

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-69026; File No. SR-OCC-2013-02]

### Self-Regulatory Organizations; the Options Clearing Corporation; Notice of Filing of Proposed Rule Change To Implement a Revised Method of Calculating Clearing Members' Respective Contributions to OCC's Clearing Fund

March 4, 2013.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder<sup>2</sup> notice is hereby given that on February 19, 2013, 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 primarily by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

OCC proposes to implement a revised method of calculating clearing members' respective contributions to OCC's clearing fund.

#### II. Self-Regulatory Organization'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 such statements.<sup>3</sup>

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

The purpose of this proposed rule change is to revise OCC's By-Laws and Rules to implement a revised method of calculating clearing members' respective contributions to OCC's clearing fund. Currently, clearing members contribute to the clearing fund in proportion to

average daily open interest, i.e., the total number of cleared contracts and open positions plus units of stock underlying open stock loan or borrow positions, over the calendar month preceding the date of calculation, subject to a \$150,000 minimum contribution. There are exceptions for a small number of Execution-Only Clearing Members,<sup>4</sup> which are required to make a minimum contribution equal to \$150,000 plus the product of \$15 per contract multiplied by the average daily volume of the Execution-Only Clearing Member over the previous calendar month, and for newly-admitted Clearing Members, whose initial contribution is fixed by OCC's Board of Directors.

OCC has developed a new allocation formula that it believes would more equitably allocate contributions among its clearing members based on each clearing member's particular activities and use of OCC's facilities. The revised formula would include the following components: (1) Open interest; (2) total risk charge; and (3) volume.<sup>5</sup> The total risk charge and volume components would be new components of the allocation formula. The Commission recently noted in publishing its Clearing Agency Standards, "registered clearing agencies must evaluate continually and make appropriate updates and improvements to their operations and risk management practices \* \* \*."<sup>6</sup> OCC believes that these proposed enhancements to its existing clearing fund allocation formula are consistent with this notion of continual evaluation and refinement.

OCC believes that the 1980 Standards for the Registration of Clearing Agencies issued by the staff of the Securities and Exchange Commission supports the idea that clearing members' use of the services of a clearing agency forms an appropriate basis on which clearing members should correspondingly be required to participate in the obligations of the clearing agency's risk management framework.<sup>7</sup> Use of a

clearing agency by its clearing members may be measured in a number of ways.

OCC believes that its proposed allocation formula is preferable to its current formula because, by incorporating measurements of volume and certain risk charges, it would apportion contributions based on more sophisticated measurements of clearing members' usage of OCC's facilities. OCC believes that clearing member volume and risk charges would recognize demands on OCC's services and facilities that are not captured by open interest alone. OCC believes that the new formula would incorporate open interest, total risk charge, and volume, in proportions that are designed to equitably allocate clearing fund requirements in light of these additional demands. Specifically, open interest, total risk charge, and volume would have weightings of 50%, 35%, and 15%, respectively. OCC contemplated alternative weightings in its decision to propose this particular allocation method but believes that the proposed formula is appropriate because it would give significant weight to the new volume and risk charge components and tie allocations more closely to demands placed by clearing members on OCC's facilities. While the revised formula would result in significant reallocations of contributions, OCC does not expect that it would unduly burden those clearing members anticipated to experience increased contributions.

OCC believes it is appropriate for open interest to continue to serve as the most heavily weighted component because open interest, generally speaking, is a measure of a clearing member's overall usage of OCC's facilities. With respect to open interest, the definition of open interest in proposed Rule 1001(d) is not identical to the definition of open interest in existing Rule 1001(b), which OCC proposes to delete. However, OCC believes that the differences in these two definitions are not material and are the result of the use of the defined term "cleared contract" in proposed Rule 1001(d) instead of specifically naming the individual types of contracts that make up "cleared contracts," as well as general updating and restructuring of the rule provision.

OCC also believes that risk and volume are relevant factors because they distinctly measure material aspects of clearance and settlement activity and therefore a clearing member's use of OCC's resources. Each clearing

rules such as clearing fund deposits, mark-to-the-market payments and margin deposits related to the service used").

<sup>4</sup> Article I of OCC's By-Laws define Execution-Only Clearing Members as those approved to act only as a Clearing Member that transfers confirmed trades or allocates positions to other Clearing Members and not to carry positions in its accounts with OCC on a routine basis.

<sup>5</sup> Because Execution-Only Clearing Members do not clear their own trades, the measure of volume applicable to them would be executed volume rather than cleared volume.

<sup>6</sup> Securities Exchange Act Release No. 34-68080 (October 22, 2012), 77 FR 66220 (November 2, 2012).

