

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-94304; File No. SR-OCC-2021-014)

February 24, 2022

Self-Regulatory Organizations; The Options Clearing Corporation; Order Granting Approval of Proposed Rule Change Concerning The Options Clearing Corporation's Cash and Investment Management

I. INTRODUCTION

On December 23, 2021, the Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change SR-OCC-2021-014 (“Proposed Rule Change”) pursuant to Section 19(b) of the Securities Exchange Act of 1934 (“Exchange Act”)¹ and Rule 19b-4² thereunder to (i) add OCC’s existing policy regarding cash and related investments to its Rules, and (ii) amend OCC’s Rules governing the use of Clearing Fund contributions to ensure access in the event of the failure of an investment counterparty with whom OCC has invested cash collateral.³ The Proposed Rule Change was published for public comment in the Federal Register on January 12, 2022.⁴ The Commission has received no

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Notice of Filing infra note 5, at 87 Fed. Reg. 1819.

⁴ Securities Exchange Act Release No. 93916 (Jan. 12, 2022), 87 Fed. Reg. 1819 (Jan. 12, 2022) (File No. SR-OCC-2021-014) (“Notice of Filing”). OCC also filed a related advance notice (SR-OCC-2021-803) (“Advance Notice”) with the Commission pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, entitled the Payment, Clearing, and Settlement Supervision Act of 2010 and Rule 19b-4(n)(1)(i) under the Exchange Act. 12 U.S.C. 5465(e)(1). 15 U.S.C. 78s(b)(1) and 17 CFR 240.19b-4, respectively. The Advance Notice was published in the Federal Register on January 12, 2022. Securities Exchange Act Release No. 93915 (Jan. 6, 2022), 87 Fed. Reg. 1814 (Jan. 12, 2022) (File No. SR-OCC-2021-803). A Notice of No Objection to the Advance Notice was published in the Federal Register on February

comments regarding the substance of the Proposed Rule Change.⁵ This order approves the Proposed Rule Change.

II. BACKGROUND⁶

OCC is proposing to add to its Rules a policy governing OCC's cash and investment practices (the "Cash and Investment Management Policy" or "Policy") and amend its Rules regarding access to Clearing Fund contributions to address the failure of an investment counterparty to return Clearing Member cash collateral.

A. Policy regarding cash and related investments

OCC's current rules include provisions governing the management and investment of both OCC's own funds and cash deposited by Clearing Members. Pursuant to its rules, OCC's Board of Directors ("Board") may invest funds in excess of the amount needed as working capital in Government securities or such other securities or financial instruments as the Board may from time to time approve.⁷ Further, OCC's rules allow it to invest in Government

23, 2022, 2022. See Securities Exchange Act Release No. 94270 (Feb. 17, 2022), 87 Fed. Reg. 10262 (Feb. 23, 2022) (File No. SR-OCC-2021-803).

⁵ The Commission received no comments on the Proposed Rule Change; however, since the Proposed Rule Change was also filed as an advance notice, all public comments received on the proposal are considered regardless of whether the comments are submitted on the Proposed Rule Change or the Advance Notice. The Commission received a comment letter on the Advance Notice that addressed market conduct generally; however, additional discussion is unnecessary because the substance of the letter does not bear on the basis for the Commission's decision to approve the Proposed Rule Change. Comments on the Advance Notice are available at <https://www.sec.gov/comments/sr-occ-2021-803/srocc2021803.htm>.

⁶ Capitalized terms used but not defined herein have the meanings specified in OCC's Rules and By-Laws, available at <https://www.theocc.com/about/publications/bylaws.jsp>.

