

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-70366; File No. SR-OCC-2013-805)

September 10, 2013

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of an Advance Notice to Amend an Existing Interpretation and Policy to Give OCC Discretion Not to Grant a Particular Clearing Member Margin Credit for an Otherwise Eligible Security

Pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010 (“Clearing Supervision Act”)<sup>1</sup> and Rule 19b-4(n)(1)(i)<sup>2</sup> of the Securities Exchange Act of 1934 (“Act”), notice is hereby given that on August 15, 2013, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the advance notice as described in Items I, II and III below, which Items have been prepared by OCC.<sup>3</sup> 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 Proposed Advance Notice

OCC proposes to amend an existing Interpretation and Policy so that OCC has discretion to disapprove as margin collateral for a particular clearing member, shares of an otherwise eligible security held as margin.

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<sup>1</sup> 12 U.S.C. 5465(e)(1).

<sup>2</sup> 17 CFR 240.19b-4(n)(1)(i).

<sup>3</sup> OCC is a designated financial market utility and is required to file advance notices with the Commission. See 12 U.S.C. 5465(e). OCC also filed the proposal 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) and 17 CFR 240.19b-4, respectively. See SR-OCC-2013-14.

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 proposed advance notice and discussed any comments it received on the proposed advance notice. 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) and (B) below, of the most significant aspects of these statements.

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

The purpose of the proposed advance notice is to provide OCC with discretion with regard to granting or not granting margin credit to a clearing member. OCC currently may withhold margin credit from all clearing members with respect to a specific security. OCC proposes to address the risk presented by concentrated positions of securities posted as margin by particular clearing members by withholding margin credit from such clearing member's accounts. OCC proposes to enhance its ability to limit its risk exposure to a concentrated position of equity securities posted as margin by a specific clearing member by providing OCC with the discretion to disregard, for the purposes of granting margin credit, some or all of the otherwise eligible equity securities posted as margin. In addition, the proposed advance notice is designed to provide OCC with discretion to make exceptions to proposed Interpretation and Policy .14 with respect to a specific clearing member. Accordingly, OCC may allow margin credit for an otherwise ineligible security for a specific clearing member in situations in which OCC determines that such security serves as a hedge to positions in cleared contracts in the same account of such clearing member.

Rule 604 lists the acceptable types of assets that clearing members may post with OCC to satisfy their margin requirements under Rule 601, including equity securities, and establishes the eligibility criteria for such assets. Equity securities are the most common form of margin assets posted by clearing members and, under Rule 601, are included in OCC's STANS margining system for the purposes of valuing such equity securities and determining on a portfolio basis a clearing member's margin obligation to OCC.

Interpretation and Policy .14 to Rule 604 allows OCC to disapprove a security as margin collateral for all clearing members based on a consideration of the factors set forth in the interpretation, including number of outstanding shares, number of outstanding shareholders and overall trading volume. The STANS system currently takes into account the risk to a portfolio presented by fluctuations in the market price of concentrated security positions by identifying the two individual securities whose adverse price movements would result in the largest losses in each account and applying additional margin requirements to an account based on those losses if appropriate.

However, this test does not evaluate a large equity securities position in relation to the securities position's average daily trade volume, which would be relevant if OCC were required to liquidate the position. OCC has determined that in the event of a clearing member liquidation, OCC may be exposed to concentration risk arising from a large equity security position deposited or pledged as margin by a particular clearing member. Depending on the relationship between the average daily trading volume of a particular security and the number of outstanding shares of such security deposited by a clearing member as margin, it is possible that the listed equities markets may not be able to quickly absorb the equity securities OCC seeks to sell, or without an appreciable negative

price impact, in the event OCC needs to liquidate the clearing member's accounts. This risk is greatest when the number of shares being sold is large and the average daily trading volume is low. Neither the STANS system nor Rule 604 explicitly addresses this type of concentration risk.

