



March 15, 2016

VIA ELECTRONIC MAIL

Christopher J. Kirkpatrick
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Rule Filing SR-OCC-2016-006 Rule Certification

Dear Secretary Kirkpatrick:

Pursuant to Section 5c(c)(1) of the Commodity Exchange Act, as amended (“Act”), and Commodity Futures Trading Commission Regulation (“CFTC”) 40.6, enclosed is a copy of the above-referenced rule filing submitted by The Options Clearing Corporation (“OCC”). The date of implementation of the rule is at least 10 business days following receipt of the rule filing by the CFTC or the date the proposed rule is approved by the Securities and Exchange Commission (the “SEC”) or otherwise becomes effective under the Securities Exchange Act of 1934 (the “Exchange Act”). This rule filing has been, or is concurrently being, submitted to the SEC under the Exchange Act.

In conformity with the requirements of Regulation 40.6(a)(7), OCC states the following:

Explanation and Analysis

This proposed rule change by OCC is designed to enhance the overall resilience of OCC’s Stock Loan/Hedge Program¹ by allowing OCC to close out the Matched-Book Positions (as defined herein) of Hedge Clearing Members requesting an orderly wind down of Matched-Book Positions through the termination by offset and “re-matching” of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC’s rules. The proposed termination by offset and re-matching of stock loan and borrow positions is designed to leave the affected Clearing Members with the same net position in such stock loan and borrow positions as prior to the adjustment.

¹ See Article XXI of OCC’s By-Laws and Chapter XXII of OCC’s Rules. It is also noted that no changes are being proposed to Article XXIA of OCC’s By-Laws or Chapter XXIIA of OCC’s Rules which address OCC’s Market Loan Program.

Background

In the Stock Loan/Hedge Program, OCC acts as a central counterparty (“CCP”) for Hedge Loans that are directly negotiated by Hedge Clearing Members and sent to OCC for clearance and settlement. A prospective Lending Clearing Member and a prospective Borrowing Clearing Member identify each other (independent of OCC) and agree on the terms of the stock loan. The Hedge Clearing Members then send the details of the stock loan to The Depository Trust Company (“Depository”) with a certain “reason code,”² which designates the stock loan as a Hedge Loan for guaranty and clearance at OCC. The Lending Clearing Member instructs the Depository to transfer a specified number of shares of Eligible Stock to the account of the Borrowing Clearing Member, and the Borrowing Clearing Member instructs the Depository to transfer the appropriate amount of cash collateral to the account of the Lending Clearing Member.³ The Depository then sends the Hedge Loan information to OCC via an end-of-day report.⁴ After OCC receives the report from the Depository, OCC validates and novates the stock loan transaction and becomes the lender to the Borrowing Clearing Member and the borrower to the Lending Clearing Member.⁵

After novation, as part of the guaranty, OCC makes Mark-to-Market Payments for all Hedge Loans on a daily basis to collateralize all loans to the negotiated levels.⁶ As the CCP, OCC guarantees the return of the full value of cash collateral to a Borrowing Clearing Member and the Loaned Stock, or value of that Loaned Stock, to the Lending Clearing Member. Settlements generally are combined and netted against other OCC settlement obligations in a Hedge Clearing Member’s account, including trade premiums and margin deficits. A Hedge Clearing Member’s open positions in the Stock Loan/Hedge Program are factored into the Hedge Clearing Member’s overall Margin⁷ and Clearing Fund contribution requirements.⁸ A significant portion of the activity in OCC’s stock lending programs relates to what is often referred to as matched-book activity where a Hedge Clearing Member maintains in an account a stock loan position for a specified number of shares of an Eligible Stock reflecting a stock

² Unique reason codes were created by the Depository for Clearing Members to designate stock loan transactions intended to be sent to OCC for novation and guarantee.

³ See OCC Rule 2202(a).

⁴ See OCC Rule 2202(b).

⁵ *Id.*

⁶ Mark-to-Market Payments are based on the value of the loaned securities and made between Clearing Members using OCC’s cash settlement system. The percentage of the value of the loaned securities, either 100% or 102%, is dependent upon the agreement between the two Hedge Clearing Members party to the transaction.

⁷ See OCC Rules 601 and 2203.

⁸ See OCC Rule 1001.

lending transaction with one Hedge Clearing Member (the Borrowing Clearing Member) and also maintains in that same account a stock borrow position for the same number, or lesser number, of shares of the same Eligible Stock with another Hedge Clearing Member (the Lending Clearing Member) (such positions being "Matched-Book Positions"). From a daily mark-to-market settlement perspective, there are typically no obligations related to Matched-Book Positions because the member is simultaneously borrowing and lending the same securities (and quantity), which are marked to the same price. OCC's margin process recognizes this and currently nets loans and borrows in the same security prior to calculating exposure, resulting in no margin on a perfectly matched position.

Currently, in order for a Hedge Clearing Member to close out its stock loan positions, including Matched-Book Positions, the Hedge Clearing Member is required to terminate its loans through instructions issued to the Depository to transfer a specified quantity of the loaned stock against payment of the settlement price in accordance with the process prescribed in Rule 2208. Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions that wish to maintain equivalent stock loan positions at OCC would then be required to initiate new stock loans, through the process described above, in accordance with Rule 2202. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and settle those transactions, which introduce the potential for market disruption. For example, because OCC maintains stock loan inventory on a bilateral basis (i.e., maintains the borrower and lender to a transaction) and guarantees the return of cash collateral and the Loaned Stock, or price of the Loaned Stock, if a Hedge Clearing Member with Matched-Book Positions fails to fulfill its obligations for the recall of loans and return of borrowed shares, there would be a temporary imbalance of the previously "matched-book" position. In addition, the successful initiation of new replacement stock loans for the Borrowing or Lending Clearing Members could be subject to disruption by operational or execution risks, with the result that one "leg" of the initiating transaction would fail. Moreover, the Borrowing and Lending Clearing Members lose the protections afforded by OCC's guaranty of their stock loan positions until the newly initiated stock loan positions have been accepted, novated, and guaranteed by OCC.

The proposed rule change would permit a Hedge Clearing Member to request the orderly wind down of Matched-Book Positions, subject to the agreement of all affected Borrowing and Lending Clearing Members, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC Rules 2202, 2208 and 2209. OCC believes the proposed rule change would eliminate the potential risks described above associated with the transfer of securities and funds and provide the overall marketplace with more stability with respect to the process of voluntarily closing out Matched-Book Positions in the Stock Loan/Hedge Program.

