

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-94542; File No. SR-OCC-2022-003)

March 29, 2022

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change by The Options Clearing Corporation Concerning Cash-Settled FLEX ETF Options.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act” or “Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on March 16, 2022, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

This proposed rule change would amend various provisions of the OCC By-Laws and Rules to accommodate the issuance, clearance and settlement of flexibly structured options on exchange-traded funds (“fund shares” or “ETFs”) that are cash settled (“Cash Settled Flex ETF Options”). The proposed changes to OCC’s By-Laws and Rules are contained in Exhibits 5A and 5B to file number SR-OCC-2022-003, respectively. Material proposed to be added to OCC’s By-Laws and Rules as currently in effect is marked by underlining, and material proposed to be deleted is marked with strikethrough

---

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

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

text. All terms with initial capitalization that are not otherwise defined herein have the same meaning as set forth in the By-Laws and Rules.<sup>3</sup>

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

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

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

(1) Purpose

The NYSE American Exchange ("NYSE American") received approval to list Cash Settled Flex ETF Options as a variation of currently-traded, physically-settled equity flex options.<sup>4</sup> Cash Settled Flex ETF Options will generally have characteristics of physically settled equity flexes; however, exercises and assignments will settle in cash (as opposed to physical settlement), with the settlement amount based on the difference between the underlying price on the date of exercise and the strike price of the exercised option.

---

<sup>3</sup> OCC's By-Laws and Rules can be found on OCC's public website: <https://www.theocc.com/Company-Information/Documents-and-Archives/By-Laws-and-Rules>.

<sup>4</sup> See Securities Exchange Act Release No. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAMER-2019-38).

OCC does not currently settle equity options in cash unless (i) the underlying security undergoes a corporate action resulting in the conversion of the option deliverable to only cash or (ii) the underlying security is otherwise unavailable for delivery.<sup>5</sup> Since OCC does not currently settle equity options in cash except for in rare circumstances, OCC's By-Laws and Rules are drafted on the premises that (i) all equity options are physically settled options; and (ii) certain provisions apply to physically settled options and certain provisions apply to cash settled options. To accommodate the Cash Settled Flex ETF Option product, OCC must revise its By-Laws and Rules to establish the following as further described below: (i) Cash Settled Flex ETF Options settle in cash; (ii) the distinction between Cash Settled Flex ETF Options and physically settled options on the same underlying security; (iii) certain provisions that currently apply only to physically settled options will also apply to Cash Settled Flex ETF Options; and (iv) specific deposits would not be allowed as collateral for Cash Settled Flex ETF Options.

### **Revisions to Distinguish Cash Settled Flex ETF Options from Physically Settled Options**

OCC proposes the following modifications to its By-Laws to emphasize the distinction between physically settled flexibly structured options and Cash Settled Flex ETF Options.

- Article I (Definitions), Section 1(F)(8). OCC is proposing to revise the definition of "Flexibly Structured Option" to (i) emphasize that such options may be physically settled or cash settled depending on the listing exchange's

---

<sup>5</sup> See OCC By-Laws Article VI, Section 11A, Interpretations and Policies .05 and Article VI, Section 19(c).

rules and (ii) clarify that Cash Settled Flex ETF Options would not be fungible with physically settled flexibly structured options and would not be consolidated with standard options listed after a flexibly structured option with the same strike, expiration date, and underlying security, as is the case with a physically settled flexibly structured option that is fungible.

- Article I (Definitions), Section 1(S)(12). OCC proposes to revise the definition of “Series” to state that the options of the same series have the same settlement method.
- Article I (Definitions), Section 1(V)(1). OCC proposes to revise the definition of “Variable Terms” to recognize that in addition to the variable terms itemized in the definition, flexibly structured options on fund shares may be either physically or cash settled.
- Article XVII (Index Options and Certain Other Cash-Settled Options), Introduction. OCC proposes to revise the introduction to add flexibly structured options that cash settle to the list of options for which Article XVII of the By-Laws applies.
- Article XVII (Index Options and Certain Other Cash-Settled Options), Section 1(C)(4). OCC proposes to revise the definition of “Class of Options” to state that flexibly structured options that cash settle shall constitute a different class of options from physically settled options on the same underlying interest.

