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 (“Clearing Supervision Act”)\(^1\) and Rule 19b-4(n)(1)(i) under the Securities Exchange Act of 1934\(^2\) notice is hereby given that on November 4, 2014, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the advance notice as described in Items I and II below, which Items have been prepared 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**

This advance notice is filed by OCC in connection with a proposed change to its operations in the form of implementing a committed master repurchase agreement program, as part of OCC’s overall liquidity plan.

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

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\(^1\) 12 U.S.C. 5465(e)(1).

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 on Comments on the Advance Notice Received from Members, Participants or Others

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

(B) Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Description of Change

This advance notice is being filed in connection with a proposed change to OCC’s operations through which OCC would implement a committed master repurchase agreement program, as discussed below, to access an additional committed source of liquidity to meet its settlement obligations.

Background

OCC has been working with a lending agent and an interested institutional investor to develop a program that would allow OCC to access an additional committed source of liquidity that does not increase the concentration of OCC’s counterparty exposure, given existing affiliations between a number of commercial banking institutions and OCC’s clearing members. The program would take the form of OCC’s implementing a committed master repurchase agreement and related confirmations (together, the “Master Repurchase Agreement”) with one or more non-bank, non-clearing member institutional investors and their agents.³

³ The agents for the institutional investors would be responsible for handling administrative aspects of the program on behalf of the investors.
OCC would conduct a due diligence review with respect to each counterparty before entering into a master repurchase arrangement with it. Because the appropriate due diligence activities and financial criteria will vary for each type of counterparty and for each individual counterparty, OCC would determine on a case-by-case basis the specific due diligence criteria it would implement. However, as the principal purpose of these activities would be to obtain assurance that each counterparty has the financial ability to satisfy its obligations under the program, the review would encompass an assessment of the counterparty’s financial statements (including external auditor reports thereon) and, as applicable, ratings and/or investment reports. As part of the due diligence process, OCC would identify key criteria relative to monitoring the financial stability of the counterparty on a going forward basis.

Although the Master Repurchase Agreement would be based on the standard form of master repurchase agreement\(^4\) so that it will be more familiar to potential institutional investors, OCC would require the Master Repurchase Agreement to contain certain additional provisions tailored to ensure a reduction in concentration risk, certainty of funding, and operational effectiveness, as described in more detail below. OCC believes that these provisions are necessary and appropriate to integrate the program into its operations and in order to promote safety and soundness consistent with OCC’s systemic responsibilities. The terms and conditions applicable to the Master Repurchase Agreement are set forth in the Summary of Indicative Terms attached to this filing as Exhibit 3.

\(^4\) The standard form master repurchase agreement is published by the Securities Industry and Financial Markets Association (“SIFMA”) and is commonly used in the repurchase market by institutional investors.
The program would be part of OCC’s overall liquidity plan, which is meant to provide OCC with access to a diverse set of sources for liquidity, which includes committed credit facilities, securities lending and securities repurchase arrangements, and clearing member funding requirements that, under certain conditions, allow OCC to obtain funds from clearing members.  

**The Proposed Program: Standard Repurchase Agreement Terms**

The Master Repurchase Agreement would generally be structured like a typical repurchase arrangement, in order to help OCC attract interest from potential institutional investors willing to be a counterparty to OCC. Under the Master Repurchase Agreement, the buyer (i.e., the institutional investor) would purchase from OCC from time to time United States government securities (“Eligible Securities”). OCC, as the seller, would transfer Eligible Securities to the buyer in exchange for a payment by the buyer to OCC in immediately available funds (the “Purchase Price”). The buyer would simultaneously agree to transfer the purchased securities back to OCC at a specified later date or on OCC’s demand (the “Repurchase Date”) against the transfer of funds by OCC to the buyer in an amount equal to the outstanding Purchase Price plus the accrued and unpaid


6 OCC would use U.S. government securities that are included in clearing fund contributions by clearing members and margin deposits of any clearing member that has been suspended by OCC for the repurchase arrangements. Article VIII, Section 5(e) of OCC’s By-Laws and OCC Rule 1104(b) authorize OCC to obtain funds from third parties through securities repurchases using these sources. The officers who may exercise this authority include the Executive Chairman and the President.
price differential (together, the “Repurchase Price”), which is the interest component of the Repurchase Price.

At all times while a transaction is outstanding, OCC would be required to maintain a specified amount of securities or cash margin with the buyer. The market value of the securities supporting each transaction would be determined daily, typically based on a price obtained from a generally recognized pricing source. If the market value of the purchased securities is determined to have fallen below OCC’s required margin, OCC would be required to transfer to the buyer sufficient cash or additional securities reasonably acceptable to the buyer so that OCC’s margin requirement is satisfied. If the market value of the purchased securities is determined to have risen to above OCC’s required margin, OCC would be permitted to require the return of excess purchased securities from the buyer.

