

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-64883; File No. SR-OCC-2011-06)

July 14, 2011

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Regarding Clearing and Settling a Price Differential Spread Futures Transaction

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934,¹ notice is hereby given that on June 30, 2011, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission the proposed rule change as described in Items I and II below, which items have been prepared primarily by OCC. OCC filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act² and Rule 19b-4(f)(4) thereunder³ so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of Terms of Substance of the Proposed Rule Change

The proposed rule change would accommodate the clearing and settling of a transaction type called a Price Differential Spread for purposes of effecting exchange transactions in futures contracts.

II. Self-Regulatory Organization’s Statement of Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule

¹ 15 U.S.C. 78s(b)(1).

² 15 U.S.C. 78s(b)(3)(A)(iii).

³ 17 CFR 240.19b-4(f)(4).

change. 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, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of Purpose of, and Statutory Basis for, the Proposed Rule Change

The purpose of this proposed rule change is to amend OCC's By-Laws and Rules to accommodate the proposed introduction by ELX Futures L.P. ("ELX"), an electronic futures market that is designated as a contract market by the Commodity Futures Trading Commission ("CFTC"), of a transaction type called a Price Differential Spread ("Price Differential Spread") for purposes of effecting exchange transactions in futures contracts.⁴ A Price Differential Spread is a pair of transactions resulting from a type of order where the party placing the order seeks to simultaneously buy and sell futures contracts on the same underlying interest but with different contract months (each such transaction referred to herein as a "leg" of the Price Differential Spread), provided that the price at which contracts are bought in one leg less the price at which contracts are sold in the other leg (the "price differential") is no greater than the limit specified by such party (such limit referred to herein as the "maximum price differential"). Price Differential Spreads are principally used to roll futures positions forward into futures with the same underlying interest but with a later delivery date. In such a transaction, the cost to the party rolling the positions forward is determined solely by the difference between the prices at which the two legs of the Price Differential Spread are executed. The price of either leg alone is not relevant. As discussed below, by allowing a Clearing Member to use contract prices that are based on the previous day's exchange-reported closing price, the actual price differential is highlighted and allocation of equivalent transactions among different customers is facilitated.

⁴ OCC understands that similar transactions are used by at least one other futures exchange.

For purposes of illustration, assume that the “front leg” of a Price Differential Spread (i.e., the leg with the nearer contract month) is the sale of futures contracts and that the “back leg” (i.e., the leg with the more distant contract month) is the purchase of futures contracts.

When submitting a Price Differential Spread order to ELX, the trader will specify the maximum price differential, and ELX will attempt to match the two legs of the Price Differential Spread based on available orders (not limited to Price Differential Spread orders) from other traders. Assume that a Clearing Member submits a Price Differential Spread order (such Clearing Member referred to herein as the “Price Differential Spread Executor”) to sell a March SYM contract and buy a June SYM contract with a maximum price differential of \$1.00 and that ELX matches the front leg to counterparty A, that buys the March SYM contract at \$118.00, and the back leg to counterparty B, that sells the June SYM contract at \$118.95. In this case, the price differential between the two legs, based on matched trade prices, is \$0.95, which is lower than the \$1.00 maximum price differential that the Price Differential Spread Executor has specified.

Price Differential Spreads are differentiated from other futures transactions cleared by OCC in that the Price Differential Spread Executor may choose at the time it submits the order to (1) record the contract prices of both legs of a Price Differential Spread at the prices at which the contracts are matched on the exchange (“Spread Engine Prices”) or (2) record the contract price of the front leg at the exchange-reported closing price on the immediately preceding trading day for the contracts bought or sold (“prior day closing price”) and record the contract price of the back leg at (a) the contract price of the front leg plus the price differential, if the front leg is the sale of futures contracts or (b) the contract price of the front leg less the price differential if the front leg is the purchase of futures contracts (“Spread Settle Prices”).