⁷ See By-Law Art. IX, Sec. 1.

securities cash that it receives and holds from Clearing Members' margin requirements and Clearing Fund contributions.⁸ OCC proposes to add its Cash and Investment Management Policy to its current investment related rules.⁹

The proposed Cash and Investment Management Policy will build on OCC's existing Rules by (i) outlining the safeguarding standards for cash and related investments managed by OCC to minimize credit and liquidity risk, and (2) providing guidelines for investments permitted by OCC's Rules as described above. With regard to safeguarding cash, the Policy would allow OCC to hold OCC Cash¹⁰ and Clearing Member Cash¹¹ in demand deposit accounts with commercial banks or in accounts at a Federal Reserve Bank. Consistent with

⁸ See OCC Rule 604(a); Rule 1006(c).

⁹ See Notice of Filing, 87 Fed. Reg. at 1820.

¹⁰ Under the proposed Policy, OCC Cash would include working capital related to future operating costs, inclusive of financial resources held to meet liquidity and resiliency requirements, proceeds from lines of credit, if any, maintained to support OCC's working capital, and investments made with OCC Cash. OCC Cash would also include OCC's Minimum Corporate Contribution. See Securities Exchange Act Release No. 92038 (May 27, 2021), 86 Fed. Reg. 29861 (Jun. 3, 2021) (File No. SR-OCC-2021-003) (establishing a persistent minimum level of OCC's own capital that it would contribute to default losses or liquidity shortfalls prior to allocating a default loss to the Clearing Fund contributions of non-defaulting Clearing Members). OCC Cash would not include cash held in respect of OCC's pension plan, post-retirement welfare plan, or other deferred compensation plans.

¹¹ Under the proposed Policy, Clearing Member Cash would include cash collateral deposited as margin or Clearing Fund contributions, cash held in liquidating settlement accounts for suspended Clearing Members pursuant to OCC's Rule 1104, and investments made with Clearing Member Cash. Clearing Member Cash would also include proceeds from OCC's syndicated credit facility and liquidity facilities. See Securities Exchange Act Release No. 88971 (May 28, 2020), 85 Fed. Reg. 34257 (Jun. 3, 2020) (File No. SR-OCC-2020-804) (discussing OCC's revolving credit facility); Securities Exchange Act Release No. 89039 (Jun. 10, 2020), 85 Fed. Reg. 36444 (Jun. 16, 2020) (File No. SR-OCC-2020-803) (discussing OCC's non-bank liquidity facility).

OCC's current Rules, the Policy would require OCC to move all margin and Clearing Fund cash related to a suspended Clearing Member into a liquidating settlement account for use in meeting the obligations of the Clearing Member.¹² The Policy would also require that OCC employ a bank account structure that segregates customer funds per applicable regulatory requirements¹³ and OCC's By-Laws and Rules.¹⁴

With regard to investments, the Policy would provide that OCC's investment strategy is to preserve principal and maintain adequate liquidity. OCC outlines its specific investments in internal procedures, but will publish its investment strategy in its Qualitative Disclosures posted to OCC's public website.¹⁵ Under the proposed Policy, OCC will invest only with counterparties that meet the financial and operational standards outlined in OCC's procedures concerning its banking relationships.¹⁶

The Policy would affirm OCC's current practice of not investing Clearing Fund cash, which is instead maintained in accounts at a Federal Reserve Bank or a commercial bank. The

¹² See OCC Rule 1104.

¹³ See 17 CFR 39.15 (requiring a derivatives clearing organization to comply with the segregation requirements section 4d of the Commodity Exchange Act).

¹⁴ See OCC By-Laws Art. VI, Sec. 3(f) (providing for maintenance of segregated futures accounts).

¹⁵ OCC's Qualitative Disclosures are available at <https://www.theocc.com/Risk-Management/PFMI-Disclosures>.

¹⁶ Additionally, OCC's Third-Party Risk Management Framework describes the basis for evaluating financial institutions based on financial resources and operational capacity, such as whether a relationship is structured to allow prompt access to assets and whether a custodian is a supervised and regulated institution that adheres to generally accepted accounting practices, maintains safekeeping procedures, and has controls that fully protect these assets. See Securities Exchange Act Release No. 90797 (Dec. 23, 2021), 85 Fed. Reg. 86592, 86593 (Dec. 30, 2021).

