

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-64740; File No. SR-OCC-2011-05)

June 24, 2011

Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving Proposed Rule Change to Provide Flexibility to The Options Clearing Corporation with Respect to its Obligations to Pay Settlement Amounts to Clearing Members Generally As Well As in Emergency Situations

I. Introduction

On April 28, 2011, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change SR-OCC-2011-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”).¹ The proposed rule change was published for comment in the Federal Register on May 12, 2011.² No comment letters were received on the proposal. This order approves the proposal.

II. Description

The purpose of this rule change is to revise OCC’s By-Laws and Rules to provide flexibility to OCC with respect to its obligations to pay settlement amounts to clearing members generally as well as in emergency situations. The proposed rule amendments will change the current daily deadline for OCC to pay settlement amounts to clearing members from 10:00 a.m. to 1:00 p.m. (All times referred to in this filing are Central Time). In addition, in the event that an emergency condition exists, the Board of Directors or certain executive officers of OCC would be authorized to extend OCC’s obligation to pay settlement amounts to clearing members beyond the 1:00 p.m. deadline.

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 34-64436 (May 6, 2011), 76 FR 27697 (May 12, 2011).

Currently, each business day morning, OCC is obligated to collect cash owed by its clearing members for the prior day's settlement activity by 9:00 a.m. OCC, in turn, is obligated to pay cash owed to its clearing members for the prior day's settlement activity by 10:00 a.m. This one-hour window is designed to give OCC time to collect all required settlement funds before having to disburse any settlement funds to its clearing members. Daily settlement activity includes obligations relating to: (1) the net premium payments arising from the prior day's option purchases and sales, (2) the mark-to-market of futures contracts and stock loan positions, and (3) exercises and assignments of cash-settled option contracts.

OCC's settlement banks routinely approve and are required to honor the associated settlements made by OCC and OCC's clearing members within these time frames. On most business days, the entire bank approval process, which irrevocably obligates each settlement bank to make settlement, is completed by 8:30 a.m.

Under OCC's rules, a failure by OCC to pay its daily settlement obligations to clearing members by 10:00 a.m. constitutes a default. During discussions among OCC's senior management of various potential extreme default and liquidity squeeze scenarios, including the possible default of one of OCC's largest clearing members, OCC analyzed the risk associated with not being able to immediately access liquidity resources in time to meet the 10:00 a.m. deadline for OCC to pay settlement amounts to clearing members. The deadline may be difficult to meet if, for example, OCC learned of a default near the 9:00 a.m. deadline. In such a circumstance, OCC would have only one hour or less when the time needed to process and communicate information is considered to access the funds necessary to meet the 10:00 a.m. deadline.

OCC's immediate liquidity resources rely heavily upon its \$2.0 billion revolving credit

facility, which is backed by Treasuries held in the clearing fund. A one-hour advance notice is required prior to OCC drawing funds from the credit facility. Beyond the credit facility, it would probably take more than one hour to raise cash by borrowing against the Treasuries held in the clearing fund that are not securing the credit facility either through tri-party repurchase agreements or a traditional bank loan.

The main benefit of moving the deadline to 1:00 p.m. for OCC to pay clearing members settlement amounts is that it allows up to four hours as opposed to the current one hour, within which OCC can meet its daily settlement requirement without being required to declare an emergency in order to do so. In addition, based on discussions with its settlement banks, OCC believes that notwithstanding a change from the current 10:00 a.m. deadline to a 1:00 p.m. deadline, the settlement banks will continue the current practice of approving settlements as soon as they can make a credit determination (i.e., confirm present funds or extend credit to the customer) and process OCC's payment requests, which are tasks that are typically completed by 8:30 a.m.

OCC also has incorporated in its rules the authority to extend the deadline for it to pay settlement amounts to clearing members to the close of the Federal Reserve Banks' Fedwire Funds Service on a settlement day, if necessary, during an emergency situation.³ Such an extension is consistent with the emergency authority other clearinghouses have to deal with late settlement scenarios. The rule amendments would authorize the Board, Chairman of the Board, Management Vice Chairman, or President of OCC to delay settlement beyond 1:00 p.m. in

³ In the event that OCC is unable to pay settlement amounts to clearing members by the close of the Fedwire Funds Service on a settlement day due to an emergency or force majeure condition, OCC will seek appropriate relief from the regulatory or supervisory authorities having jurisdiction over OCC.

emergency situations. The rule amendments would authorize the named officers to take such action because the decision may need to be made under time constraints where the Board (or even the Membership/Risk Committee) could not be convened in time to take the necessary action.⁴ OCC anticipates that the emergency authority would be used infrequently, if ever. Under proposed Rule 505, such authority could only be used upon a determination by the Board or an authorized officer that extension of the settlement time is necessary or advisable for the protection of OCC or otherwise in the public interest. In the event that the emergency authority is exercised, a number of protections are built into the process. For example, the determination and the reasons for the extension will be promptly reported to the Commission, the Commodities Futures Trading Commission, and any other regulatory or supervisory authorities having jurisdiction over OCC. In addition, the clearing members will be notified of the extension, and a report outlining the emergency actions will be maintained in OCC's records.

For drafting clarity and economy, the specific settlement times have been removed from the applicable rules, a new definition of "settlement day" has been created, and a revised definition of "settlement time" has been inserted in Article I of the By-Laws.

III. Discussion

Section 17A(b)(3)(F) of the Act⁵ requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of security transactions and to generally protect investors and the public interest. Because the proposed rule change modifies OCC's Rules and By-Laws to give OCC flexibility to make settlement

⁴ Similar authority is provided to the OCC Chairman (or the Board) to summarily suspend a clearing member. See OCC Rule 1102.

⁵ 15 U.S.C. 78q-1(b)(3)(F).

payments to its clearing members in a timely manner during normal and abnormal market conditions, the proposed rule change promotes the prompt and accurate clearance and settlement of security transactions and generally protects investors and the public interest and therefore is consistent with the requirements of Section 17A(b)(3)(F) of the Act.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act⁶ and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁷ that the proposed rule change (File No. SR-OCC-2011-05) be, and hereby is, approved.⁸

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.⁹

Cathy H. Ahn
Deputy Secretary

⁶ 15 U.S.C. 78q-1.

⁷ 15 U.S.C. 78s(b)(2).

⁸ In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

⁹ 17 CFR 200.30-3(a)(12).