

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-51826; File No. SR-OCC-2004-17)

June 13, 2005

Self-Regulatory Organizations; The Options Clearing Corporation; Order Granting Approval of a Proposed Rule Change Relating to Calculating Net Capital under OCC Rule 307

I. Introduction

On September 27, 2004, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR-OCC-2004-17 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”).<sup>1</sup> Notice of the proposal was published in the Federal Register on April 18, 2005.<sup>2</sup> No comment letters were received. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

II. Description

The proposed rule change amends OCC Rule 307 by adopting Interpretation and Policy .01 (“IP .01”) thereunder that would require clearing members that could otherwise take advantage of Commission Rule 15c3-1(a)(6) under the Act to include the risk-based haircuts associated with proprietary securities positions in determining their compliance with OCC’s minimum net capital requirements.

OCC Rule 307 requires a clearing member to compute its “net capital,” “aggregate indebtedness,” and “debt-equity total” in accordance with Commission Rule 15c3-1 under the

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> Securities Exchange Act Release No. 51521, (April 11, 2005), 70 FR 20198.

Act for purposes of OCC Rules.<sup>3</sup> New IP .01 under OCC Rule 307 will require clearing members that could otherwise take advantage of Commission Rule 15c3-1(a)(6) to deduct the risk-based haircuts associated with proprietary securities positions in determining their compliance with OCC's minimum net capital requirements.<sup>4</sup> Although the exemption in Rule 15c3-1(a)(6) from the securities haircuts in Rule 15c3-1(c)(2)(vi) and Appendix A under Rule 15c3-1 ensures from a systemic standpoint that capital exists to support open positions, it does not ensure that capital is maintained in the entity to which OCC has credit exposure. As a result, OCC is exposed to the volatility of the positions relative to the clearing member's net income without any reserve against net capital. OCC believes that the exemption in Rule 15c3-1(a)(6) gives those clearing members added leverage enabling them to expand positions to several times their net capital.

In order to provide an adjustment period for those clearing members that may be affected by IP .01, IP .01 will not take effect until July 27, 2005, for firms that are clearing members at the time when it becomes effective.

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<sup>3</sup> OCC Rule 307 provides that a clearing member that is registered as a futures commission merchant and is not otherwise required to calculate net capital in accordance with Rule 15c3-1 may instead calculate net capital as required under the rules of the Commodity Futures Trading Commission.

<sup>4</sup> Rule 15c3-1 requires that every broker or dealer maintain net capital no less than the minimum net capital as set forth by the rule. Paragraph (c) of the rule defines net capital as the net worth of a broker or dealer, adjusted by among other things, securities haircuts that are set forth in paragraph (c)(vi) and appendix A of the rule. Paragraph (a)(6) allows market makers, specialists, and certain other dealers to elect to apply paragraph (a)(6)(iii) in lieu of paragraph (c)(vi) or Appendix A under Rule 15c3-1. In general, paragraph (a)(6)(iii) requires that a dealer maintain a liquidating equity with respect to securities positions in his market maker or specialist account at least equal to 25 percent of the market value of the long positions and 30 percent of the market value of the short positions.

### III. Discussion

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible.<sup>5</sup> The proposed rule change imposes a more stringent net capital requirement than is currently in OCC's rules for the purpose of assuring that OCC has collected sufficient capital from its members in relation to such members' clearance and settlement activity. The Commission is satisfied with OCC's explanation that for purposes of OCC's minimum net capital requirement those members that qualify for the exemption in Rule 15c3-1(a)(6) should be required to deduct the risk based haircuts in Rule 15c3-1(c)(2)(vi) and Appendix A under Rule 15c3-1. This more conservative approach to minimum net capital requirements should better enable OCC to protect itself and its members from the potential losses associated with insolvency situations. Accordingly, the Commission finds that the proposed rule change is designed to assure the safeguarding of securities and funds which are in OCC's custody or control or for which OCC is responsible.

### IV. Conclusion

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

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-OCC-2004-17) be and hereby is approved.

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<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>6</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>6</sup> 17 CFR 200.30-3(a)(12).