Policy would also limit the investment of margin cash to instruments that provide liquidity to OCC by the following business day. In contrast, the Policy would not limit the investment of OCC cash in excess of 110 percent of its Target Capital Requirement¹⁷ to overnight transactions. Further, the Policy would require procedures to ensure that end-of-day margin cash balances remain above the aggregate level of any Required Cash Deposits to support OCC's management of liquidity risk.¹⁸ Under the Policy, interest or gain received on investments will belong to OCC except as otherwise provided for in OCC's Rules.¹⁹

B. Access to Clearing Fund Contributions

OCC's current Rules define the conditions under which OCC may use Clearing Fund assets to make good losses or expenses suffered by OCC or by the Clearing Fund with regard to borrowings made by OCC.²⁰ OCC's Rules also define the conditions under which OCC may borrow Clearing Fund assets.²¹ OCC's Rules address OCC's authority to access Clearing Fund

¹⁷ OCC's Target Capital Requirement is the amount of shareholders' equity recommended by OCC management and approved by the Board to ensure compliance under both the Commission and Commodity Futures Trading Commission rules and to keep such additional amount the Board may approve for capital expenditures. See OCC Rule 101(T)(1).

¹⁸ Under its Liquidity Risk Management Framework, OCC may require a Clearing Member Group to post cash collateral to supplement OCC's Available Liquidity Resources when stressed liquidity demands for that Clearing Member Group are above established thresholds or until the settlement demand is met. See Exchange Act Release No. 89014 (Jun. 4, 2020), 85 Fed. Reg. 35446, 35449 (Jun. 10, 2020) (File No. SR-OCC-2020-003).

¹⁹ See e.g., Securities Exchange Act Release No. 82502 (Jan. 12, 2018), 82 Fed. Reg. 2825, 2826 (Jan. 19, 2018) (File No. SR-OCC-2017-009) (stating that OCC would pass interest income earned on Clearing Fund cash deposited at a Federal Reserve Bank through to its Clearing Members).

²⁰ See OCC Rule 1006(a) and (c).

²¹ See OCC Rule 1006(f).

assets related to the failure of a bank or clearing organization to perform its obligations to OCC, but not the failure of an investment counterparty. OCC proposes a series of changes to its Rules, described below, to broaden OCC's authority to access Clearing Fund assets to address the potential failure of an investment counterparty to meet its obligations to OCC.

OCC proposes to amend its Rules 1006(a) and (c) to add "investment counterparty" to the list of counterparties whose failure to perform any obligation to OCC when due because of its bankruptcy, insolvency, receivership, suspension of operations, or any similar event that causes OCC to sustain a loss. OCC also proposes to amend its Rule 1006(f) to authorize OCC to take possession of cash or securities deposited by Clearing Members as contributions to the Clearing Fund and securities in which the OCC has invested Clearing Fund cash contributions if OCC reasonably believes it necessary to borrow to meet its liquidity needs for same-day settlement as a result of the failure of an investment counterparty. However, the proposed changes to Rules 1006(a), (c), and (f) would limit access to failures with respect to cash invested under Rules 604(a) and 1002(c), which deal with margin cash and Clearing Fund cash contributions, respectively.

OCC is also proposing to restate and reorganize Rule 1006(f), which currently consists of a single paragraph, into four subparagraphs with the following headings: (1) Conditions; (2) Uses; (3) Term; Clearing Fund Charge; and (4) Substitution Requests. To eliminate a potential inconsistency with Rule 1006(c), OCC would revise the condition triggering OCC's access to the Clearing Fund from failure "to achieve daily settlement" to failure "to perform any obligation to the Corporation when due." The proposed changes to 1006(f) also include the removal of a gendered pronoun and other administrative changes.

