

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-68225; File No. AN-OCC-2012-04)

November 14, 2012

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Advance Notice to Revise the Method for Determining the Minimum Clearing Fund Size to Include Consideration of the Amount Necessary to Draw on Secured Credit Facilities

Pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010 (“Clearing Supervision Act”)¹ and Rule 19b-4(n)(1)(i),² notice is hereby given that on October 18, 2012, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the advance notice described in Items I, II, and III below, which Items have been prepared primarily by OCC. The Commission is publishing this notice to solicit comments on the advance notice from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Advance Notice

OCC proposes to revise the method for determining the minimum clearing fund size to include consideration of the amount necessary for OCC to draw on its secured credit facilities.

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Advance Notice

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the advance notice and discussed any comments it received on the advance notice.

The text of these statements may be examined at the places specified in Item IV below. OCC

¹ 12 U.S.C. 5465(e)(1).

² 17 CFR 240.19b-4(n)(i).

has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.³

(A) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Advance Notice

The purpose of this advance notice is to implement a minimum clearing fund size equal to 110% of the amount of committed credit facilities secured by the clearing fund to ensure that the amount of the clearing fund likely will exceed the required collateral value that would be necessary for OCC to be able to draw in full on such credit facilities. OCC's clearing fund is primarily intended to provide a high degree of assurance that market integrity will be maintained in the event that one or more clearing members or other specified entities to which OCC has credit exposure fails to meet its obligations.⁴ This includes the potential use of the clearing fund as a source of liquidity should it ever be the case that OCC is unable to obtain prompt delivery of, or convert promptly to cash, any asset credited to the account of a suspended clearing member.

On September 23, 2011, the Commission approved a proposed rule change by OCC to establish the size of OCC's clearing fund as the amount that is required, within a confidence level selected by OCC, to sustain the maximum anticipated loss under a defined set of scenarios

³ The Commission has modified the text of the summaries prepared by OCC.

⁴ Under Article VIII, Section 1 of OCC's By-Laws, the clearing fund may be used to pay losses suffered by OCC: (1) as a result of the failure of a clearing member to perform its obligations with regard to any exchange transaction accepted by OCC; (2) as a result of a clearing member's failure to perform its obligations in respect of an exchange transaction or an exercised/assigned options contract, or any other contract or obligations in respect of which OCC is liable; (3) as a result of the failure of a clearing member to perform its obligations in respect of stock loan or borrow positions; (4) as a result of a liquidation of a suspended clearing member's open positions; (5) in connection with protective transactions of a suspended clearing member; (6) as a result of a failure of any clearing member to make any other required payment or to render any other required performance; or (7) as a result of a failure of any bank or securities or commodities clearing organization to perform its obligations to OCC.

as determined by OCC, subject to a minimum clearing fund size of \$1 billion.⁵ OCC implemented this change in May 2012. Until that time, the size of OCC's clearing fund was calculated each month as a fixed percentage of the average total daily margin requirement for the preceding month, provided that the calculation resulted in a clearing fund of \$1 billion or more.⁶

Under the formula that is implemented for determining the size of the clearing fund as a result of the May 2012 change, OCC's Rules provide that the amount of the fund is equal to the larger of the amount of the charge to the fund that would result from (i) a default by the single "clearing member group"⁷ whose default would be likely to result in the largest draw against the clearing fund or (ii) an event involving the near-simultaneous default of two randomly-selected "clearing member groups" in each case as calculated by OCC with a confidence level selected by OCC.⁸ The size of the clearing fund continues to be recalculated monthly, based on a monthly averaging of daily calculations for the previous month, and it is subject to a requirement that its minimum size may not be less than \$1 billion.

⁵ Securities Exchange Act Release No. 34-65386 (September 23, 2011), 76 FR 60572 (September 29, 2011) (SR-OCC-2011-10).

⁶ If the calculation did not result in a clearing fund size of \$1 billion or more, then the percentage of the average total daily margin requirement for the preceding month that resulted in a fund level of at least \$1 billion would be applied. However, in no event was the percentage permitted to exceed 7%. With the rule change approved in September 2011, this 7% limiting factor on the minimum clearing fund size was eliminated.

⁷ The term "clearing member group" is defined in OCC's By-Laws to mean a clearing member and any member affiliates of the clearing member.

⁸ The confidence levels employed by OCC in calculating the charge likely to result from a default by OCC's largest "clearing member group" and the default of two randomly-selected "clearing member groups" were approved by the Commission at 99% and 99.9%, respectively. However, the Commission approval order notes that OCC retains discretion to employ different confidence levels in these calculations provided that OCC will not employ confidence levels of less than 99% without first filing a proposed rule change.

