effectiveness of the clearing agency's risk management procedures.

### **(3) Board and Committee Meeting Management**

OCC will remove from the RC Charter certain mandatory recusal requirements designed to apply to Member Directors of the RC as described in section I(6)(a) above. OCC makes available on its website its Code of Conduct for OCC Directors, which addresses the identification and management of conflicts of interest.<sup>53</sup> OCC believes that this specific recusal requirement contained in the RC charter is unnecessary in light of the existing requirements under Delaware law and OCC's Code of Conduct for OCC Directors. The Commission finds that revising OCC's governing documents by incorporating the identification and management of conflicts of interest in a single policy or procedure related to the governance of a clearing agency is consistent with the

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<sup>52</sup> Id.

<sup>53</sup> OCC has not filed its Code of Conduct for OCC Directors with the Commission as a rule under Section 19 of the Act.

requirement in Rule 17Ad-22(d)(8)<sup>54</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act applicable to clearing agencies because such revised documents will continue to include requirements for the identification and management of director conflicts of interest.

OCC also will make several revisions the Board Charter and Committee Charters regarding the meeting structure and frequency of its Board and Committees. As described in sections I(3)(a) and I(3)(e) above, OCC will make revisions to the Board Charter and Committee Charters intended to enhance the framework for holding and recording executive sessions of the Board and Committees. The amended Board Charter will require the Executive Chairman, in consultation with the Corporate Secretary, to establish an agenda in advance of each Board meeting, and revisions to the GNC Charter will similarly require the GNC Chair, in consultation with the Corporate Secretary, to establish an agenda in advance of each GNC meeting. Revisions to the Board Charter and Committee Charters will discourage attendance by telephone at Board and Committee meetings to promote fully informed discussions and decisions. In addition, OCC will amend the Board Charter to authorize the Board to hold additional meetings, as it deems appropriate. Finally, as described in sections I(5)(a) and I(6)(a), respectively, OCC will amend the CPC Charter to specify that the CPC will meet four times per year, as opposed to in advance of each Board meeting, and will amend the RC Charter to specify that the RC will meet six, as opposed to seven, times per year. The Commission

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<sup>54</sup> 17 CFR 240.17Ad-22(d)(8).

finds that changes to OCC's governing documents to clearly describe Board and Committee meeting practices and require the Board and Committees to hold and record executive sessions as described in this paragraph are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>55</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act.

#### **(4) Board and Committee Responsibilities and Functions**

As described above, OCC is amending the Board Charter and Committee Charters regarding the functions and responsibilities of the Board and its Committees. The revised Board Charter will describe the Board's responsibilities in light of OCC's role as a systemically important financial market utility, as detailed in section I(3)(b) above. As described in section I(3)(c) above, amendments to the Board Charter will require the Board to review its Charter, OCC's Corporate Governance Principles, and Fitness Standards annually. Additional revisions to the Board Charter are intended to specify that, in addition to overseeing major capital expenditures and approving the annual budget and corporate plan, the Board is responsible for reviewing and approving OCC's financial objectives and strategies, capital plan and capital structure, OCC's fee structure, and major corporate plans and actions, as well as periodically reviewing the types and amounts of insurance coverage available in light of OCC's clearing operations. The Commission finds that changes to OCC's Board Charter designed to document OCC's recognition of its responsibilities as a systemically important financial market utility, to

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<sup>55</sup> Id.



require the Board to review certain OCC governing documents annually, and to specify further the Board's responsibilities are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>56</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act applicable to clearing agencies.

As described in section I(3)(e) above, OCC is amending the Board Charter and Committee Charters to require the Board and the Committees to perform annual self-evaluations, and require the Board to evaluate individual directors annually. The Commission finds that changes to OCC's Board Charter and Committee Charters to require OCC's governing bodies to perform such evaluations should support the effectiveness of OCC's governing bodies and thus are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>57</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act applicable to clearing agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures.

Revisions to the Board Charter are intended to make the RC, as opposed to the Board, responsible for overseeing OCC's framework for managing strategic, financial, and operational risk, with continued oversight from the Board. OCC stated that this

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<sup>56</sup> Id.

