

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-78151; File No. SR-OCC-2016-003)

June 24, 2016

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Related to the Acceptance of Pass-Through Letters of Credit as a Form of Margin Asset

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 17, 2016, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared by OCC. OCC filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act³ and Rule 19b-4(f)(4)(ii) thereunder⁴ 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. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

The proposed rule change by OCC would amend OCC Rule 604 to permit pass-through letters of credit (“Pass-Through Letters of Credit”) as a form of margin asset to satisfy margin obligations for futures, futures options, and commodity options positions (collectively referred to as “futures positions”) held in segregated futures accounts and segregated futures professional accounts (collectively referred to as “segregated futures accounts”) that are not eligible to hold

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(iii).

⁴ 17 CFR 240.19b-4(f)(4)(ii).

positions in security futures.⁵ Capitalized terms not defined herein have the same meaning as set forth in the OCC By-Laws and Rules.

II. Clearing Agency's Statement of the 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 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 these statements.

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

(1) Purpose

The purpose of the proposed rule change is to amend OCC Rule 604 to permit Pass-Through Letters of Credit as a form of margin asset to satisfy margin obligations for positions held in segregated futures accounts that are not eligible to hold positions in security futures in order to provide futures market participants with the ability to deposit similar forms of collateral for segregated futures accounts at OCC as they could deposit at other futures clearinghouses. OCC Rule 604(c) allows Clearing Members to deposit letters of credit as a form of margin asset provided that such letters of credit meet the form prescribed by OCC and satisfy the robust eligibility requirements and risk controls enumerated under the Rule.⁶ OCC currently accepts

⁵ See OCC By-Laws Article I, Section 1.S.(5) and (6) defining segregated futures accounts and segregated futures professional accounts.

⁶ Rule 604(c) requires, among other things, that: (i) letters of credit must contain the unqualified commitment of the issuer to pay a specified sum of money to OCC within certain specified time periods; (ii) all letters of credit must be irrevocable; and (iii) OCC may draw upon a letter of credit at any time, whether or not the Clearing Member that deposited such letter of credit has been suspended by OCC or is in default with respect to

two party letters of credit as a form of margin asset under Rule 604(c), which are letters of credit issued by an OCC approved bank or trust on behalf of a Clearing Member, with OCC as beneficiary. Such letters of credit may be used by Clearing Members to meet margin obligations arising from positions held in any OCC account type.

Recently, certain futures market participants have inquired about using Pass-Through Letters of Credit as a form of margin asset at OCC. Pass-Through Letters of Credit are letters of credit issued on behalf of a third party (in this case, a customer of a Clearing Member) with a joint beneficiary structure that would allow the Clearing Member, as a joint beneficiary, to “pass through” the letter of credit directly to the clearinghouse, as joint beneficiary, and avoid the need for the Clearing Member to write its own letter of credit to the clearinghouse or to deposit cash margin on behalf of the customer. Pass-Through Letters of Credit are standard collateral vehicles accepted by other futures clearinghouses, particularly clearinghouses that provide clearance and settlement services for energy futures products. In order to provide OCC’s futures commission merchant (“FCM”) Clearing Members with the ability to deposit similar forms of collateral for segregated futures accounts as they could deposit at other futures clearinghouses,

any obligation to OCC, if OCC determines that such draw is advisable to protect OCC, other Clearing Members, or the general public. Moreover, if a Clearing Member deposits a letter of credit that indicates on its face that it is being deposited to serve as margin for the Clearing Member’s customers’ account or for a segregated futures account, such letter of credit shall not constitute margin for any other account maintained by the Clearing Member until such time as the issuing bank shall instruct OCC by amendment to the letter of credit stating that such letter of credit is not so restricted. *See* OCC Rule 604(c)(1) and (3). Letters of credit are also subject to specific eligibility standards for issuing banks and both Clearing Member and issuer concentration limits. Specifically, no more than 50% of a Clearing Member’s margin on deposit at any given time may include letters of credit in the aggregate, and no more than 20% may include letters of credit issued by any one institution. Moreover, the total amount of letters of credit issued for the account of any one Clearing Member by a U.S. or Non-U.S. institution shall not exceed 15% of such institution’s Tier 1 Capital. *See* OCC Rule 604, Interpretations and Policies .01, .02, and .04.

OCC proposes to add new Interpretation and Policy .10 to Rule 604 to permit its FCM Clearing Members to deposit Pass-Through Letters of Credit as margin assets to satisfy margin requirements for their futures customers. Pass-Through Letters of Credit would be permitted only to satisfy margin obligations for positions held in segregated futures accounts and would not be available as a form of margin asset to satisfy margin obligations for securities products.⁷