Voluntary Termination by Offset and Re-Matching

OCC proposes to amend its By-Laws and Rules to permit a Hedge Clearing Member to request an orderly wind down of its Matched-Book Positions, contingent upon the explicit

agreement of the requesting Hedge Clearing Member, its counterparty Borrowing Clearing Member, and counterparty Lending Clearing Member, and at the sole discretion of OCC, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC's rules. First, OCC proposes to amend Article I of its By-Laws to add new defined terms "Matched-Book Borrowing Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that borrows Eligible Stock from a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock and "Matched-Book Lending Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that lends Eligible Stock to a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock. OCC also proposes to add a new definition for "Matched-Book Positions," which would be defined as Hedge Loan positions in which a single Hedge Clearing Member borrows Eligible Stock from its Matched-Book Lending Clearing Member and lends an equal or lesser amount of the same Eligible Stock to its Matched-Book Borrowing Clearing Member.

In addition, OCC proposes to amend Rule 2208 to adopt new rules for the voluntary termination by offset and re-matching of Matched-Book Positions. Specifically, OCC proposes to adopt new Rule 2208(e)(1), which would provide that a Hedge Clearing Member may submit a written request to OCC to effect one or more position adjustments to terminate by offset all or some of its Matched-Book Positions if the following conditions are met. First, the requesting Hedge Clearing Member, its Matched-Book Lending Clearing Member, and its Matched-Book Borrowing Clearing Member have furnished to the Corporation their written agreement to (i) the termination by offset of such Matched-Book Positions maintained in the requesting Hedge Clearing Member's account and (ii) the Corporation's re-matching the stock borrow position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Borrowing Clearing Member against the stock loan position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Lending Clearing Member. Second, the written agreement furnished by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member must be in the form specified by OCC. Third, the written request to terminate by offset and to re-match stock loan and borrow positions may be for less than the total number of shares of the Eligible Stock that is the subject of the stock loan and borrow positions maintained, as applicable, by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member, but must be for an equal number of shares.

Additionally, proposed Rule 2208(e)(2) would provide that, if OCC in its sole discretion approves the requested termination by offset and re-matching of positions, the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member would not be required to issue instructions to the Depository to terminate such stock loans and stock borrow positions maintained in the Stock Loan/Hedge Program or to initiate new stock lending transactions for inclusion in the Stock Loan/Hedge Program as currently required under Rules 2202(a) and 2208(a).

Proposed Rules 2208(e)(3) and (4) would provide that, from and after the time OCC has completed the requested position adjustments to terminate by offset and re-match the specified stock loan and borrow positions, the requesting Hedge Clearing Member would have no further obligation under the By-Laws and Rules with respect to such positions; however, the Borrowing Clearing Member with re-matched stock borrow positions remains obligated as a Borrowing Clearing Member and the Lending Clearing Member with re-matched stock loan positions remains obligated as a Lending Clearing Member with respect to the re-matched positions as specified in the By-Laws and Rules applicable to the Stock Loan/Hedge Program.

Proposed Rule 2208(e)(5) would require the requesting Hedge Clearing Member and re-matched Borrowing Clearing Member and Lending Clearing Member to make any necessary bookkeeping entries at the Depository necessitated by the termination by offset and re-matching upon notification that the termination by offset and re-matching has been completed as set forth in proposed Rule 2209(h).

In addition, OCC proposes to adopt new Rule 2209(h) to specify that, in the event of a termination by offset and re-matching of a stock loan under proposed Rule 2208(e), such termination by offset and re-match shall be complete upon OCC completing all position adjustments in the accounts of the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member in accordance with Rule 2208(e) and the earlier of (i) communicating confirmation of the transaction in the form of direct written communications with the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member or (ii) when systems reports are produced and provided to the Clearing Members reflecting the transaction.

OCC also proposes conforming and clean-up changes to Article XXI, Sections 2, 3 and 4 of its By-Laws. Article XXI, Section 2 would be revised to (i) account for the netting of stock loan and stock borrow positions during the voluntary termination by offset and re-matching of Matched-Book Positions in accordance with proposed Rule 2208(e) and (ii) make clean-up changes to ensure the consistent use of the defined term "Eligible Stock." Additionally, Article XXI, Sections 3 and 4 would be revised to state that the voluntary termination by offset of Matched-Book Positions in accordance with proposed Rule 2208(e) would be excluded from the requirement to pay the settlement price against delivery of the Loaned Stock as currently required for all terminations under OCC's existing rules.

OCC reviewed the derivatives clearing organization ("DCO") core principles ("Core Principles") as set forth in the Act. During this review, OCC identified the following Core Principles as potentially being impacted:

Risk Management. OCC believes that by implementing the proposed rule change it will be better able to manage the risks associated with discharging its responsibilities as set forth in

Christopher J. Kirkpatrick

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the DCO Core Principles because it would eliminate the potential execution and operational risks associated with the termination and re-initiation of Matched-Book Positions by allowing Hedge Clearing Members to terminate by offset and re-match Matched-Book Positions without requiring the transfer of securities and funds. In addition, OCC would provide the public with information about the voluntary close out of Matched-Book Positions in the Stock Loan/Hedge Program so that parties may more accurately identify any potential risks associated with using OCC's Stock Loan/Hedge Program services.

Opposing Views

No opposing views were expressed related to the rule amendments.

Notice of Pending Rule Certification

OCC hereby certifies that notice of this rule filing has been given to Clearing Members of OCC in compliance with Regulation 40.6(a)(2) by posting a copy of the submission on OCC's website concurrently with the filing of this submission.

Certification

OCC hereby certifies that the rule set forth at Item 1 of the enclosed filing complies with the Act and the CFTC's regulations thereunder.

Should you have any questions regarding this matter, please do not hesitate to contact me.

Sincerely,



Justin W. Byrne
Vice President, Regulatory Filings

Enclosure

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 19b-4

Proposed Rule Change

by

THE OPTIONS CLEARING CORPORATION

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

Item 1. Text of the Proposed Rule Change

This proposed rule change by The Options Clearing Corporation (“OCC”) is designed to enhance the overall resilience of OCC’s Stock Loan/Hedge Program¹ by allowing OCC to close out the Matched-Book Positions (as defined herein) of Hedge Clearing Members requesting an orderly wind down of Matched-Book Positions through the termination by offset and “re-matching” of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC’s rules. All capitalized terms not defined herein have the same meaning as in OCC’s By-Laws and Rules. Material proposed to be added to OCC’s By-Laws and Rules as currently in effect is marked by underlining and material proposed to be deleted is enclosed in bold brackets.