To address concentration risk arising from the potential need to liquidate a particular clearing member's margin collateral, OCC proposes to expand its discretion under Interpretation and Policy .14 to limit, in OCC's discretion, the margin credit granted to an individual clearing member account which maintains a concentrated equity securities position by disregarding some or all of the otherwise eligible equity securities posted as margin based on an assessment of specific factors listed in Interpretation and Policy .14. OCC considers an equity security's average daily trading volume and the number of shares a clearing member deposited as margin to be the two most significant factors when making a decision to limit margin credit due to concentration risk.<sup>4</sup> In addition, OCC proposes to amend Interpretation and Policy .14 so that it may grant margin credit when otherwise ineligible securities are deposited as margin collateral if such ineligible securities act as a hedge against cleared contracts held in the same account. For example, if a clearing member deposits otherwise ineligible equity securities as margin, OCC may nevertheless deem such ineligible securities to be acceptable margin collateral to the extent that the position is a hedge against a short position in its cleared contracts, because a decline in the value of the securities that serve as a hedge would be wholly or partially offset by an increase in value in the hedged

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<sup>4</sup> The limit is currently two times the equity security's average daily trading volume.

position thereby reducing or eliminating the concentration risk. In such a situation, OCC will limit the margin credit granted to the lesser of a multiple of the daily trading volume or the "delta equivalent position"<sup>5</sup> for the particular equity security, taking into account the hedging position.<sup>6</sup>

OCC staff has been monitoring concentrated securities positions and assessing the impact of the proposed change described in this advance notice filing. OCC believes that, with OCC's assistance by supplying additional information to clearing members, clearing members will be able to accommodate the proposed changes without undue hardship. Accordingly, after receiving regulatory approval for the proposed advance notice, OCC will implement the change and work on an "as needed" manual basis with

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<sup>5</sup> The "delta equivalent position" is the value of a securities position that takes into account the position's use as a hedge against cleared option or futures positions. This value is calculated using the "delta" of the option or futures contract, which is the ratio between the theoretical change in the price of an underlying asset to the corresponding change in the price of the options or futures contract. Thus, delta measures the sensitivity of an options or futures contract price to changes in the price of the underlying asset. For example, a delta of +0.7 means that for every \$1 increase in the price of the underlying stock, the price of a call option will increase by \$0.70. Delta for an option or future can be expressed in shares of the underlying asset. For example, a standard put option with a delta of -.45 would have a delta of -45 shares, because the unit of trading is 100 shares.

<sup>6</sup> Assume, for example, an average daily trade volume of 250 shares, a threshold of 2 times the average daily trade volume, and a delta of -300 shares for the options on a particular security in a particular account. A position of 700 shares that did not hedge any short options or futures would receive credit for only 500 shares (i.e., 2 times the average daily trade volume). If the net long position in the account, as adjusted for the delta of short option and futures positions, were only 400, credit would be given for the entire 700 shares since the delta equivalent position is below the 500 share threshold. However, if the option delta were +300, the net long position would be 1000, and credit would only be given for 500 shares because the delta equivalent position would exceed the 500 share threshold.

clearing members that are impacted until the limits are imposed systematically and the distribution of the applicable files and reports to clearing members is automated.

The proposed advance notice is consistent with Section 806(e)(1)(A)<sup>7</sup> of the Payment, Clearing, and Settlement Supervision Act of 2010 because the proposed change could be deemed to materially affect the nature or level of risks presented by OCC. The proposed advance notice enhances OCC's ability to limit its risk exposure to potential losses from defaults by clearing members under normal market conditions through the use of risk-based parameters and encourages clearing members to have sufficient financial resources to meet their obligations to OCC. The proposed advance notice is not inconsistent with any existing OCC By-Laws or Rules, including those proposed to be amended.

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

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

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

The clearing agency may implement the proposed change pursuant to Section 806(e)(1)(G) of the Clearing Supervision Act<sup>8</sup> if it has not received an objection to the proposed change within 60 days of the later of (i) the date that the Commission received the advance notice or (ii) the date the Commission receives any further information it requested for consideration of the notice. The clearing agency shall not

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<sup>7</sup> 12 U.S.C. 5465(e)(1)(A).

<sup>8</sup> 12 U.S.C. 5465(e)(1)(G).

implement the proposed change if the Commission objects to the proposed change within the required time period.

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

The clearing agency 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. 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-2013-805 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 SR-OCC-2013-805. 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 of submission.

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 the filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at

[http://www.theocc.com/components/docs/legal/rules\\_and\\_bylaws/sr\\_occ\\_13\\_805.pdf](http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_13_805.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 SR-OCC-2013-805 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

By the Commission.

Kevin M. O'Neill  
Deputy Secretary