As in a typical master repurchase agreement, an event of default would occur with respect to the buyer if the buyer failed to purchase securities on a Purchase Date, failed to transfer purchased securities on any applicable Repurchase Date, or failed to transfer any interest, dividends or distributions on purchased securities to OCC within a specified period after receiving notice of such failure. An event of default would occur with respect to OCC if OCC failed to transfer purchased securities on a Purchase Date or failed to repurchase purchased securities on an applicable Repurchase Date. The Master Repurchase Agreement would also provide for standard events of default for either party,

7 OCC expects that it would be required to maintain margin equal to 102% of the Repurchase Price, which is a standard rate for arrangements involving U.S. government securities.

8 OCC expects that it would use clearing fund securities and securities posted as margin by defaulting clearing members, as more fully discussed in footnote 7.
including a party’s failure to maintain required margin or an insolvency event with respect to the party.

Upon the occurrence of an event of default, the non-defaulting party, at its option, would have the right to accelerate the Repurchase Date of all outstanding transactions between the defaulting party and the non-defaulting party, among other rights. For example, if OCC were the defaulting party with respect to a transaction and the buyer chose to terminate the transaction, OCC would be required to immediately transfer the Repurchase Price to the buyer. If the buyer were the defaulting party with respect to a transaction and OCC chose to terminate the transaction, the buyer would be required to deliver all purchased securities to OCC. If OCC or the buyer did not timely perform, the non-defaulting party would be permitted to buy or sell, or deem itself to have bought or sold, securities as needed to be made whole and the defaulting party would be required to pay the costs related to any covering transactions. Additionally, if OCC was required to obtain replacement securities as a result of an event of default, the buyer would be required to pay the excess of the price paid by OCC to obtain replacement securities over the Repurchase Price.

The Proposed Program: Customized Features to Promote a Reduction in Concentration Risk, Certainty of Funding and Operational Effectiveness

In addition to the master repurchase agreement, OCC would enter into an individualized master confirmation with each buyer and its agent which would set forth certain terms and conditions applicable to all transactions entered into under the Master Repurchase Agreement by that buyer. As discussed above, these required terms and conditions would be designed to promote OCC’s goals of reduced concentration risk, certainty of funding and operational effectiveness. The terms of the master confirmations
under each Master Repurchase Agreement may vary from one another, because a separate master confirmation will be negotiated for a given buyer at the time that buyer becomes a party to the Master Repurchase Agreement. Because the arrangements between OCC and the individual buyers have not been fully negotiated, OCC has identified the following as key standards that would need to be incorporated into each repurchase arrangement entered into under the program.9

Counterparties

OCC would only enter into repurchase arrangements with institutional investors, such as pension funds or insurance companies, that are not OCC clearing members or banks affiliated with any OCC clearing member. This requirement would allow OCC to access stable, reliable sources of funding, without increasing the concentration of its exposure to counterparties that are affiliated banks, broker/dealers and futures commission merchants. This reduction in concentration risk is a key advantage of this proposed program.

Commitment to Fund and Funding Accounts

OCC would seek funding commitments from one or more potential counterparties that would equal $1 billion in the aggregate,10 with each commitment extending for 364 days or more. Each counterparty would be obligated to enter into transactions under the Master Repurchase Agreement up to its committed amount so long as no default had

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9 OCC expects that the Master Repurchase Agreement will also include other, more routine, provisions such as the method for giving notices and basic due authorization representations by the parties.

10 The $1 billion in commitments could be spread across multiple counterparties, but $1 billion represents the proposed aggregate size of the program.
occurred and OCC transferred sufficient Eligible Securities. Each counterparty would be obligated to enter into transactions even if OCC had experienced a material adverse change, such as the failure of a clearing member. This commitment to provide funding would be a key departure from ordinary repurchase arrangements and a key requirement for OCC. Each commitment would be supported by an agreement by the counterparty to maintain cash and investments acceptable to OCC that must be readily converted into cash in a designated account into which OCC had visibility. The creation of a funding account is important because it would provide OCC with two key protections. First, it would help OCC ensure that the committed funds would be available each day, as discussed below. Second, it would facilitate prompt funding by counterparties that are not commercial banks and therefore are not in the business of daily funding.