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THE OPTIONS CLEARING CORPORATION**BY-LAWS**

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ARTICLE I – Definitions**Definitions**

SECTION 1. Unless the context requires otherwise (or except as otherwise specified in the By-Laws or Rules), the terms defined herein shall, for all purposes of these By-Laws and the Rules of the Corporation, have the meanings herein specified.

A. – L. *No change.*

M.

(1) – (7) *No change.*

¹ See Article XXI of OCC’s By-Laws and Chapter XXII of OCC’s Rules. It is also noted that no changes are being proposed to Article XXIA of OCC’s By-Laws or Chapter XXIIA of OCC’s Rules which address OCC’s Market Loan Program.

Matched-Book Borrowing Clearing Member

(8) The term “Matched-Book Borrowing Clearing Member” shall mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that borrows Eligible Stock from a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock.

Matched-Book Lending Clearing Member

(9) The term “Matched-Book Lending Clearing Member” shall mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that lends Eligible Stock to a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock.

Matched-Book Positions

(10) The term “Matched-Book Positions” shall mean Hedge Loan positions in which a single Hedge Clearing Member borrows Eligible Stock from a Matched-Book Lending Clearing Member and lends an equal or lesser amount of the same Eligible Stock to a Matched-Book Borrowing Clearing Member.

(8) – (13) *Renumbered as (11) – (16); otherwise no change*

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ARTICLE XXI – Stock Loan/Hedge Program

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Role of the Corporation

SECTION 2. (a) Commencing at the time at which the Corporation accepts a Stock Loan as described in Rule 2202, the role of the Corporation in respect of the Stock Loan shall be that of a principal, and the Corporation shall have the position of borrower to the Lending Clearing Member and lender to the Borrowing Clearing Member. Without limiting the generality of the foregoing: (i) the rights of the two Clearing Members that are parties to a Stock Loan to receive mark-to-market payments, and their obligations to make mark-to-market payments, shall be as against the Corporation, and not as against each other; and (ii) in the event of a termination of a Stock Loan in accordance with the Rules (with the exception of a termination by offset as provided in Rule 2208(e)), the right of the Lending Clearing Member to receive the Loaned Stock and the obligation of the Lending Clearing Member to pay the settlement price shall be as against the Corporation, and the obligation of the Borrowing Clearing Member to deliver the Loaned Stock and the right of the Borrowing Clearing Member to receive the settlement price shall be as against the Corporation. In addition to the foregoing:

(1) stock loan positions of a Clearing Member established as a result of Stock Loans relating to the same Eligible Stock in which the Clearing Member is the Lending Clearing Member shall be

aggregated for position reporting purposes, but shall not be netted against any stock borrow position which the Clearing Member may be carrying relating to the same Eligible Stock for any purpose other than (i) as described in Rule 601 with respect to determining the Clearing Member's margin obligations to the Corporation and (ii) as may be permitted pursuant to the Rules with respect to suspended Clearing Members or the voluntary termination by offset and re-matching of Matched-Book Positions in accordance with Rule 2208(e); and

(2) stock borrow positions of a Clearing Member established as the result of Stock Loans relating to the same Eligible Stock in which the Clearing Member is the Borrowing Clearing Member shall be aggregated for position reporting purposes, but shall not be netted against any stock loan position which the Clearing Member may be carrying relating to the same Eligible Stock for any purpose other than (i) as described in Rule 601 with respect to determining the Clearing Member's margin obligations to the Corporation and (ii) as may be permitted pursuant to the Rules with respect to suspended Clearing Members or the voluntary termination by offset and re-matching of Matched-Book Positions in Accordance with Rule 2208(e).

(b) Upon acceptance of a Stock Loan, the Corporation shall create a stock loan position in the account designated by the Lending Clearing Member, identifying the Eligible [Security]Stock that is the subject of the Stock Loan, the number of shares loaned, the amount of Collateral received from the Borrowing Clearing Member and the identity of the Borrowing Clearing Member, and shall create a stock borrow position in the account designated by the Borrowing Clearing Member, identifying the Eligible [Security]Stock that is the subject of the Stock Loan, the number of shares borrowed, the amount of Collateral delivered to the Lending Clearing Member and the identity of the Lending Clearing Member. The Corporation shall identify stock loan and stock borrow positions resulting from Hedge Loans separately from positions resulting from Market Loans.

(c) *No change*

Agreements of Borrowing Clearing Member

SECTION 3. The Clearing Member that is the Borrowing Clearing Member in respect of a Stock Loan agrees with the Corporation that: (a) upon the acceptance of the Stock Loan by the Corporation, the resulting stock borrow position of the Borrowing Clearing Member shall be created and subsequently maintained in accordance with Section 2 of this Article XXI, (b) so long as such stock borrow position is thereafter maintained, the Borrowing Clearing Member shall make all required margin deposits with the Corporation in accordance with Rule 2203 and all required mark-to-market payments to the Corporation in accordance with Rule 2204, and (c) with the exception of a termination by offset as provided in Rule 2208(e), in the event that the Lending Clearing Member, the Borrowing Clearing Member or the Corporation terminates the Stock Loan, the Borrowing Clearing Member shall deliver the Loaned Stock, against payment of the settlement price, in accordance with the By-Laws and the Rules.

Agreements of Lending Clearing Member

SECTION 4. The Clearing Member that is the Lending Clearing Member in respect of a Stock Loan agrees with the Corporation that: (a) upon the acceptance of the Stock Loan by the Corporation, the resulting stock loan position of the Lending Clearing Member shall be created and subsequently maintained in accordance with Section 2 of this Article XXI, (b) so long as such stock loan position is thereafter maintained, the Lending Clearing Member shall make all required margin deposits with the Corporation in accordance with Rule 2203 and all required mark-to-market payments to the Corporation in accordance with Rule 2204, and (c) with the exception of a termination by offset as provided in Rule 2208(e), in the event that the Borrowing Clearing Member, the Lending Clearing Member or the Corporation terminates the Stock Loan, the Lending Clearing Member shall pay the settlement price, against delivery of the Loaned Stock, in accordance with the By-Laws and the Rules.