After matching both legs of a Price Differential Spread, ELX will send to OCC a pair of

matched trade reports, each of which will identify the buyer, the seller, the futures contract traded, the exchange-assigned identification number (“Price Differential Spread ID”) connecting the two legs of the Price Differential Spread, the Spread Engine Price, and the Spread Settle Price. The matched trade reports also will indicate the price type (i.e., the Spread Engine Price or the Spread Settle Price) that OCC should use to record the trades on behalf of the Price Differential Spread Executor.⁵ Continuing the example, assume that the prior day closing price for the March SYM contract was \$117.90. If the Price Differential Spread Executor elects to use the Spread Engine Prices at the time it submits the order, OCC will initially record the front leg at \$118.00 and the back leg at \$118.95. Alternatively, if the Price Differential Spread Executor elects to use the Spread Settle Prices at the time it submits the order, OCC will initially record the front leg at \$117.90 and the back leg at \$118.85 (which is the sum of the \$117.90 contract price for the front leg plus the price differential of \$0.95 because the front leg is the sale of a futures contract).⁶ In addition, after the two legs of the Price Differential Spread have been accepted by OCC for clearance and prior to a deadline established by OCC, which deadline would occur before the initial variation payment, the Price Differential Spread Executor may access OCC’s systems to change its initial election with respect to such trades as between using the Spread Engine Prices and using the Spread Settle Prices. ELX has informed OCC that Price

⁵ In the case where each counterparty to the trade has entered into the trade as part of its own Price Differential Spread, the matched trade report will identify separately with respect to each counterparty the price to be initially recorded as the contract price and the Price Differential Spread ID.

⁶ Assume instead that the front leg is the purchase of a futures contract at \$118.95 and the back leg is the sale of a futures contract at \$118.00. The price differential is still \$0.95. If the Price Differential Spread Executor elects to use the Spread Settle Prices at the time it submits the order, OCC will initially record the front leg at \$117.90 and the back leg at \$116.95 (which is the \$117.90 contract price minus the price differential of \$0.95 because the front leg is the purchase of a futures contract).

Differential Spread traders require the flexibility to choose between the prices being used for clearing their Price Differential Spreads for purposes of allowing them to allocate trades among multiple customers at an equitable price similar to the average pricing functionality that already exists in OCC's trade allocation process and that the implementation of this new post-trade process will be consistent with existing practices in the futures industry. ELX also has informed OCC that Price Differential Spread transactions will not affect the prices at which trades are publicly reported.

Except in the case where the counterparty to a leg of a Price Differential Spread enters into the trade as part of its own Price Differential Spread and elects to record the trade using the Spread Settle Price, the counterparty sees the trade as an ordinary stand-alone futures transaction, and OCC will record the trade on behalf of the counterparty using the Spread Engine Price. Therefore, continuing the example, in a case where the Price Differential Spread Executor chooses to use the Spread Settle Prices for clearing a Price Differential Spread, the trades as recorded on OCC's books and records for the Price Differential Spread Executor will use a different set of prices (i.e., \$117.90 and \$118.85) from those recorded for counterparty A and counterparty B (i.e., \$118.00 and \$118.95). However, the aggregate amount of the variation payments that the Price Differential Spread Executor will pay to or collect from OCC will be the same (except for very small discrepancies due to rounding differences as described below) regardless of which set of prices is used to calculate variation payments because the price differential between the two legs of the Price Differential Spread is the same (i.e., \$0.95). Accordingly, and subject to the treatment of rounding differences as described in the following paragraphs, OCC's clearing system will be in balance because the variation payments due to or from the Price Differential Spread Executor on the futures contracts executed as part of the Price

Differential Spread will equal the amount due to or from the counterparties to those transactions on an aggregate basis even if not on a contract-by-contract basis.

When the Price Differential Spread Executor records the trades using the Spread Settle Prices, rounding the Spread Settle Prices to the nearest applicable minimum price increment when the initial variation payments on the trades are calculated may result in the Price Differential Spread Executor paying slightly more or receiving slightly less than it would have paid or received if it had elected to record the trades using the Spread Engine Prices. In either case the amount will be no more than one cent per contract. The amount by which the Price Differential Spread Executor receives slightly less or pays slightly more than it would have otherwise paid or received with respect to the trades will fund the amount by which other Price Differential Spread Executors are entitled to receive more or pay less as a result of OCC's rounding procedures.