**Funding Mechanics**

Funding mechanics would be targeted so that OCC would receive the Purchase Price in immediately available funds within 60 minutes of its request for funds and delivery of Eligible Securities and, if needed, prior to OCC’s regular daily settlement time. These targeted funding mechanics would allow OCC to receive needed liquidity in time to satisfy settlement obligations, even in the event of a default by a clearing member or a market disruption. The funding mechanism may be, for example, delivery versus payment/receive versus payment or another method acceptable to OCC that both

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11. This would include OCC’s regular daily settlement time and any extended settlement time implemented by OCC in an emergency situation under Rule 505.

12. Delivery versus payment/receive versus payment is a method of settlement under which payment for securities must be made prior to or simultaneously with delivery of the securities.
satisfies the objectives of the master repurchase agreement program and presents limited operational risks.

*No Rehypothecation*

Under the terms of each master confirmation, the buyer would not be permitted to grant any third party an interest in purchased securities, the custody account at the custodian in which purchased securities are held or any cash held in OCC’s account. This requirement is important for two reasons. First, because the buyer would be prohibited from rehypotecating purchased securities, the purchased securities should never leave the account and there should be no third-party claims against the purchased securities. Second, the prohibition on rehypothecation would also reduce the risk that a third party could interfere with the buyer’s transfer of the purchased securities on the Repurchase Date. Further, the custodian would agree to provide OCC with daily information about each buyer’s account. This visibility would allow OCC to act quickly in the event a buyer violates any requirements.

*Early Termination Rights*

Under the Master Repurchase Agreement, OCC would have the ability to terminate any transaction upon written notice to the buyer, but a buyer would only be able to terminate a transaction upon the occurrence of an event of default with respect to OCC, as further described below. A notice of termination by OCC would specify a new Repurchase Date prior to the originally agreed upon Repurchase Date. Upon the early termination of a transaction, the buyer would be required to return all purchased securities to OCC and OCC would be required to pay the Repurchase Price. This optional early termination right is important to OCC because OCC’s liquidity needs may
change unexpectedly over time and as a result OCC may not want to keep a transaction outstanding as long as originally planned.

**Substitution**

Under the Master Repurchase Agreement, OCC would have the ability to substitute any Eligible Securities for purchased securities in its discretion by a specified time, so long as the Eligible Securities satisfy any applicable criteria contained in the Master Repurchase Agreement and the transfer of the Eligible Securities would not create a margin deficit, as described above. This substitution right is important to OCC because it must be able to manage requests of clearing members to return excess or substitute Eligible Securities in accordance with established operational procedures.

**Events of Default**

Beyond the standard events of default for a failure to purchase or transfer securities on the applicable Purchase Date or Repurchase Date, as described above, OCC would require that the Master Repurchase Agreement not contain any additional events of default that would restrict OCC’s access to funding and that it contain an additional default remedy. Most importantly, OCC would require that it would not be an event of default if OCC suffers a “material adverse change”. This provision is important because it provides OCC with certainty of funding, even in difficult market conditions.

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13 In addition to its substitution rights, OCC could cause the return of purchased securities by exercising its optional early termination rights under the Master Repurchase Agreement. If OCC were to terminate part or all of a transaction, the buyer would be required to return purchased securities to OCC against payment of the corresponding Repurchase Price.

14 When included in a contract, a “material adverse change” is typically defined as a change that would have a materially adverse effect on the business or financial condition of a company.
Upon the occurrence of an event of default, in addition to the non-defaulting party’s right to accelerate the Repurchase Date of all outstanding transactions or to buy or sell securities as needed to be made whole, the non-defaulting party may elect to take the actions specified in the “mini close-out” provision of the Master Repurchase Agreement, rather than declaring an event of default. For example, if the buyer fails to transfer purchased securities on the applicable Repurchase Date, rather than declaring an event of default, OCC may (1) if OCC has already paid the Repurchase Price, require the buyer to repay the Repurchase Price, (2) if there is a margin excess, require the buyer to pay cash or delivered purchased securities in an amount equal to the margin excess, or (3) declare that the applicable transaction, and only that transaction, will be immediately terminated, and apply default remedies under the Master Repurchase Agreement to only that transaction. Therefore, if the buyer fails to deliver purchased securities on any Repurchase Date, OCC would have remedies that allow it to mitigate risk with respect to a particular transaction, without declaring an event of default with respect to all transactions under the Master Repurchase Agreement.

Anticipated Effect on and Management of Risk

OCC believes that the overall impact of the program on the risks presented by OCC would be to reduce settlement risk associated with OCC’s operations as a clearing agency. The program would reduce settlement risk by providing an additional source of liquidity, from diversified funding sources that decrease OCC’s concentration of risk, with funding certainty and operational efficiency. The resulting reduction in OCC settlement risk would lead to a corresponding reduction in systemic risk and would have a positive impact on the safety and soundness of the clearing system by enabling OCC to
have continuous access to funds to settle its obligations to its clearing members. OCC’s consistent ability to timely settle its obligations is a key part of OCC’s role as a clearing agency and allows OCC to mitigate counterparty risk within the market. In order to sufficiently perform this key role in promoting market stability, it is critical that OCC continuously has access to funds to settle its obligations.