<sup>57</sup> Id.

function is already performed by the RC (as reflected in the RC Charter). The Commission finds that changes to the Board and RC Charters intended to clarify the RC's responsibility for the oversight of the risk management matters, as described in section I(3)(b) above, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>58</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to promote the effectiveness of the clearing agency's risk management procedures.

OCC will revise the AC, RC, and TC Charters to clarify the reporting lines of certain officers to their respective Board Committees. In addition, the revised Committee Charters, among other things, will require that the AC meets regularly, but no less than annually with the CFO, CAE, and CCO; that the RC meets regularly, but no less than annually with the CRO; and that the TC meets regularly, but no less than annually with the CSO. Additionally, the revised Committee Charters will authorize the officers listed above, other than the CFO, to communicate directly with the Chairs of their respective Board Committees. The Commission finds that these changes to OCC's Committee Charters to clarify reporting lines of officers responsible for OCC's control and risk management functions, as described in sections I(4)(a), I(6)(a), and I(8) above, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>59</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent,

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<sup>58</sup> Id.

<sup>59</sup> Id.

among other things, to promote the effectiveness of the clearing agency's risk management procedures.

As noted above, OCC will revise certain Committee Charters regarding the reporting lines of the CRO, CAE, and CCO. Consistent with these changes, OCC will also revise the RC and AC Charters such that the RC will set compensation for the CRO, and the AC will set compensation for the CAE and CCO. Relatedly, OCC will amend the CPC Charter to remove a requirement that the CPC meet with the RC Chair or AC Chair in executive session regarding the compensation of the CRO, CAE, or CCO. As described above in sections I(4)(b), I(5)(a), and I(6)(c) above, these changes are intended to underscore the independence of the CRO, CAE, and CCO. The Commission finds that these changes are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>60</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to promote the effectiveness of the clearing agency's risk management procedures.

OCC is amending the AC Charter regarding the AC's responsibilities. The amended charter, among other things, will restate and revise the AC's responsibility for oversight of the external auditor and financial reporting; the Internal Audit department, Compliance department, and compliance related matters; and OCC's Chief Audit Executive and Chief Compliance Officer.

As described in greater detail in section I(4)(b) above, the amendments are intended to reinforce and expand upon the AC's oversight responsibilities, which should

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<sup>60</sup> Id.

support OCC's control framework. The Commission believes that the governance of OCC's control framework is important to OCC's overall functioning. Therefore, the Commission finds that the changes to the AC Charter to restate and revise the AC's responsibility for oversight of OCC's control functions and the officers responsible for managing such functions, as described above, are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>61</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to promote the effectiveness of the clearing agency's risk management procedures.

OCC is amending the CPC Charter regarding the CPC's responsibilities. Under the revised CPC Charter, among other things, the CPC will be responsible for assisting the Board with oversight of OCC's overall performance as well as capital and leadership planning, approving the goals and objectives of the Executive Chairman, and reviewing the compensation of the Management Committee. The amended CPC Charter will restate and revise the CPC's responsibility for oversight of OCC's Capital Plan; human resources and compensation programs; and employee benefit programs, including the monitoring of the Administrative Committee.

Under the revised CPC Charter, the CPC will also be responsible for providing periodic updates to the Board regarding CPC actions with respect to compensation, retirement, and employee welfare plans, financial position and performance of such plans, and adherence to investment guidelines. The Commission finds that changes to OCC's CPC Charter as described in detail in section I(5)(b) above are consistent with the

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<sup>61</sup> Id.

requirement in Rule 17Ad-22(d)(8)<sup>62</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to fulfill the public interest requirements of Section 17A of the Act applicable to clearing agencies, among other things, to support the objectives of owners and participants.