While all such discrepancies in variation payments due to OCC's rounding procedures should net to zero when averaged over time, they may not net to precisely zero on any business day. Any net excess received by OCC on any business day will be contributed to a "Rounding Fund" and will be carried forward to fund any net amount that OCC may be required to pay on subsequent days. In order to ensure that there is always a sufficient positive balance in the Rounding Fund to fund any such net amount that may be owed by OCC, a cushion is needed. Accordingly, ELX has agreed in an amendment to the Clearing Agreement between OCC and ELX to provide OCC an initial amount of \$5,000 as a contribution to the Rounding Fund and to contribute additional amounts as reasonably required by OCC to provide a larger cushion should growth in product volume indicate such additional amounts are required. The Rounding Fund will be held by OCC in one or more bank accounts used by OCC to make daily cash settlements

with Clearing Members so that it will be automatically available to fund variation payments as needed and to eliminate the expense and operational risk of unnecessary funds transfers. OCC will maintain a record of the amount held in the Rounding Fund on OCC's own books and records. If at any time ELX ceases to clear transactions through OCC or ceases to permit Price Differential Spread transactions, OCC will pay any amount left in the Rounding Fund to ELX.

OCC proposes to make the following amendments to its By-Laws and Rules in order to accommodate clearance of Price Differential Spreads. OCC proposes to add a new Rule 1301A. to (1) define Price Differential Spreads,⁷ (2) require the listing exchange to include the Spread Engine Price and the Spread Settle Price and to identify (separately with respect to each counterparty to the trade, if applicable) which of the two prices is to be initially recorded as the contract price and the Price Differential Spread ID in each of the matched trade reports that the listing exchange sends to OCC with respect to Price Differential Spreads, (3) permit a Clearing Member to choose post trade the contract prices to be used for clearing its Price Differential Spread trades, and (4) highlight the rounding situation described above. OCC would also make a minor conforming amendment to Rule 1301.

In addition, OCC and ELX would enter into Amendment 1 to the Agreement for Clearing and Settlement Services dated December 5, 2008, between OCC and ELX to accommodate Price Differential Spreads. A copy of Amendment 1 is attached hereto as Exhibit 5.

OCC states that the proposed changes to OCC's By-Laws and Rules are consistent with the purposes and requirements of Section 17A of the Act⁸ because they effect a change in an

⁷ OCC also proposes to add the term "Price Differential Spread" to Article I of its By-Laws as a cross reference to Rule 1301A where the term is actually defined.

⁸ 15 U.S.C. 78q-1.

existing service of OCC that does not adversely affect the safeguarding of securities or funds in OCC's custody or control or for which OCC is responsible or significantly affect the respective rights or obligations of OCC or persons using its securities clearing services. The proposed rule change is not inconsistent with any rules of OCC including any rules proposed to be amended.

B. Self-Regulatory Organization's Statement on Burden on Competition

OCC does not believe that the proposed rule change will have any impact or impose any burden on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

OCC has not solicited or received written comments relating to the proposed rule change. OCC will notify the Commission of any written comments it receives.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act⁹ and Rule 19b-4(f)(4)¹⁰ because it effects a change in an existing service of a registered clearing agency that does not adversely affect the safeguarding of securities or funds in the custody or control of the clearing agency or for which it is responsible and does not significantly affect the respective rights or obligations of the clearing agency or persons using the service. At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

IV. Solicitation of Comments

⁹ Supra note 2.

¹⁰ Supra note 3.

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. 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 No. SR-OCC-2011-06 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 No. SR-OCC-2011-06. 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 proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change 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 such filings also will be available for inspection and copying at OCC's principal office and OCC's website (http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_11_06.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 No. SR-OCC-2011-06 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.¹¹

Cathy H. Ahn
Deputy Secretary

¹¹ 17 CFR 200.30-3(a)(12).