<sup>7</sup> Securities Exchange Act Release No. 34-16900 (June 17, 1980); 45 FR 41920 (June 23, 1980) (providing in pertinent part that "all participants utilizing similar clearing agency services \* \* \* should be required to comply fully with the clearing agency's internal financial and operational

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

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> The Commission has modified the text of the summaries prepared by OCC.

member's contribution to the clearing fund should therefore take these measures of usage of OCC's facilities into account. OCC notes that clearing members whose OCC accounts contain positions that are well-diversified and/or exhibit relatively little exposure to overall market direction would likely have a smaller required contribution under the proposed formula. Clearing members exhibiting a relatively large exposure to market direction, a concentration in contracts that individually present high amounts of risk, and undiversified accounts would generally experience a larger required contribution than is the case under the current formula.

OCC believes that the inclusion of risk and volume metrics within OCC's clearing fund allocation formula would generally reflect similar practices that are already in place at other registered clearing agencies. OCC believes that these existing allocation practices of other clearing agencies represent a meaningful benchmark of practices that are used across the industry. Taking those practices into account, OCC evaluated the appropriateness of including these mechanisms in its own allocation formula in a way that is tailored to the nature and demands of OCC's particular business. OCC understands that one clearing agency allocates contributions among its affected clearing members using certain measures of volume and open interest in addition to considering margin requirements over a given period.<sup>8</sup> The rules of another clearing agency provide that clearing member contributions to its clearing fund are determined according to a wide variety of risk-based charges meant to account for the ways in which clearing members utilize its services.<sup>9</sup>

<sup>8</sup> See *CME Clearing Financial Safeguards*, (2012) (explaining that CME Group maintains three separate clearing funds that correspond to the different asset classes for which it provides clearance and settlement services and that the allocation method for each clearing fund is distinct), available at <http://www.cmegroup.com/clearing/files/financialsafeguards.pdf>.

<sup>9</sup> See *National Securities Clearing Corporation Rules and Procedures*, (September 4, 2012) Procedure XV. Clearing Fund Formula and Other Matters (providing that allocation of the clearing fund contributions for National Securities Clearing Corporation participants involves risk-based charges that include, but are not limited to, (1) Value-at-Risk to determine the potential future exposure of a given portfolio based on historical price movements; (2) mark-to-market to measure unrealized profit or loss of unsettled securities positions; (3) a fail charge to account for transactions that do not settle; and (4) other special charges to address any volatility or lack of liquidity in a security), available at [http://www.dtcc.com/legal/rules\\_proc/nscc\\_rules.pdf](http://www.dtcc.com/legal/rules_proc/nscc_rules.pdf).

OCC's intends that its proposed total risk charge would measure the economic significance of the activities of a clearing member. The total risk charge is equal to the margin requirement, as determined by OCC, of the accounts of the clearing member exclusive of the net asset value of those accounts. OCC notes that a range of factors influence the relationship between the open interest in a clearing member's account and its associated risk charge. For example, for each clearing member these factors include, but are not limited to, the types of positions, number of long positions versus short positions, value of the securities underlying the contracts, volatility of the underlying, diversification, number of accounts of the clearing member, and the extent to which the clearing member's options positions are in-the-money or out-of-the-money.

Volume, like open interest, is a measure of a clearing member's level of usage of OCC's facilities. However, volume is distinct from open interest in that it is a function of the average turnover of the positions in the clearing member's account. Therefore, market-making, high frequency trading, and execution-only services are all examples of activities that tend to elevate volume relative to open interest. By contrast, holding long term positions in long term contracts is an example of activity that would lower a clearing member's volume relative to its open interest.

OCC notes that most Clearing Member Groups<sup>10</sup> will experience a material change (i.e., an increase or decrease of 10% or greater in the dollar amount of a Clearing Member Group's aggregated Clearing Fund requirement) under the new formula. The majority of the Clearing Member Groups that would experience a material change increase in Clearing Fund requirements are smaller single firms with lower initial Clearing Fund requirements. OCC notes that small firms tend to experience an increase under the new allocation formula for two reasons. First, smaller firms often have portfolios lacking the diversification that lowers the risk compared with open interest for larger firms. Second, firms that have a small fraction of combined open interest, total risk, and volume, experience increases simply due to the fact that the new formula adds a clearing fund share on top of the \$150,000 minimum as opposed to instead of it. To allow firms that would face a substantial increase in

<sup>10</sup> The term "Clearing Member Group" is defined in OCC's By-Laws as a Clearing Member and any Member Affiliates of such Clearing Member.

their clearing fund requirements adequate time to prepare for the proposed changes, OCC would provide all clearing members significant lead time, as described below, before implementing the new formula and would also use an incremental approach to implementation that would phase in the percentage weightings applicable to each component. OCC believes that this approach would provide clearing members with an important opportunity to secure any additional funds that they anticipate would be necessary in connection with the requirements of the new formula or to otherwise modify their activities, for instance by reducing positions, to manage the impact of the new formula.