OCC is amending the RC Charter to clarify and expand the RC's responsibilities. Under the revised RC Charter, the RC will be responsible for coordinating with the other Committees to achieve comprehensive oversight of OCC's risk-related matters, among other things. The amended RC Charter will restate and revise the RC's responsibility for oversight of membership and margin requirements; OCC's Enterprise Risk Management program and risk tolerances; contingency planning and model risk management; the process for managing exposures to banks, depositories, financial market utilities, and trade sources as well as the process for managing liquidity needs; and management's handling of the Financial Risk Management group, review of OCC's risk reporting metrics, and identification of risk issues for escalation to the Board.

The amended RC Charter will also restate and revise the RC's responsibility for discussing, with management, the impact on systemic stability that could arise out of OCC's responses to extraordinary market events. The Commission finds that the changes to the RC Charter as described in detail in section I(5)(b) above clarify and expand the RC's responsibilities for coordination of risk-related matters, oversight of membership requirements and risk management, and discussion of the potential impact of OCC's responses to extraordinary market events, and are consistent with the requirement in Rule

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<sup>62</sup> Id.

17Ad-22(d)(8)<sup>63</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to promote the effectiveness of the clearing agency's risk management procedures.

#### **(5) Administrative Textual Changes**

OCC will make a number of textual changes to its governing documents that are not intended to change the meaning of those documents. Such changes include the following:

- As described in section I(2)(c) above, OCC will consolidate the current By-Law provisions describing its Board Committees. OCC will also add By-Law provisions to describe those Board Committees not currently described in the By-Laws.
- As described in section I(3)(a) above, OCC will revise the Board Charter, consistent with existing rules, to reflect an increase in the number of Public Directors on OCC's Board from three to five. As described in section I(3)(b) above, OCC will replace language in the Board Charter concerning the Board's obligations that duplicates language currently in OCC's By-Laws with a general statement that the Board will perform functions, as it believes necessary, or as prescribed by rules or regulation, and will reorganize section IV of the Board Charter. As described in section I(3)(c) above, OCC will remove the list of stakeholders from the introductory language of the Board

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<sup>63</sup> Id.

Charter, and will revise the language throughout the charter to recognize the TC.

- As described in greater detail in section I(3)(d) above, OCC will remove, from its Fitness Standards, descriptions of the categories of directors represented on the Board because they are maintained in Article III of the By-Laws.
- Across all of the charters, OCC will replace references to the “Performance Committee” and the “Governance Committee” with references to the “Compensation and Performance Committee” and “Governance and Nominating Committee,” respectively.
- In certain Committee Charters, OCC will add broad statements that encompass and replace current language concerning the respective Committee’s functions and responsibilities. The AC Charter will state that the AC oversees internal controls and compliance. OCC will remove language regarding review of the Corporate Plan and administration of compensation plans from the CPC charter. OCC will broaden the RC Charter description of the RC’s oversight of the clearing membership framework.
- As described in section I(4)(a), OCC will replace the term “independent accountant” with “external auditor” in the AC Charter. As described in section I(5)(a), OCC will reword the delegation of authority to the Administrative Committee in the CPC Charter. As described in section I(7), OCC will renumber sections in the first paragraph of the GNC Charter.
- As described in section I(6)(b), OCC will remove language from the RC Charter regarding the approval of non-U.S. institutions to issue letters of credit

because this language contradicts OCC's By-Laws. OCC will remove language from the TC Charter related to audit because that language was inadvertently carried-over from the AC Charter.

The Commission believes that the foregoing changes clarify the language of OCC's governing documents. The Commission finds that changes designed to clarify the language of a clearing agency's governing documents are consistent with the requirement in Rule 17Ad-22(d)(8)<sup>64</sup> that each registered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent, among other things, to support the objectives of owners and participants.

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<sup>64</sup>

Id.



III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of Act, and in particular, with the requirements of Section 17A of the Act and the rules and regulations thereunder.<sup>65</sup>

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>66</sup> that the proposed rule change (SR-OCC-2016-002), as modified by Amendment No. 1, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>67</sup>

Robert W. Errett  
Deputy Secretary

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<sup>65</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>66</sup> 15 U.S.C. 78s(b)(2).

<sup>67</sup> 17 CFR 200.30-3(a)(12).