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THE OPTIONS CLEARING CORPORATION

RULES

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CHAPTER XXII

Stock Loan/Hedge Program

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Rule 2201 - 2207 *No change.*

RULE 2208 - Settlement Date

(a) – (d) *No change*

(e)(1) Notwithstanding any other provision of the By-Laws or Rules, and subject to such requirements and limitations described in this Rule 2208, a Hedge Clearing Member may submit a written request to the Corporation to effect one or more position adjustments to terminate by offset all or some of its Matched-Book Positions if the following conditions are met:

(i) the requesting Hedge Clearing Member, its Matched-Book Lending Clearing Member, and its Matched-Book Borrowing Clearing Member have furnished to the Corporation their written agreement to (A) the termination by offset of such Matched-Book Positions maintained in the requesting Hedge Clearing Member's account and (B) the Corporation's re-matching the stock borrow position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Borrowing Clearing Member against the stock loan position for the same number of shares in the

same Eligible Stock maintained in a designated account of the Matched-Book Lending Clearing Member;

(ii) The written agreement furnished by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member must be in a form satisfactory to the Corporation in its sole discretion; and

(iii) The written request to terminate by offset and to re-match stock loan and borrow positions may be for less than the total number of shares of the Eligible Stock that is the subject of the stock loan and borrow positions maintained, as applicable, by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member, but must be for an equal number of shares.

(2) In the event the Corporation, in its sole discretion, approves the requested termination by offset and re-matching of positions, the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member are not required to issue instructions to the Depository in accordance with Rules 2202(a) and 2208(a) to terminate such stock loan and stock borrow positions maintained in the Stock Loan/Hedge Program or to initiate new stock loan transactions for inclusion in the Stock Loan/Hedge Program.

(3) From and after the time the Corporation has completed the requested position adjustments to terminate by offset and re-match the Matched-Book Positions maintained in the requesting Hedge Clearing Member's account as set forth in Rule 2209(h), the requesting Hedge Clearing Member shall have no further obligation under the By-Laws and Rules with respect to such positions.

(4) From and after the time the Corporation has completed the termination by offset and re-matching as set forth in Rule 2209(h), the Borrowing Clearing Member with re-matched stock borrow positions remains obligated as a Borrowing Clearing Member and the Lending Clearing Member with re-matched stock loan positions remains obligated as a Lending Clearing Member with respect to the re-matched positions as specified in the By-Laws and Rules applicable to the Stock Loan/Hedge Program.

(5) Upon notification that the Corporation has completed the termination by offset and re-matching of stock loan and borrow positions as set forth in Rule 2209(h), the requesting Hedge Clearing Member and the Borrowing Clearing Member and Lending Clearing Member with re-matched stock loan and borrow positions shall make any necessary bookkeeping entries at the Depository necessitated by the termination by offset and re-matching.

RULE 2209 - Settlement

(a) – (g) *No change.*

(h) In the event of a termination by offset and re-match of a stock loan under Rule 2208(e), such termination by offset and re-match shall be complete upon the Corporation completing all

position adjustments in the accounts of the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member in accordance with Rule 2208(e) and the earlier of (i) communicating confirmation of the transaction either in the form of direct written communications with the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member and the Matched-Book Lending Clearing Member or (ii) when systems reports are produced and provided to the Clearing Members reflecting the transaction.

(h) Renumbered as (i); otherwise no change

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Item 2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved for filing with the Commission by the Board of Directors of OCC at a meeting held on February 19, 2016.

Questions should be addressed to Justin Byrne, Vice President, Regulatory Filings, at 202-971-7238.

Item 3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

A. Purpose

OCC proposes amendments to its By-Laws and Rules designed to enhance the overall resilience of OCC's Stock Loan/Hedge Program by allowing OCC to close out the Matched-Book Positions of a Hedge Clearing Member requesting an orderly wind down of Matched-Book Positions through the termination by offset and re-matching of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC's rules. The proposed termination by offset and re-matching of stock loan and borrow positions is designed to leave the affected Clearing Members with the same net position in such stock loan and borrow positions as prior to the adjustment.

Background

In the Stock Loan/Hedge Program, OCC acts as a central counterparty (“CCP”) for Hedge Loans that are directly negotiated by Hedge Clearing Members and sent to OCC for clearance and settlement. A prospective Lending Clearing Member and a prospective Borrowing Clearing Member identify each other (independent of OCC) and agree on the terms of the stock loan. The Hedge Clearing Members then send the details of the stock loan to The Depository Trust Company (“Depository”) with a certain “reason code,”² which designates the stock loan as a Hedge Loan for guaranty and clearance at OCC. The Lending Clearing Member instructs the Depository to transfer a specified number of shares of Eligible Stock to the account of the Borrowing Clearing Member, and the Borrowing Clearing Member instructs the Depository to transfer the appropriate amount of cash collateral to the account of the Lending Clearing Member.³ The Depository then sends the Hedge Loan information to OCC via an end-of-day report.⁴ After OCC receives the report from the Depository, OCC validates and novates the stock loan transaction and becomes the lender to the Borrowing Clearing Member and the borrower to the Lending Clearing Member.⁵

After novation, as part of the guaranty, OCC makes Mark-to-Market Payments for all Hedge Loans on a daily basis to collateralize all loans to the negotiated levels.⁶ As the CCP,

² Unique reason codes were created by the Depository for Clearing Members to designate stock loan transactions intended to be sent to OCC for novation and guarantee.

³ See OCC Rule 2202(a).

⁴ See OCC Rule 2202(b).

⁵ *Id.*

⁶ Mark-to-Market Payments are based on the value of the loaned securities and made between Clearing Members using OCC’s cash settlement system. The percentage of the value of the loaned securities, either 100% or 102%, is dependent upon the agreement between the two Hedge Clearing Members party to the transaction.

OCC guarantees the return of the full value of cash collateral to a Borrowing Clearing Member and the Loaned Stock, or value of that Loaned Stock, to the Lending Clearing Member.