The Master Repurchase Agreement, like any liquidity source, would involve certain risks, but OCC would structure the program to mitigate those risks. Most of these risks are standard in any master repurchase agreement. For example, a buyer could fail to deliver, or delay in delivering, purchased securities to OCC by the applicable Repurchase Date. OCC will address this risk by seeking a security interest from the buyer in that portion of the purchased securities representing the excess of the market value over the Repurchase Price, or by obtaining other comfort from the buyer that the purchased securities will be timely returned. Further, the purchased securities generally will not be “on-the-run” securities, i.e. the most recently issued Treasury securities. The demand in the marketplace for Treasury securities, for uses other than collateral, is much greater for on-the-run Treasury securities, and therefore, OCC believes buyers will have little incentive to retain the securities transferred by OCC.

The mechanics under the Master Repurchase Agreement would be structured so that OCC could avoid losses by paying the Repurchase Price. For example, OCC will have optional early termination rights in each master confirmation, under which OCC would be able to accelerate the Repurchase Date of any transaction by providing written notice to the buyer and paying the Repurchase Price. Through this mechanism, OCC can
maintain the benefit of the Master Repurchase Agreement, while mitigating any risk associated with a particular transaction.

The Master Repurchase Agreement would be structured to avoid potential third-party risks, which are typical of repurchase arrangements. The prohibition on buyer rehypothecation and use of purchased securities, along with OCC’s visibility into the buyer’s custody account, would reduce the risk to OCC of a buyer default.

As with any repurchase arrangement, OCC is subject to the risk that it may have to terminate existing transactions and accelerate the applicable Repurchase Date with respect to a buyer due to changes in the financial health or performance of the buyer. Terminating transactions could negatively affect OCC’s liquidity position. However, any negative effect is reduced by the fact that OCC maintains a number of different financing arrangements, and thus will have access to liquidity sources in the event the Master Repurchase Agreement is no longer a viable source.

Under the Master Repurchase Agreement, OCC would be obligated to transfer additional cash or securities as margin in the event the market value of any purchased securities decreases. OCC seeks to ensure it can meet any such obligation by monitoring the value of the purchased securities and maintaining adequate cash resources to make any required payments. Such payments are expected to be small in comparison to the total amount of cash received for each transfer of purchased securities.

Consistency with the Payment, Clearing and Settlement Supervision Act

OCC believes that the proposed change is consistent with Section 805(b)(1) of the Payment, Clearing and Settlement Supervision Act.\textsuperscript{15} The objectives and principles of

\textsuperscript{15} 12 U.S.C. 5464(b)(1).
Section 805(b)(1) of the Payment, Clearing and Settlement Supervision Act specify the promotion of robust risk management, promotion of safety and soundness, reduction of systemic risks and support of the stability of the broader financial system. OCC believes that the proposed change would promote these objectives because the program should provide OCC with an additional source of committed liquidity to meet its settlement obligations while at the same time being structured to mitigate certain operational risks, as described above, that arise in connection with this committed liquidity source.

**Accelerated Commission Action Requested**

OCC requests that the Commission notify OCC that it has no objection to the change no later than December 12, 2014, in order to allow OCC to implement the master repurchase agreement program beginning in mid-December. OCC requests Commission action to ensure that OCC can access this source of additional liquidity on a timely basis, given the importance of maintaining diverse funding sources in connection with OCC’s risk management.

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

The designated clearing agency may implement this change if it has not received an objection to the proposed change within 60 days of the later of (i) the date that the Commission receives the notice of proposed change, or (ii) the date the Commission receives any further information it requests for consideration of the notice. The designated clearing agency shall not implement this change if the Commission has an objection.

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16 *Id.*
The Commission may, during the 60-day review period, extend the review period for an additional 60 days for proposed changes that raise novel or complex issues, subject to the Commission providing the designated clearing agency with prompt written notice of the extension. The designated clearing agency may implement a change in less than 60 days from the date of receipt of the notice of proposed change by the Commission, or the date the Commission receives any further information it requested, if the Commission notifies the designated clearing agency in writing that it does not object to the proposed change and authorizes the designated clearing agency to implement the change on an earlier date, subject to any conditions imposed by the Commission.

The designated 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. Please include File Number SR-OCC-2014-809 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-2014-809. 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 am and 3:00 pm. Copies of
the filing also will be available for inspection and copying at the principal office of OCC and on OCC’s website at


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-2014-809 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