III. DISCUSSION AND COMMISSION FINDINGS

Section 19(b)(2)(C) of the Exchange Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Exchange Act and the rules and regulations thereunder applicable to such organization.²² After carefully considering the Proposed Rule Change, the Commission finds that the proposal is consistent with the requirements of the Exchange Act and the rules and regulations thereunder applicable to OCC. More specifically, the Commission finds that the proposal is consistent with Section 17A(b)(3)(A) of the Exchange Act,²³ and Rule 17Ad-22(e)(13)²⁴ and Rule 17Ad-22(e)(16)²⁵ thereunder, as described in detail below.

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

Section 17A(b)(3)(F) of the Exchange Act requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions as well as to ensure the safeguarding of securities and funds which are in the custody or control of the clearing agency.²⁶ Based on its review of the record, and for the reasons described below, the Commission finds the proposal is consistent with Section 17A(b)(3)(F) of the Exchange Act.

²² 15 U.S.C. 78s(b)(2)(C).

²³ 15 U.S.C. 78q-1(b)(3)(A).

²⁴ 17 CFR 240.17Ad-22(e)(13).

²⁵ 17 CFR 240.17Ad-22(e)(16).

²⁶ 15 U.S.C. 78q-1(b)(3)(F).

The Commission believes that the proposed adoption of the Cash and Investment Management Policy would be consistent with the the safeguarding of securities and funds because the proposed changes would build on OCC's current Rules for managing cash and investments. The Policy, which OCC proposes to add to its Rules, includes standards for safeguarding OCC Cash and Clearing Member Cash through the application of OCC's counterparty standards, such as allowing OCC Cash and Clearing Member Cash to be deposited only in a Federal Reserve Bank or in demand deposit accounts with institutions that meet the standards set out in OCC's current risk management strategy to minimize the risk of loss or delay in access to such funds. Further, to support OCC's liquidity risk management practices, the Policy includes limitations on the permitted tenure of investments. The Commission believes, therefore, that adding the Policy to OCC's Rules is consistent with the safeguarding of securities and funds in OCC's custody or control.

The Commission believes that the proposed changes to broaden OCC's authority to access Clearing Fund contributions are consistent with promoting the prompt and accurate clearance and settlement of securities transactions. The proposed changes will increase OCC's authority to access Clearing Fund contributions to address losses or shortfalls arising out of the failure of an investment counterparty to perform with regard to investments, margin cash or Clearing Fund cash. In the event that a counterparty with whom OCC has invested Clearing Member Cash has failed, the proposed rule change is designed to allow OCC to access the Clearing Fund to meet OCC's payment obligations. Ensuring that OCC is able to meet its payment obligations would, in turn, reduce the likelihood of a disruption to the timely settlement of derivatives contracts and related transactions, such as the payment of premiums or cash settlements arising out of exercise and assignment activities. The Commission believes,

therefore, that allowing OCC access to the Clearing Fund contributions in the event of a failure of an investment counterparty would promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions.

The Commission believes, therefore, that the proposal to add OCC's policy regarding cash and related investments to its Rules, and amend OCC's Rules governing the use of Clearing Fund contributions to ensure access in the event of the failure of an investment counterparty with whom OCC has invested cash collateral, is consistent with the requirements of Section 17A(b)(3)(F) of the Exchange Act.²⁷

B. Consistency with Rule 17Ad-22(e)(13) under the Exchange Act

Rule 17Ad-22(e)(13) under the Exchange Act requires, among other things, that a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to ensure the covered clearing agency has the authority to take timely action to contain losses and liquidity demands and continue to meet its obligations.²⁸

As the Commission has observed previously, OCC relies on the resources in its Clearing Fund to manage the potential losses arising out of the default of a Clearing Member under extreme but plausible market conditions.²⁹ OCC also relies on such resources to manage potential liquidity shortfalls arising out of the default of a Clearing Member under extreme but

²⁷ 15 U.S.C. 78q-1(b)(3)(F).