The Clearing Fund requirements under the new allocation formula will be communicated to the clearing membership prior to the time they become effective to allow clearing members to review and prepare for any changes they may experience in their specific Clearing Fund contribution amount. OCC will contact those clearing members that will be negatively impacted in a material manner (i.e., an increase of 10% or greater in the dollar amount of a Clearing Member Group's aggregate Clearing Fund requirement) to confirm such clearing members have reviewed the pro forma Clearing Fund requirement numbers and they are ready to meet the new requirement upon implementation. OCC will then begin a two stage phase in process for the new Clearing Fund requirements. The first stage of implementation will occur within 180 calendar days from the date that OCC provides notice to clearing members of its intent to implement the new formula. At that stage, open interest, total risk charge, and volume would be applied in the formula with weightings of 75%, 17.5%, and 7.5%, respectively. The second stage of implementation and the final weightings of 50%, 35%, and 15% would then be implemented within 360 days from the same date of the original notice to clearing members concerning implementation of the new formula.

The proposed rule change would also create a defined term in OCC's By-Laws, "Futures-Only Affiliated Clearing Member," to refer to a clearing member that is admitted solely for the purpose of clearing transactions in security futures, commodity futures, and/or futures options.<sup>11</sup> While the definition

<sup>11</sup> Article VIII, Section 2 of OCC's By-Laws actually refers also to "commodity options," but options directly on an underlying commodity—as opposed to options on futures—are now included in Section 1a(47) of the Commodity Exchange Act

is new, there would be no substantive change to Section 2 of Article VIII, under which, if such a clearing member is a member affiliate of an earlier-admitted clearing member, the clearing member's initial clearing fund contribution may be fixed by the Board as an amount that excludes the minimum clearing fund component of \$150,000, so long as the earlier-admitted clearing member already satisfies that requirement.

OCC believes that the proposed rule change is consistent with Section 17A of the Securities Exchange Act of 1934 ("Act")<sup>12</sup> and the rules and regulations thereunder because the proposed modifications would help ensure that the Rules of OCC "provide for the equitable allocation of reasonable dues, fees, and other charges among its participants"<sup>13</sup> and thereby promotes prompt and accurate clearance and settlement<sup>14</sup> by enhancing the clearing fund allocation methodology to continue to account for open interest but also to additionally use risk charges and volume to account for other exposures to OCC that result from clearing member activities.

*(B) Self-Regulatory Organization's Statement on Burden on Competition*

OCC does not believe that the proposed rule change would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

*(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others*

Written comments 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**

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve or disapprove the proposed rule change or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

**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:

*Electronic Comments*

- Use the Commissions Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-OCC-2013-02 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 Number SR-OCC-2013-02. This file number should be included on the subject line if email 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 Web site (<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 Web site viewing and printing in the Commission's Public Reference Section, 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 will also be available for inspection and copying at the principal office of OCC and on OCC's Web site at [http://www.theocc.com/components/docs/legal/rules\\_and\\_bylaws/sr\\_0cc\\_13\\_02.pdf](http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_0cc_13_02.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-2013-02 and should

be submitted on or before March 29, 2013.

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

**Kevin M. O'Neill,**  
*Deputy Secretary.*

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**SECURITIES AND EXCHANGE COMMISSION**

**[Release No. 34-69018; File No. SR-BATS-2013-013]**

**Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Related to Mini Options**

March 1, 2013.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 20, 2013, BATS Exchange, Inc. ("BATS" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange filed a proposal for the BATS Options Market ("BATS Options") to list and trade option contracts overlying 10 shares of a security ("Mini Options").

The text of the proposed rule change is available at the Exchange's Web site at <http://www.batstrading.com>, at the principal office of the Exchange, and at the Commission's Public Reference Room.

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

In its filing with the Commission, the Exchange 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. The Exchange has prepared summaries, set

to fall within the definition of a "swap." 7 U.S.C. 1a(47). Since OCC does not currently have rules for the clearing of swaps, the reference to commodity options is being omitted from the new definition.

<sup>12</sup> 15 U.S.C. 78q-1.

<sup>13</sup> 15 U.S.C. 78q-1(b)(3)(D).

<sup>14</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>15</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> 17 CFR 240.19b-4.