This minimum dollar size for OCC's clearing fund is the subject of this advance notice. OCC maintains committed credit facilities that are secured by the clearing fund in order to provide a source of liquidity in the event of a default by a clearing member or one of OCC's settlement banks. The change arises out of a regular review that OCC conducts in order to determine the appropriate aggregate amount of such committed credit facilities. In addition to its liquidity exposure to the potential failure of a clearing member, OCC also evaluates its liquidity exposure to settlement banks in respect of their ability to wire net settlement proceeds in time for OCC to meet its settlement obligations at one or more of OCC's other settlement banks as well as OCC's credit exposure to banks that issue letters of credit on behalf of clearing members as a form of margin.

OCC's committed credit facilities are secured by assets in the clearing fund and certain margin deposits of suspended clearing members. In light of the uncertainty regarding the amount of margin assets of a suspended clearing member that might be eligible at any given point to support borrowing under the secured credit facilities, OCC has considered the availability of funds based on a consideration of the amount of the clearing fund deposits available as collateral. To draw on the full amount of its credit facilities secured by the clearing fund, the size of the clearing fund would need to be approximately \$2.2 billion. The \$2.2 billion figure reflects a 10% increase above the total size of such credit facilities, which is meant to account for the percentage discount applied to collateral pledged by OCC in determining the amount available for borrowing.

Based on monthly recalculation information, the size of OCC's clearing fund during the period from July 2011 to July 2012 was less than \$2.2 billion on eight occasions. Therefore, to address the risk that the assets in the clearing fund might at any time be insufficient to enable

OCC to meet potential liquidity needs by fully accessing its committed credit facilities that are secured by the clearing fund, the proposed rule change described by the advance notice would amend the requirement that the minimum size of the clearing fund cannot be less than \$1 billion by providing instead that the minimum clearing fund size would be equal to the greater of either \$1 billion or 110% of the amount of such committed credit facilities. OCC proposes to denote the credit facility component of the minimum clearing fund requirement as a percentage of the total amount of the credit facilities that OCC actually secures with clearing fund assets because OCC negotiates these credit facility agreements, including size and other terms, on an annual basis and the total size is therefore subject to change.

(B) Clearing Agency's Statement on Burden on Competition

OCC does not believe that the proposed changes contained in the advance notice will have any impact or impose any burden on competition.

(C) Clearing Agency's Statement on Comments on the Advance Notice Received from Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule changes contained in the advance notice.

III. Date of Effectiveness of the Advance Notice and Timing for Commission Action

The proposed changes contained in the advance notice may be implemented pursuant to Section 806(e) (1)(G) of Clearing Supervision Act⁹ if the Commission does not object to the proposed changes within 60 days of the later of (i) the date that the advance notice was filed with

⁹ 12 U.S.C. 5465.

the Commission or (ii) the date that any additional information requested by the Commission is received. The clearing agency shall not implement the proposed changes contained in the advance notice if the Commission objects to the proposed changes.

The Commission may extend the period for review by an additional 60 days if the proposed changes raise novel or complex issues, subject to the Commission providing the clearing agency with prompt written notice of the extension. Proposed changes may be implemented in fewer than 60 days from the date the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the proposed changes and authorizes the clearing agency to implement the proposed changes on an earlier date, subject to any conditions imposed by the Commission.

The proposals contained in this advance notice shall not take effect until all regulatory actions required with respect to the proposals are completed.¹⁰ The clearing agency shall post notice on its website of proposed changes that are implemented.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Comments may be submitted by any of the following methods:

¹⁰ OCC also filed the proposals contained in this advance notice as a proposed rule change under Section 19(b)(1) of the Exchange Act and Rule 19b-4 thereunder. 15 U.S.C. 78s(b)(1); 17 CFR 240.19b-4. Pursuant to Section 19(b)(2) of the Exchange Act, within forty-five days of the date of publication of the proposed rule change in the Federal Register or within such longer period up to ninety days if the Commission designates or the self-regulatory organization consents the Commission will either: (i) by order approve or disapprove the proposed rule change or (ii) institute proceedings to determine whether the proposed rule change should be disapproved. 17 U.S.C. 78s(b)(2)(A). See Securities Exchange Act Release No. 34-68130 (November 1, 2012), 77 FR 66900 (November 7, 2012) (SR-OCC-2012-19).

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 AN-OCC-2012-04 on the subject line.

Paper Comments:

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

All submissions should refer to File Number AN-OCC-2012-04. 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 advance notice that are filed with the Commission, and all written communications relating to the advance notice 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 filings also will be available for inspection and copying at the principal office of OCC and on OCC's website at

http://www.optionsclearing.com/components/docs/legal/rules_and_bylaws/sr_occ_12_19.pdf.

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number AN-OCC-2012-04 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

By the Commission.

Kevin O'Neill
Deputy Secretary