²⁸ 17 CFR 240.17Ad-22(e)(13).

²⁹ See Securities Exchange Act Release No. 87717 (Dec. 11, 2019), 84 Fed. Reg. 68985, 68987 (Dec. 17, 2019) (File No. SR-OCC-2019-009).

plausible market conditions.³⁰ In the event of a Clearing Member default, unless it has access to the Clearing Fund contributions of non-defaulting Clearing Members, OCC's inability to access the defaulter's cash collateral due to the failure of an investment counterparty could inhibit OCC's ability to contain losses and liquidity demands. The Commission also believes that the proposed changes to restate and reorganize Rule 1006(f) would enhance the rule's clarity, and therefore help ensure OCC's authority to access Clearing Fund contributions to address losses or shortfalls arising out of the failure of an investment counterparty to perform with regard to investments of margin cash or Clearing Fund cash.

The Commission believes, therefore, that the proposed changes to broaden OCC's authority to access to Clearing Fund contributions are consistent with Rule 17Ad-22(e)(13) under the Exchange Act.³¹

C Consistency with Rule 17Ad-22(e)(16) under the Exchange Act

Rule 17Ad-22(e)(16) under the Exchange Act requires that a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to safeguard its own and its participants' assets, minimize the risk of loss and delay in access to these assets, and invest such assets in instruments with minimal credit, market and liquidity risks.³² In adopting Rule 17Ad-22(e)(16), the Commission provided guidance for consideration

³⁰ See Securities Exchange Act Release No. 89014 (Jun. 4, 2020), 85 Fed. Reg. 35446, 35450 (Jun. 10, 2020) (File No. SR-OCC-2020-003) (stating that cash contributions to the Clearing fund serve as an important source of liquidity and that non-cash contributions provide a source of collateral necessary for OCC to access sources of liquidity).

³¹ 17 CFR 240.17Ad-22(e)(13).

³² 17 CFR 240.17Ad-22(e)(16).

by covered clearing agencies.³³ Such guidance included the consideration of whether a covered clearing agency's investment strategy is consistent with its overall risk management strategy and fully disclosed to participants.³⁴

The Commission believes that the proposed Cash and Investment Management Policy would support and enhance OCC's current Rules regarding the investment of its and its participants' cash assets. As described above, the Policy outlines safeguarding standards, such as allowing OCC Cash and Clearing Member cash to be deposited only in a Federal Reserve Bank or in demand deposit accounts with institutions that meet the standards set out in OCC's current risk management strategy (e.g., OCC's Third Party Risk Management Framework) to minimize the risk of loss or delay in access to such funds. The Commission believes further that limiting the investment of cash to Government Securities, and specifically limiting the investment of Clearing Member Cash to instruments that provide liquidity to OCC by the following business day, is consistent with investing in assets with minimal credit, market, and liquidity risks.³⁵

The Commission believes, therefore, that the addition of the Cash and Investment Management Policy to OCC's Rules is consistent with Rule 17Ad-22(e)(16) under the Exchange Act.³⁶

³³ Covered Clearing Agency Standards, 81 Fed. Reg. at 70837.

³⁴ Id.

³⁵ The Policy would allow OCC to invest its own cash in longer-tenured instruments only where such cash is in excess of 110 percent of OCC's Target Capital Requirement.

³⁶ 17 CFR 240.17Ad-22(e)(16).

IV. CONCLUSION

On the basis of the foregoing, the Commission finds that the Proposed Rule Change is consistent with the requirements of the Exchange Act, and in particular, the requirements of Section 17A of the Exchange Act³⁷ and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Exchange Act,³⁸ that the Proposed Rule Change (SR-OCC-2021-014) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³⁹

Jill M. Peterson
Assistant Secretary

³⁷ In approving this Proposed Rule Change, the Commission has considered the proposed rules' impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

³⁸ 15 U.S.C. 78s(b)(2).

³⁹ 17 CFR 200.30-3(a)(12).