Settlements generally are combined and netted against other OCC settlement obligations in a Hedge Clearing Member's account, including trade premiums and margin deficits. A Hedge Clearing Member's open positions in the Stock Loan/Hedge Program are factored into the Hedge Clearing Member's overall Margin⁷ and Clearing Fund contribution requirements.⁸

A significant portion of the activity in OCC's stock lending programs relates to what is often referred to as matched-book activity where a Hedge Clearing Member maintains in an account a stock loan position for a specified number of shares of an Eligible Stock reflecting a stock lending transaction with one Hedge Clearing Member (the Borrowing Clearing Member) and also maintains in that same account a stock borrow position for the same number, or lesser number, of shares of the same Eligible Stock with another Hedge Clearing Member (the Lending Clearing Member) (such positions being "Matched-Book Positions"). From a daily mark-to-market settlement perspective, there are typically no obligations related to Matched-Book Positions because the member is simultaneously borrowing and lending the same securities (and quantity), which are marked to the same price. OCC's margin process recognizes this and currently nets loans and borrows in the same security prior to calculating exposure, resulting in no margin on a perfectly matched position.

Currently, in order for a Hedge Clearing Member to close out its stock loan positions, including Matched-Book Positions, the Hedge Clearing Member is required to terminate its loans through instructions issued to the Depository to transfer a specified quantity of the loaned stock

⁷ See OCC Rules 601 and 2203.

⁸ See OCC Rule 1001.

against payment of the settlement price in accordance with the process prescribed in Rule 2208. Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions that wish to maintain equivalent stock loan positions at OCC would then be required to initiate new stock loans, through the process described above, in accordance with Rule 2202. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and settle those transactions, which introduce the potential for market disruption. For example, because OCC maintains stock loan inventory on a bilateral basis (i.e., maintains the borrower and lender to a transaction) and guarantees the return of cash collateral and the Loaned Stock, or price of the Loaned Stock, if a Hedge Clearing Member with Matched-Book Positions fails to fulfill its obligations for the recall of loans and return of borrowed shares, there would be a temporary imbalance of the previously “matched-book” position. In addition, the successful initiation of new replacement stock loans for the Borrowing or Lending Clearing Members could be subject to disruption by operational or execution risks, with the result that one “leg” of the initiating transaction would fail. Moreover, the Borrowing and Lending Clearing Members lose the protections afforded by OCC’s guaranty of their stock loan positions until the newly initiated stock loan positions have been accepted, novated, and guaranteed by OCC.

The proposed rule change would permit a Hedge Clearing Member to request the orderly wind down of Matched-Book Positions, subject to the agreement of all affected Borrowing and Lending Clearing Members, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC Rules 2202, 2208 and 2209. OCC believes the proposed rule change would eliminate the potential risks described above associated with the transfer of securities and funds and provide the overall marketplace with more stability with

respect to the process of voluntarily closing out Matched-Book Positions in the Stock Loan/Hedge Program.

Voluntary Termination by Offset and Re-Matching

OCC proposes to amend its By-Laws and Rules to permit a Hedge Clearing Member to request an orderly wind down of its Matched-Book Positions, contingent upon the explicit agreement of the requesting Hedge Clearing Member, its counterparty Borrowing Clearing Member, and counterparty Lending Clearing Member, and at the sole discretion of OCC, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC's rules. First, OCC proposes to amend Article I of its By-Laws to add new defined terms "Matched-Book Borrowing Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that borrows Eligible Stock from a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock and "Matched-Book Lending Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that lends Eligible Stock to a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock. OCC also proposes to add a new definition for "Matched-Book Positions," which would be defined as Hedge Loan positions in which a single Hedge Clearing Member borrows Eligible Stock from its Matched-Book Lending Clearing Member and lends an equal or lesser amount of the same Eligible Stock to its Matched-Book Borrowing Clearing Member.

In addition, OCC proposes to amend Rule 2208 to adopt new rules for the voluntary termination by offset and re-matching of Matched-Book Positions. Specifically, OCC proposes to adopt new Rule 2208(e)(1), which would provide that a Hedge Clearing Member may submit a written request to OCC to effect one or more position adjustments to terminate by offset all or

some of its Matched-Book Positions if the following conditions are met. First, the requesting Hedge Clearing Member, its Matched-Book Lending Clearing Member, and its Matched-Book Borrowing Clearing Member have furnished to the Corporation their written agreement to (i) the termination by offset of such Matched-Book Positions maintained in the requesting Hedge Clearing Member's account and (ii) the Corporation's re-matching the stock borrow position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Borrowing Clearing Member against the stock loan position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Lending Clearing Member. Second, the written agreement furnished by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member must be in the form specified by OCC. Third, the written request to terminate by offset and to re-match stock loan and borrow positions may be for less than the total number of shares of the Eligible Stock that is the subject of the stock loan and borrow positions maintained, as applicable, by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member, but must be for an equal number of shares.

Additionally, proposed Rule 2208(e)(2) would provide that, if OCC in its sole discretion approves the requested termination by offset and re-matching of positions, the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member would not be required to issue instructions to the Depository to terminate such stock loans and stock borrow positions maintained in the Stock Loan/Hedge Program or to initiate new stock lending transactions for inclusion in the Stock Loan/Hedge Program as currently required under Rules 2202(a) and 2208(a).

Proposed Rules 2208(e)(3) and (4) would provide that, from and after the time OCC has completed the requested position adjustments to terminate by offset and re-match the specified stock loan and borrow positions, the requesting Hedge Clearing Member would have no further obligation under the By-Laws and Rules with respect to such positions; however, the Borrowing Clearing Member with re-matched stock borrow positions remains obligated as a Borrowing Clearing Member and the Lending Clearing Member with re-matched stock loan positions remains obligated as a Lending Clearing Member with respect to the re-matched positions as specified in the By-Laws and Rules applicable to the Stock Loan/Hedge Program.

Proposed Rule 2208(e)(5) would require the requesting Hedge Clearing Member and re-matched Borrowing Clearing Member and Lending Clearing Member to make any necessary bookkeeping entries at the Depository necessitated by the termination by offset and re-matching upon notification that the termination by offset and re-matching has been completed as set forth in proposed Rule 2209(h).

In addition, OCC proposes to adopt new Rule 2209(h) to specify that, in the event of a termination by offset and re-matching of a stock loan under proposed Rule 2208(e), such termination by offset and re-match shall be complete upon OCC completing all position adjustments in the accounts of the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member in accordance with Rule 2208(e) and the earlier of (i) communicating confirmation of the transaction in the form of direct written communications with the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member or (ii) when systems reports are produced and provided to the Clearing Members reflecting the transaction.