## **Revisions to Apply Certain Provisions for Physically Settled Options to, and Exclude the Application of Certain Provisions for Index Options and other Cash Settled Options from, Cash Settled Flex ETF Options**

OCC also proposes the following modifications to its By-Laws and Rules to emphasize the application of certain provisions that otherwise apply only to physically settled options and to exclude application of certain provisions that otherwise would apply to all cash settled options.

- Article I (Definitions), Section 1(C)(15). OCC proposes to revise the definition of “Clearing Member” to clarify that a Clearing Member is not an “Index Clearing Member” solely by virtue of being approved to clear Cash Settled Flex ETF Options.
- Article I (Definitions), Section 1(R)(5). OCC currently defines “Reporting Authority” when used with respect of any cash-settled contract to mean the source that OCC uses as the official source for the current price or value of the underlying interest. OCC would revise this definition to emphasize that the reporting for Cash Settled Flex ETF Options will be the same source used by OCC for physically settled equity options with the same underlying interest. This change is designed to facilitate the use of the same closing price for automatic exercise determinations on both physically settled and cash settled options with the same underlying security, thereby ensuring that expiration processing for a Cash Settled Flex ETF Option will align with expiration processing for a physically settled product on the same underlying security.
- Article XVII (Index Options and Certain Other Cash-Settled Options), Section 1(R)(3). “Reporting Authority” is also defined in Article XVII for index and

certain other cash settled options. OCC proposes to revise this definition to explicitly exclude Cash Settled Flex ETF Options and to emphasize that the reporting authority for Cash Settled Flex ETF Options is the same source used by OCC for physically settled equity options.

- Article XVII (Index Options and Certain Other Cash-Settled Options), Sections 3(a) and 3(h). This provision currently states that the adjustment provisions of Article VI, Section 11A do not apply to cash settled equity contracts. Since adjustment decisions for Cash Settled Flex ETF Options and physically settled options on the same underlying should be the same, OCC is proposing to add language to this section to state explicitly that Article VI, Section 11A of the By-Laws applies to Cash Settled Flex ETF Options.

#### **Revisions Unique to the Nature of Cash Settled Flex ETF Options**

Finally, OCC proposes to revise the following By-Laws and Rules to accommodate unique characteristics of Cash Settled Flex ETF Options.

- Article XVII (Index Options and Certain Other Cash-Settled Options), Section 4(a)(2). This provision states the method by which the exercise settlement amount for exercised contracts of an affected series is fixed for index options and certain other cash-settled options. OCC proposes to add a sentence to this provision to state that the exercise settlement amount for Cash Settled Flex ETF Options shall be determined by using the last reported sale price for the underlying security during regular trading hours. This is consistent with the expiration closing price determination for physically settled options in Rule 805.

- Chapter VI (Margins), Rule 610 (Deposits in Lieu of Margin). Rule 610 allows for Clearing Members to use specific deposits of the underlying security as collateral to short customer positions on a call option. Specific deposits allow a short call position to be fully covered because the security that will need to be delivered if the call option writer is assigned is pledged to OCC for the purpose of covering the short position. OCC proposes to modify Rule 610 to disallow specific deposits for Cash Settled Flex ETF Options because such options do not require delivery of the underlying security upon assignment. Consequently, a specific deposit of the underlying security will not cover the delivery requirement of Cash Settled Flex ETF Options as it does for a physically settled option. OCC would, however, allow escrow deposits to be made for Cash Settled Flex ETF Options.
- Chapter VIII (Exercise and Assignment), Rule 805 (Expiration Exercise Procedure) and Chapter XVIII (Index Options and Certain Other Cash Settled Options), Rule 1804 (Expiration Exercise Procedure for Cash-Settled Options). Rule 805(j) states that the “closing price” used for any underlying security in Rule 805 is the last reported sale price for the underlying security during regular trading hours (as determined by OCC) on the trading day immediately preceding the expiration date, or on the expiration date if the expiration date is a trading day, on such national securities exchange or other domestic securities market as OCC shall determine. OCC is proposing to revise Rule 805(j) to state explicitly that the same definition of “closing price” applies to underlying securities for Cash Settled Flex ETF Options. Rule

1804 generally provides for the expiration exercise procedure for cash-settled options. OCC is proposing to add an interpretation and policy to Rule 1804 to clarify that, notwithstanding its general application to cash-settled options, the determination of the closing price for an underlying security of a flexibly structured cash settled equity option is the same as the determination of the closing price per Rule 805(j).

