

THE OPTIONS CLEARING CORPORATION

ONE N. WACKER DRIVE, SUITE 600, CHICAGO, ILLINOIS 60606

WILLIAM H. NAVIN

EXECUTIVE VICE PRESIDENT, GENERAL COUNSEL, AND SECRETARY

TEL 312.322.1817 FAX 312.322.1836

WNAVIN@THEOCC.COM

May 27, 2005

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: Proposed Rules for Customer Portfolio and Cross-Margining: Release No. 34-51614, File No. SR-CBOE-2002-03 and Release No. 34-51615, File No. SR-NYSE-2002-19

Dear Mr. Katz:

The Options Clearing Corporation ("OCC") submits this letter to comment on the above-captioned proposed rules of the Chicago Board Options Exchange ("CBOE") and the New York Stock Exchange ("NYSE"). The two rule filings (the "Exchange rule filings"), which are essentially identical in substance, are intended to permit the implementation of a pilot program that would allow member organizations to margin customer positions in listed (i) broad-based market index options, (ii) index warrants, and (iii) related exchange-traded funds ("eligible securities products") according to a portfolio margin methodology as an alternative to the strategy-based margin methodology currently set forth in exchange rules. In addition, the proposed rule changes would provide, also on a pilot basis, for customer participation in cross-margining programs by allowing broad-based index futures and options on such futures ("eligible futures products") to be included with eligible securities products in a separate customer cross-margin account that would be margined on a portfolio basis. The proposals, which are described in detail in the rule filings, would limit participation in the portfolio and cross-margining programs to customers having net equity in their brokerage accounts of at least \$5 million.

OCC strongly urges the Commission to move forward promptly with the approval of the pending rule filings. The pilot program was developed through a process that included input of many interested securities firms as well as OCC, the Chicago Mercantile Exchange ("CME"), The Clearing Corporation ("CCorp") and other interested constituencies, including several members of the Commission staff and the staff of the Commodity Futures Trading Commission (the "CFTC"). Since the original customer portfolio and cross-margining rule filings were submitted and published for comment in 2002, significant effort has been expended to address the regulatory issues surrounding program implementation. As it is our understanding that there are no unresolved issues, we see no reason for delaying the approval of these proposals.

Our purpose in submitting this letter, however, is not simply to urge the approval of the exchanges' rule filings. It is also to remind the Commission of the other regulatory actions that are necessary in order to implement the proposed pilot programs. We are concerned that, unless attention is given to these other issues, the approval of the Exchange rule filings will not provide for the implementation of the pilot program as intended. The other necessary regulatory actions are as follows:

Implementation of both the portfolio margining and customer cross-margining pilot programs requires approval by the Commission of SR-OCC-2003-04, which amends OCC's By-Laws to create a type of account referred to as a "customers' lien account" that will be used for, among other things, customer portfolio margining accounts and customer cross-margining accounts.¹ This rule filing was published for comment on March 8, 2005, but thus far has not been approved. Implementation of both pilot programs also requires a response by the Commission staff to a related no action request. In connection with the OCC lien account filing just described, OCC submitted a request for a no action letter that would allow OCC's lien to attach to all long option positions and other assets in the customers' lien account as contemplated by File No. SR-OCC-2003-04 without deeming the Clearing Member to be in violation of Rules 8c1-1, 15c2-1 or 15c3-3(c) under the 1934 Act.² Without the requested no action relief, prospective participants in the pilot program may be unwilling to participate.

While the foregoing actions are essential to both the portfolio margining pilot and the cross-margining pilot, implementation of the cross-margining pilot requires certain additional regulatory actions. The Commission staff several years ago determined that customer cross-margining accounts must be treated as securities accounts and not as segregated futures accounts for regulatory purposes. In order to do that, it is necessary to obtain relief from provisions of the Commodity Exchange Act and the CFTC's regulations that would otherwise require futures positions to be carried in segregated futures accounts. Accordingly, CBOE requested that the CFTC issue an appropriate exemptive order. The staff of the CFTC has indicated that it would give consideration to such an exemption, and has requested clarification as to the treatment under the Securities Investor Protection Act ("SIPA") of customer claims relating to futures products in cross-margining accounts in the event of the insolvency of the carrying broker-dealer/futures commission merchant.

We have been informed by the Commission staff that the status under SIPA of customer claims for futures products will be clarified through the adoption by the Commission of amendments to its Rule 15c3-3. As a release proposing such amendments has yet to be

¹ Cross-margining programs currently exist between OCC and CME and between OCC and CCorp, both of which are derivatives clearing organizations ("DCOs") regulated by the CFTC. OCC and the DCOs will amend their cross-margining agreements to include customer cross-margining accounts in a manner consistent with the customer cross-margining pilot as proposed.

² See letter from William H. Navin to Michael A. Macchiaroli dated January 13, 2005. The letter, as requested by the Commission staff, combines the no action relief with respect to the customer lien account with a request for relief from the same regulations relating to certain spread positions involving security futures. The substance of the no action request was originally included in SR-OCC-2003-04, but was deleted by an amendment to the rule filing and separately submitted as a no action request at the direction of the Commission staff.

published and it is unclear when such amendments will be adopted, OCC recommends that the Commission's approval of the Exchange rule filings allow the implementation of portfolio margining prior to the adoption of the amendments to Rule 15c3-3 necessary to implement cross-margining. This recommendation is not intended to minimize the importance of the cross-margining component of the rule filings relative to the portfolio margining component, but rather recognizes the reality that implementation of the cross-margining pilot will require additional regulatory actions unrelated to portfolio margining. Cross-margining programs have received the universal support of financial regulators because of their utility in reducing systemic risk in the financial markets. We believe that this is a sufficiently important issue to deserve some priority among the many issues facing the Commission and its staff.

As we have described above, the approval of the Exchange rule filings alone will be insufficient to allow implementation of either the portfolio margining pilot or the cross-margining pilot. Both pilots also require approval of the OCC non-lien customer account and issuance of the related no-action letter, and the cross-margining pilot requires amendments to SEC Rule 15c3-3 as well as a CFTC exemptive order. While we are recommending that the Commission take the regulatory actions necessary to implement the portfolio margining pilot independently of the Rule 15c3-3 amendments needed to permit the cross-margining pilot to go forward, we strongly urge that the Commission move forward promptly on the Rule 15c3-3 amendments so that both the cross-margining pilot, as well as the portfolio margining pilot, can be promptly implemented.

We appreciate the opportunity to comment on these matters. We would be pleased to discuss any of these issues with you further. Please feel free to contact me at (312) 322-1817 or Andy Naughton at (312) 322-2007.

Sincerely,



William H. Navin

cc: Michael Macchiaroli, SEC
Jerry Carpenter, SEC
John Lawton, CFTC