OCC also proposes conforming and clean-up changes to Article XXI, Sections 2, 3 and 4 of its By-Laws. Article XXI, Section 2 would be revised to (i) account for the netting of stock loan and stock borrow positions during the voluntary termination by offset and re-matching of Matched-Book Positions in accordance with proposed Rule 2208(e) and (ii) make clean-up changes to ensure the consistent use of the defined term “Eligible Stock.” Additionally, Article XXI, Sections 3 and 4 would be revised to state that the voluntary termination by offset of Matched-Book Positions in accordance with proposed Rule 2208(e) would be excluded from the requirement to pay the settlement price against delivery of the Loaned Stock as currently required for all terminations under OCC’s existing rules.

B. Statutory Basis

OCC believes the proposed rule change is consistent with Section 17A(b)(3)(F) of the Securities Exchange Act of 1934, as amended (the “Act”),⁹ and the rules thereunder applicable to OCC. The proposed rule change would allow OCC to close out the Matched-Book Positions of Hedge Clearing Members, which could include distressed Hedge Clearing Members or Hedge Clearing Members otherwise wishing to wind down their Matched-Book Positions in an orderly manner, through the termination by offset and re-matching of such positions. As described above, under OCC’s existing rules, the close out of Matched-Book Positions requires the transfer of securities against the payment of settlement prices. Moreover, to the extent Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions wish to continue to maintain equivalent stock loan positions at OCC, those members would be required to initiate new stock loans to replace the closed out positions. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and

⁹ 15 U.S.C. 78q-1(b)(3)(F).

settle those transactions, which introduce the potential for execution and operational risks and thereby pose risks to the prompt and accurate clearance and settlement of securities transactions and the safeguarding of securities and funds associated therewith. The proposed rule change would eliminate these risks by allowing OCC and its Hedge Clearing Members to close out Matched-Book Positions through a process of termination by offset and re-matching without requiring the transfer of securities and funds. Moreover, due to the nature of Matched-Book Positions, the proposed position adjustments would enable the requesting Hedge Clearing Member to orderly wind down its Matched-Book Positions while ensuring the Matched-Book Borrowing and Matched-Book Lending Clearing Members' positions are continuously protected by OCC's guaranty. OCC therefore believes the proposed rule change is designed to promote the prompt and accurate clearance of settlement of securities transactions, the safeguarding of securities and funds in the custody or control of OCC or for which it is responsible and, in general, to protect investors and the public interest in accordance with Section 17A(b)(3)(F) of the Act.¹⁰

Item 4. Self-Regulatory Organization's Statement on Burden on Competition

OCC does not believe that the proposed rule change would have any impact or impose any burden on competition.¹¹ The proposed rules would be equally applicable to all Hedge Clearing Members at OCC. The proposed rule change is designed to allow for the termination by offset and re-matching of Matched-Book Positions without requiring the transfer of securities and funds between Hedge Clearing Members and exposing OCC's members to the risks attendant to such

¹⁰ *Id.*

¹¹ 15 U.S.C. 78q-1(b)(3)(I).

transfers (as described in detail above). Accordingly, OCC does not believe that the proposed rule change would have any impact or impose any burden on competition.

Item 5. 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.

Item 6. Extension of Time Period for Commission Action

OCC does not consent to an extension of the time period specified in Section 19(b)(2) of the Act.¹²

Item 7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)

The proposed rule change has been filed for immediate effectiveness under Section 19(b)(3)(A)(iii) of the Act¹³ and Rule 19b-4(f)(4)(i) thereunder¹⁴ as it effects a change in an existing service of a registered clearing agency that (1) 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 (2) does not significantly affect the respective rights or obligations of the clearing agency or persons using the service. As described below, the proposed rule change would effect a change in OCC’s existing Stock Loan/Hedge Program clearing services without adversely affecting the safeguarding of securities or funds or significantly affecting the rights and obligations of OCC or persons using the service.

¹² 15 U.S.C. 78s(b)(2).

¹³ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁴ 17 CFR 240.19b-4(f)(4)(i).

The proposed rule change would not adversely affect the safeguarding of securities or funds in the custody or control of OCC or for which it is responsible. Currently, in order for a Hedge Clearing Member to close out its stock loan positions, including Matched-Book Positions, the Hedge Clearing Member is required to terminate its loans through instructions issued to the Depository to transfer a specified quantity of the loaned stock against payment of the settlement price in accordance with the process prescribed in Rule 2208. Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions that wish to maintain equivalent stock loan positions at OCC would then be required to initiate new stock loans in accordance with Rule 2202. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and settle those transactions, which introduce the potential for market disruption. For example, because OCC maintains stock loan inventory on a bilateral basis (i.e., maintains the borrower and lender to a transaction) and guarantees the return of cash collateral and the Loaned Stock, or price of the Loaned Stock, if a Hedge Clearing Member fails to fulfill its obligations for the recall of loans and return of borrowed shares, there would be a temporary imbalance of the previously “matched-book” position. In addition, the successful initiation of new replacement stock loans for the Borrowing or Lending Clearing Members could be subject to disruption by operational or execution risks, with the result that one “leg” of the initiating transaction would fail. Moreover, the Borrowing and Lending Clearing Members lose the protections afforded by OCC’s guaranty of their stock loan positions until the newly initiated stock loan positions have been accepted, novated, and guaranteed by OCC. The proposal would allow OCC to close out the Matched-Book Positions of Hedge Clearing Members requesting an orderly wind down of Matched-Book Positions, subject to the explicit agreement of all affected Hedge Clearing Members, through the termination by offset and re-

matching of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC Rules 2202, 2208 and 2209. The proposed rule change would eliminate the potential risks described above associated with the transfer of securities and funds and is thereby designed to assure the safeguarding of securities and funds in the custody or control of OCC or for which it is responsible.

Finally, the proposed rule change would not significantly affect the respective rights or obligations of OCC or persons using its Stock Loan/Hedge Program clearing services. The proposed rule change would offer a voluntary service for OCC's Hedge Clearing Members to close out Matched-Book Positions. This voluntary termination and re-matching would be subject to the explicit agreement of all affected Hedge Clearing Members and would also be subject to the discretion of OCC. If either OCC or any of the affected Hedge Clearing Members objected to the terms of such a position adjustment, the voluntary termination and re-matching would not occur and both OCC and its members would retain the same rights and obligations as under the existing rules, under which Hedge Clearing Members can terminate and initiate new stock loans pursuant to the ordinary course of business. Moreover, due to the nature of Matched-Book Positions, if all parties agree to the voluntary re-matching of Matched-Book Positions, the proposed position adjustments would leave the affected Clearing Members with the same net position in such stock loans as prior to the adjustment while ensuring the Matched-Book Borrowing and Lending Clearing Members' positions continue to maintain the protections of OCC's guaranty. For these reasons, OCC does not believe the proposed rule change would have a significant impact on the rights or obligations of OCC or its members.