- Chapter XVIII (Index Options and Certain Other Cash Settled Options), Rule 1804 (Expiration Exercise Procedure for Cash Settled Options). OCC proposes to revise Rule 1804(a) and Rule 1804(b) to state that Cash Settled Flex ETF Options will be deemed exercised on expiration if the strike price is \$0.01 or more in-the-money in accordance with the provisions of Rule 805(d). This will ensure that the threshold used for automatic exercises of Cash Settled Flex ETF Options will be the same as the threshold established for physically settled equity options rather than the \$1.00 per contract threshold established in Rule 1804.
- Chapter VIII (Exercise and Assignment) Rule 805 (Expiration Exercise Procedure) I&P.03 and Chapter XVIII (Index Options and Certain Other Cash Settled Options), Rule 1804 (Expiration Exercise Procedure for Cash Settled Options). Rule 805, interpretation and policy .03 states that the exercise procedures set forth in Rule 805 apply to flexibly structured equity options. OCC proposes to add language excepting from application of Rule 805(d) American-style Cash Settled Flex ETF Options subject to delayed settlement for any deliverable component. Similarly, OCC is proposing to add language



to Rule 1804(a) to state explicitly that Rule 805(d) does not apply to American-style Cash Settled Flex ETF Options that have a deliverable component subject to delayed settlement. These changes are necessary because any such option with a pended delivery component on its expiration date should not be automatically exercised, as the total value of the option deliverable can only be estimated. OCC anticipates this outcome would be rare, and likely the result of a contract adjustment that involves cash in lieu of fractional shares that have yet to be finalized on an option's an expiration date.

(2) Statutory Basis

Section 17A(b)(3)(F) of the Act<sup>6</sup> 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. OCC believes the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act<sup>7</sup> because it is designed to promote prompt and accurate clearance and settlement of securities transactions in flexibly structured options. The proposed rule change accomplishes this by maintaining consistency between OCC's By-Laws and Rules and NYSE American's rules as applied to the clearance and settlement of Cash Settled Flex ETF Options. Because Cash Settled Flex ETF Options are fundamentally unique from currently listed flexibly structured equity options, OCC By-Laws and Rules

---

<sup>6</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>7</sup> 15 U.S.C. 78q-1.

must provide for two different types of settlement methods for flexibly structured options with ETFs as the underlying securities to provide clearance and settlement of Cash Settled Flex ETF Options. The proposed changes are necessary to make explicit the differences between Cash Settled Flex ETF Options and physically settled options on the same underlying ETF, and will allow OCC to issue, clear, and settle Cash Settled Flex ETF Options in alignment with exchange rules for this product type. Accordingly, OCC believes the proposed rule change is designed to promote the prompt and accurate clearance and settlement of securities and derivatives transactions in accordance with Section 17A(b)(3)(F) of the Act.<sup>8</sup>

In addition, the proposed rule change is not inconsistent with the existing By-Laws and Rules of OCC, including any rules proposed to be amended.

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

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

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

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

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds

---

8

Id.

such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

OCC shall post notice on its website of proposed changes that are implemented.

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

#### IV. Solicitation of Comments

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

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-OCC-2022-003 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Vanessa Countryman, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-OCC-2022-003. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The

Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at <https://www.theocc.com/Company-Information/Documents-and-Archives/By-Laws-and-Rules>.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-OCC-2022-003 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

J. Matthew DeLesDernier  
Assistant Secretary

---

<sup>9</sup> 17 CFR 200.30-3(a)(12).