

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-94900; File No. SR-OCC-2022-001)

May 12, 2022

Self-Regulatory Organizations; Options Clearing Corporation; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change Concerning The Options Clearing Corporation's Margin Methodology for Incorporating Variations in Implied Volatility

I. Introduction

On January 24, 2022, the Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change SR-OCC-2022-001 (“Proposed Rule Change”) pursuant to Section 19(b) of the Securities Exchange Act of 1934 (“Exchange Act”)¹ and Rule 19b-4² thereunder to change quantitative models related to certain volatility products.³ The Proposed Rule Change was published for public comment in the Federal Register on February 11, 2022.⁴ The Commission has received comments regarding the Proposed Rule Change.⁵

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Notice of Filing infra note 4, at 87 Fed. Reg. 8072.

⁴ Securities Exchange Act Release No. 94165 (Feb. 7, 2022), 87 Fed. Reg. 8072 (Feb. 11, 2022) (File No. SR-OCC-2022-001) (“Notice of Filing”). OCC also filed a related advance notice (SR-OCC-2022-801) (“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 February 11, 2022. Securities Exchange Act Release No. 94166 (Feb. 7, 2022), 87 Fed. Reg. 8063 (Feb. 11, 2022) (File No. SR-OCC-2022-801).

⁵ Comments on the Proposed Rule Change are available at <https://www.sec.gov/comments/sr-occ-2022-001/srocc2022001.htm>. Since the proposal contained in the Proposed Rule Change was also filed as an advance

On March 24, 2022, pursuant to Section 19(b)(2) of the Exchange Act,⁶ the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the Proposed Rule Change.⁷ This order institutes proceedings, pursuant to Section 19(b)(2)(B) of the Exchange Act,⁸ to determine whether to approve or disapprove the Proposed Rule Change.

II. Summary of the Proposed Rule Change

OCC is a central counterparty (“CCP”), which means it interposes itself as the buyer to every seller and seller to every buyer for financial transactions. As the CCP for the listed options markets in the U.S., as well as for certain futures, OCC is exposed to the risk that one or more of its members may fail to make a payment or to deliver securities. OCC addresses such exposures, in part, by requiring its members to provide collateral, including margin collateral. Margin is the collateral that CCPs, like OCC, collect to cover potential changes in a member’s positions over a set period of time. Typically, margin is designed to cover such exposures during normal market conditions, which means that margin collateral should be sufficient to exposures at least 99 out of 100 days.

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.

⁶ 15 U.S.C. 78s(b)(2).

⁷ Securities Exchange Act Release No. 94165 (Feb. 7, 2022), 87 Fed. Reg. 8072 (Feb. 11, 2022) (File No. SR-OCC-2022-001).

⁸ 15 U.S.C. 78s(b)(2)(B).

Margin requirements may fluctuate from day to day; however, CCPs seek to reduce fluctuations that could otherwise impose systemic risk. For example, if a CCP collects too little margin during relatively stable market conditions, then it would need to collect significantly more margin during stressed market conditions. Margin requirements that are strongly reactive to market movements are considered to be “procyclical.” By contrast, a CCP may collect slightly more margin during quiet times to reduce the additional strain it places on members during times of market stress.

OCC’s process for setting margin requirements considers several distinct risk factors, including volatility. OCC’s current models for estimating the impact of volatility on member positions have a number of limitations that may result in procyclical margin requirements. OCC is proposing to change its models to reduce the level of procyclicality in its margin requirements caused by changes in volatility. The changes OCC is proposing would also provide for offsets between products based on the same underlying asset. Based on data provided by OCC, the proposed model changes would likely increase margin requirements slightly overall, which, in turn, would reduce the additional amount of margin OCC would need to collect during periods of market stress.

The proposed changes to OCC’s models are a continuation of volatility model changes that OCC has implemented over the past several years. In 2015, the Commission approved OCC’s proposal to more broadly incorporate variations in implied volatility in OCC’s margin methodology.⁹ In 2018, OCC modified its implied volatility model to address issues highlighted by large spikes in volatility.

⁹ See Securities Exchange Act Release No. 76781 (Dec. 28, 2015), 81 Fed. Reg. 135 (Jan. 4, 2016) (File No. SR-OCC-2015-016).

As described in the Notice of Filing,¹⁰ OCC proposes to change three quantitative models related to certain volatility products. Specifically, OCC proposes the following changes:

- (1) implement a new model for incorporating variations in implied volatility within OCC's margin methodology for products based on the S&P 500 Index;
- (2) implement a new model to margin futures on volatility indexes;¹¹ and
- (3) replace OCC's model to for margining variance futures.¹²

III. Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Exchange Act¹³ to determine whether the Proposed Rule Change should be approved or disapproved. Institution of proceedings is appropriate at this time in view of the legal and policy issues raised by the Proposed Rule Change. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, the Commission seeks and encourages interested persons to comment on the Proposed Rule Change, providing the Commission with arguments to support the Commission's analysis as to whether to approve or disapprove the Proposed Rule Change.