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.¹⁵

Item 8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

Item 9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

Item 10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

Item 11. Exhibits

Exhibit 1A. Completed notice of the proposed rule change for publication in the Federal Register.

¹⁵ Notwithstanding its immediate effectiveness, implementation of this rule change will be delayed until this change is deemed certified under CFTC Regulation §40.6.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, The Options Clearing Corporation has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

THE OPTIONS CLEARING CORPORATION

By: 
Justin Byrne
Vice President, Regulatory Filings

EXHIBIT 1A

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-[_____]; File No. SR-OCC-2016-006)

March 15, 2016

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Related to the Voluntary Termination by Offset and Re-matching of Matched-Book Positions in the Stock Loan/Hedge Program

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 March 15, 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 primarily by OCC. OCC filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii)³ of the Act and Rule 19b-4(f)(4)(i)⁴ thereunder 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 purpose of this proposed rule change is to enhance the overall resilience of OCC’s Stock Loan/Hedge Program⁵ by allowing OCC to close out the Matched-Book Positions (as defined herein) of Hedge Clearing Members requesting an orderly wind down of Matched-Book

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)(i).

⁵ See Article XXI of OCC’s By-Laws and Chapter XXII of OCC’s Rules. It is also noted that no changes are being proposed to Article XXIA of OCC’s By-Laws or Chapter XXIIA of OCC’s Rules which address OCC’s Market Loan Program.

Positions through the termination by offset and “re-matching” of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC’s 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

OCC proposes amendments to its By-Laws and Rules designed to enhance the overall resilience of OCC’s Stock Loan/Hedge Program by allowing OCC to close out the Matched-Book Positions of a Hedge Clearing Member requesting an orderly wind down of Matched-Book Positions through the termination by offset and re-matching of such positions without requiring the transfer of securities against the payment of settlement prices as currently required under OCC’s rules. The proposed termination by offset and re-matching of stock loan and borrow positions is designed to leave the affected Clearing Members with the same net position in such stock loan and borrow positions as prior to the adjustment.

Background

In the Stock Loan/Hedge Program, OCC acts as a central counterparty (“CCP”) for Hedge Loans that are directly negotiated by Hedge Clearing Members and sent to OCC for

clearance and settlement. A prospective Lending Clearing Member and a prospective Borrowing Clearing Member identify each other (independent of OCC) and agree on the terms of the stock loan. The Hedge Clearing Members then send the details of the stock loan to The Depository Trust Company (“Depository”) with a certain “reason code,”⁶ which designates the stock loan as a Hedge Loan for guaranty and clearance at OCC. The Lending Clearing Member instructs the Depository to transfer a specified number of shares of Eligible Stock to the account of the Borrowing Clearing Member, and the Borrowing Clearing Member instructs the Depository to transfer the appropriate amount of cash collateral to the account of the Lending Clearing Member.⁷ The Depository then sends the Hedge Loan information to OCC via an end-of-day report.⁸ After OCC receives the report from the Depository, OCC validates and novates the stock loan transaction and becomes the lender to the Borrowing Clearing Member and the borrower to the Lending Clearing Member.⁹

After novation, as part of the guaranty, OCC makes Mark-to-Market Payments for all Hedge Loans on a daily basis to collateralize all loans to the negotiated levels.¹⁰ As the CCP, OCC guarantees the return of the full value of cash collateral to a Borrowing Clearing Member and the Loaned Stock, or value of that Loaned Stock, to the Lending Clearing Member. Settlements generally are combined and netted against other OCC settlement obligations in a

⁶ Unique reason codes were created by the Depository for Clearing Members to designate stock loan transactions intended to be sent to OCC for novation and guarantee.

⁷ See OCC Rule 2202(a).

⁸ See OCC Rule 2202(b).

⁹ *Id.*

¹⁰ Mark-to-Market Payments are based on the value of the loaned securities and made between Clearing Members using OCC’s cash settlement system. The percentage of the value of the loaned securities, either 100% or 102%, is dependent upon the agreement between the two Hedge Clearing Members party to the transaction.

Hedge Clearing Member's account, including trade premiums and margin deficits. A Hedge Clearing Member's open positions in the Stock Loan/Hedge Program are factored into the Hedge Clearing Member's overall Margin¹¹ and Clearing Fund contribution requirements.¹²

A significant portion of the activity in OCC's stock lending programs relates to what is often referred to as matched-book activity where a Hedge Clearing Member maintains in an account a stock loan position for a specified number of shares of an Eligible Stock reflecting a stock lending transaction with one Hedge Clearing Member (the Borrowing Clearing Member) and also maintains in that same account a stock borrow position for the same number, or lesser number, of shares of the same Eligible Stock with another Hedge Clearing Member (the Lending Clearing Member) (such positions being "Matched-Book Positions"). From a daily mark-to-market settlement perspective, there are typically no obligations related to Matched-Book Positions because the member is simultaneously borrowing and lending the same securities (and quantity), which are marked to the same price. OCC's margin process recognizes this and currently nets loans and borrows in the same security prior to calculating exposure, resulting in no margin on a perfectly matched position.

Currently, in order for a Hedge Clearing Member to close out its stock loan positions, including Matched-Book Positions, the Hedge Clearing Member is required to terminate its loans through instructions issued to the Depository to transfer a specified quantity of the loaned stock against payment of the settlement price in accordance with the process prescribed in Rule 2208. Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions that wish to maintain equivalent stock loan positions at OCC would then be required to initiate new

¹¹ See OCC Rules 601 and 2203.

¹² See OCC Rule 1001.

stock loans, through the process described above, in accordance with Rule 2202. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and settle those transactions, which introduce the potential for market disruption. For example, because OCC maintains stock loan inventory on a bilateral basis (i.e., maintains the borrower and lender to a transaction) and guarantees the return of cash collateral and the Loaned Stock, or price of the Loaned Stock, if a Hedge Clearing Member with Matched-Book Positions fails to fulfill its obligations for the recall of loans and return of borrowed shares, there would be a temporary imbalance of the previously “matched-book” position. In addition, the successful initiation of new replacement stock loans for the Borrowing or Lending Clearing Members could be subject to disruption by operational or execution risks, with the result that one “leg” of the initiating transaction would fail. Moreover, the Borrowing and Lending Clearing Members lose the protections afforded by OCC’s guaranty of their stock loan positions until the newly initiated stock loan positions have been accepted, novated, and guaranteed by OCC.