Pass-Through Letters of Credit would be subject to the same requirements and risk controls of Rule 604 as the currently accepted two party letters of credit. Pass-Through Letters of Credit deposited as margin assets would be based on the industry standard *Unified Clearing Group Uniform Letter of Credit Terms – (Pass-Through)*, would be consistent with terms accepted by other futures clearinghouses, and would work similarly to the two party letters of credit currently used by OCC Clearing Members. Specifically, the issuing bank would be required to notify OCC of any changes to the terms of the letter of credit (and in certain cases, OCC would be required to affirmatively accept such changes) prior to such changes becoming effective. The issuing bank would be required to inform OCC in the event that a Clearing Member beneficiary wished to draw on the letter of credit, and all potential draws on the letter of credit, regardless of who initiates them, would be deposited directly into the FCM Clearing Member's OCC segregated futures account and would be subject to all of the rules and limitations surrounding the use and withdraw [sic] of margin funds under OCC's Rules. For these reasons, OCC believes that Pass-Through Letters of Credit, under the terms and restrictions

⁷ In connection with the proposed rule change, OCC would implement procedural checks and verifications in its Collateral Services and Member Services Departments to ensure that (1) Pass-Through Letters of Credit would not be permitted to be allocated to a segregated futures account unless that account is not eligible to hold positions in security futures and (2) accounts holding Pass-Through Letters of Credit as a form of margin asset would not be enabled to hold positions in security futures.

described above, are similar to the existing two party letters of credit currently on deposit as margin assets at OCC and do not raise any unique risks to OCC.

In addition, existing Interpretations and Policies .10-.16 to Rule 604 would be renumbered but otherwise remain unchanged

(2) Statutory Basis

OCC believes that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act,⁸ and the rules thereunder applicable to OCC. As noted above, the form of Pass-Through Letters of Credit that would be accepted by OCC would have terms that work similarly to the two party letters of credit currently used by OCC Clearing Members and would be subject to the same restrictions and safeguards contained in Rule 604 and the Interpretations and Policies thereunder.⁹ These safeguards include, among other things, that letters of credit deposited as margin assets have an unqualified commitment of the issuer to pay OCC within certain specified time periods, that all letters of credit must be irrevocable, and that OCC may draw upon a letter of credit at any time, whether or not the Clearing Member that deposited such letter of credit has been suspended by OCC or is in default with respect to any obligation to OCC. Moreover, the issuer and concentration limits for letters of credit deposited as margin assets are designed to ensure that OCC does not have excessive exposure to a particular issuing bank or to letters of credit generally as a form of margin asset. These requirements are designed to minimize the risk of loss or delay in OCC's access to funds payable under the letter of credit and reduce the likelihood that OCC would need to use the mutualized resources in its Clearing Fund to fulfill obligations arising from Clearing Members depositing letters of credit as a form of margin asset.

⁸ 15 U.S.C. 78q-1(b)(3)(F).

⁹ *See supra* note 6 and related text.

In addition to the restrictions and safeguards under Rule 604, the terms of the Pass-Through Letters of Credit would require that they effectively operate similarly to the two party letters of credit currently on deposit as margin assets at OCC. For example, OCC must be notified of (and in certain cases must affirmatively accept) any changes to the terms of the letter of credit, the issuing bank would be required to inform OCC in the case that the Clearing Member beneficiary wished to draw on the letter of credit, and all potential draws on the letter of credit, regardless of who initiates them, would be deposited directly into the FCM Clearing Member's segregated futures account.

For the reasons stated above, OCC believes that the proposed rule change is designed to assure the safeguarding of securities and funds which are in the custody or control of OCC or for which it is responsible in accordance with Section 17A(b)(3)(F) of the Act¹⁰ and is reasonably designed to ensure that OCC holds margin assets in a manner that minimizes risk of loss or delay in its access to them, consistent with Rule 17Ad-22(d)(3).¹¹ The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended.

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

OCC does not believe that the proposed rule change would have any impact or impose any burden on competition¹² not necessary or appropriate in furtherance of the Act because it pertains solely to OCC's activities relating to the clearing of commodity futures products subject to the exclusive jurisdiction of the CFTC and therefore would not have any impact or impose any burden on competition in securities markets or any other market governed by the Act.

¹⁰ 15 U.S.C. 78q-1(b)(3)(F).

¹¹ 17 CFR 240.17Ad-22(d)(3).

¹² 15 U.S.C. 78q-1(b)(3)(I).

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

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

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

The foregoing rule change has become effective upon filing¹³ pursuant to Section 19(b)(3)(A)(iii) of the Act¹⁴ and Rule 19b-4(f)(4)(ii) thereunder¹⁵ because it effects a change in an existing service of OCC that (i) primarily affects the clearing operations of OCC with respect to products that are not securities, including futures that are not security futures and (ii) does not significantly affect any securities clearing operations of OCC or any rights or obligations of OCC with respect to securities clearing or persons using such securities-clearing 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

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:

¹³ Notwithstanding the immediate effectiveness of the proposed rule change, implementation of this rule change is also contingent on it being deemed certified under CFTC Regulation §40.6.

¹⁴ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁵ 17 CFR 240.19b-4(f)(4)(ii).

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-2016-003 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-2016-003. 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 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.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_16_003.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-2016-003 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.¹⁶

Brent J. Fields
Secretary

¹⁶ 17 CFR 200.30-3(a)(12).