¹⁰ See Notice of Filing, supra note 4.

¹¹ A volatility index is an index designed to measure the volatiles implied by the prices of options on an underlying index.

¹² A variance future is an exchange-traded futures contract based on the expected realized variance of an underlying interest.

¹³ 15 U.S.C. 78s(b)(2)(B).

Pursuant to Section 19(b)(2)(B) of the Exchange Act,¹⁴ the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of, and input from commenters with respect to, the Proposed Rule Change's consistency with Section 17A of the Exchange Act,¹⁵ and the rules thereunder, including the following provisions:

- Section 17A(b)(3)(F) of the Exchange Act,¹⁶ which requires, among other things, that the rules of a clearing agency must be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible; and
- Rule 17Ad-22(e)(2) under the Exchange Act,¹⁷ which requires a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that, among other things, (1) are clear and transparent,¹⁸ (2) clearly prioritize the safety and efficiency of the covered clearing agency,¹⁹ and (3) support the public interest requirements in Section 17A of the Exchange Act (15 U.S.C. 78q-1) applicable to clearing agencies, and the objectives of owners and participants.²⁰

¹⁴ Id.

¹⁵ 15 U.S.C. 78q-1.

¹⁶ 15 U.S.C. 78q-1(b)(3)(F).

¹⁷ 17 CFR 240.17Ad-22(e)(2).

¹⁸ 17 CFR 240.17Ad-22(e)(2)(i).

¹⁹ 17 CFR 240.17Ad-22(e)(2)(ii).

²⁰ 17 CFR 240.17Ad-22(e)(2)(iii).

- Rule 17Ad-22(e)(3) under the Exchange Act,²¹ which requires a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the covered clearing agency, which, among other things, includes risk management policies, procedures, and systems designed to identify, measure, monitor, and manage the range of risks that arise in or are borne by the covered clearing agency, that are subject to review on a specified periodic basis and approved by the board of directors annually.²²
- Rule 17Ad-22(e)(4) under the Exchange Act,²³ which requires a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes.
- Rule 17Ad-22(e)(6) under the Exchange Act,²⁴ which requires a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to cover, if the covered clearing agency provides central counterparty services, its credit exposures to its participants by

²¹ 17 CFR 240.17Ad-22(e)(3).

²² 17 CFR 240.17Ad-22(e)(3)(i).

²³ 17 CFR 240.17Ad-22(e)(4).

²⁴ 17 CFR 240.17Ad-22(e)(6).

establishing a risk-based margin system that, among other things, (1) considers, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market²⁵ (2) calculates sufficient margin to cover its potential future exposure to participants in the interval between the last margin collection and the close out of positions following a participant default;²⁶ and uses an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products.²⁷

- Rule 17Ad-22(e)(23) under the Exchange Act,²⁸ which requires a covered clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for, among other things, sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency.²⁹

IV. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the Proposed Rule Change. In particular, the Commission invites the written views of interested persons concerning whether the

²⁵ 17 CFR 240.17Ad-22(e)(6)(i).

²⁶ 17 CFR 240.17Ad-22(e)(6)(iii).

²⁷ 17 CFR 240.17Ad-22(e)(6)(v).

²⁸ 17 CFR 240.17Ad-22(e)(23).

²⁹ 17 CFR 240.17Ad-22(e)(23)(ii).

Proposed Rule Change is consistent with Section 17A(b)(3)(F) of the Exchange Act,³⁰ Rule 17Ad-22(e)(6) under the Exchange Act,³¹ or any other provision of the Exchange Act, or the rules and regulations thereunder. Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4(g) under the Exchange Act,³² any request for an opportunity to make an oral presentation.³³

Interested persons are invited to submit written data, views, and arguments regarding whether the Proposed Rule Change should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register].

The Commission asks that commenters address the sufficiency of OCC's statements in support of the Proposed Rule Change, which are set forth in the Notice of Filing,³⁴ in addition to any other comments they may wish to submit about the Proposed Rule Change.

³⁰ 15 U.S.C. 78q-1(b)(3)(F).

³¹ 17 CFR 240.17Ad-22(e)(6).

³² 17 CFR 240.19b-4(g).

³³ Section 19(b)(2) of the Exchange Act grants to the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

³⁴ See Notice of Filing, supra note 4.

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. Please include File Number SR-OCC-2022-001 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2022-001. 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-2022-001 and should be submitted on or before [insert date 21 days from publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³⁵

J. Matthew DeLesDernier
Assistant Secretary

³⁵ 17 CFR 200.30-3(a)(31).