The proposed rule change would permit a Hedge Clearing Member to request the orderly wind down of Matched-Book Positions, subject to the agreement of all affected Borrowing and Lending Clearing Members, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC Rules 2202, 2208 and 2209. OCC believes the proposed rule change would eliminate the potential risks described above associated with the transfer of securities and funds and provide the overall marketplace with more stability with respect to the process of voluntarily closing out Matched-Book Positions in the Stock Loan/Hedge Program.

Voluntary Termination by Offset and Re-Matching

OCC proposes to amend its By-Laws and Rules to permit a Hedge Clearing Member to request an orderly wind down of its Matched-Book Positions, contingent upon the explicit agreement of the requesting Hedge Clearing Member, its counterparty Borrowing Clearing Member, and counterparty Lending Clearing Member, and at the sole discretion of OCC, without requiring the transfer of securities against the payment of settlement prices as currently required under OCC's rules. First, OCC proposes to amend Article I of its By-Laws to add new defined terms "Matched-Book Borrowing Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that borrows Eligible Stock from a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock and "Matched-Book Lending Clearing Member," which would mean, with respect to any Matched-Book Positions, the Hedge Clearing Member that lends Eligible Stock to a Hedge Clearing Member maintaining Matched-Book Positions in that Eligible Stock. OCC also proposes to add a new definition for "Matched-Book Positions," which would be defined as Hedge Loan positions in which a single Hedge Clearing Member borrows Eligible Stock from its Matched-Book Lending Clearing Member and lends an equal or lesser amount of the same Eligible Stock to its Matched-Book Borrowing Clearing Member.

In addition, OCC proposes to amend Rule 2208 to adopt new rules for the voluntary termination by offset and re-matching of Matched-Book Positions. Specifically, OCC proposes to adopt new Rule 2208(e)(1), which would provide that a Hedge Clearing Member may submit a written request to OCC to effect one or more position adjustments to terminate by offset all or some of its Matched-Book Positions if the following conditions are met. First, the requesting Hedge Clearing Member, its Matched-Book Lending Clearing Member, and its Matched-Book Borrowing Clearing Member have furnished to the Corporation their written agreement to (i) the

termination by offset of such Matched-Book Positions maintained in the requesting Hedge Clearing Member's account and (ii) the Corporation's re-matching the stock borrow position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Borrowing Clearing Member against the stock loan position for the same number of shares in the same Eligible Stock maintained in a designated account of the Matched-Book Lending Clearing Member. Second, the written agreement furnished by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member must be in the form specified by OCC. Third, the written request to terminate by offset and to re-match stock loan and borrow positions may be for less than the total number of shares of the Eligible Stock that is the subject of the stock loan and borrow positions maintained, as applicable, by the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member, but must be for an equal number of shares.

Additionally, proposed Rule 2208(e)(2) would provide that, if OCC in its sole discretion approves the requested termination by offset and re-matching of positions, the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and Matched-Book Lending Clearing Member would not be required to issue instructions to the Depository to terminate such stock loans and stock borrow positions maintained in the Stock Loan/Hedge Program or to initiate new stock lending transactions for inclusion in the Stock Loan/Hedge Program as currently required under Rules 2202(a) and 2208(a).

Proposed Rules 2208(e)(3) and (4) would provide that, from and after the time OCC has completed the requested position adjustments to terminate by offset and re-match the specified stock loan and borrow positions, the requesting Hedge Clearing Member would have no further

obligation under the By-Laws and Rules with respect to such positions; however, the Borrowing Clearing Member with re-matched stock borrow positions remains obligated as a Borrowing Clearing Member and the Lending Clearing Member with re-matched stock loan positions remains obligated as a Lending Clearing Member with respect to the re-matched positions as specified in the By-Laws and Rules applicable to the Stock Loan/Hedge Program.

Proposed Rule 2208(e)(5) would require the requesting Hedge Clearing Member and re-matched Borrowing Clearing Member and Lending Clearing Member to make any necessary bookkeeping entries at the Depository necessitated by the termination by offset and re-matching upon notification that the termination by offset and re-matching has been completed as set forth in proposed Rule 2209(h).

In addition, OCC proposes to adopt new Rule 2209(h) to specify that, in the event of a termination by offset and re-matching of a stock loan under proposed Rule 2208(e), such termination by offset and re-match shall be complete upon OCC completing all position adjustments in the accounts of the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member in accordance with Rule 2208(e) and the earlier of (i) communicating confirmation of the transaction in the form of direct written communications with the requesting Hedge Clearing Member, the Matched-Book Borrowing Clearing Member, and the Matched-Book Lending Clearing Member or (ii) when systems reports are produced and provided to the Clearing Members reflecting the transaction.

OCC also proposes conforming and clean-up changes to Article XXI, Sections 2, 3 and 4 of its By-Laws. Article XXI, Section 2 would be revised to (i) account for the netting of stock loan and stock borrow positions during the voluntary termination by offset and re-matching of

Matched-Book Positions in accordance with proposed Rule 2208(e) and (ii) make clean-up changes to ensure the consistent use of the defined term “Eligible Stock.” Additionally, Article XXI, Sections 3 and 4 would be revised to state that the voluntary termination by offset of Matched-Book Positions in accordance with proposed Rule 2208(e) would be excluded from the requirement to pay the settlement price against delivery of the Loaned Stock as currently required for all terminations under OCC’s existing rules.

(2) Statutory Basis

OCC believes the proposed rule change is consistent with Section 17A(b)(3)(F) of the Securities Exchange Act of 1934, as amended (the “Act”),¹³ and the rules thereunder applicable to OCC. The proposed rule change would allow OCC to close out the Matched-Book Positions of Hedge Clearing Members, which could include distressed Hedge Clearing Members or Hedge Clearing Members otherwise wishing to wind down their Matched-Book Positions in an orderly manner, through the termination by offset and re-matching of such positions. As described above, under OCC’s existing rules, the close out of Matched-Book Positions requires the transfer of securities against the payment of settlement prices. Moreover, to the extent Borrowing and Lending Clearing Member counterparties to the Matched-Book Positions wish to continue to maintain equivalent stock loan positions at OCC, those members would be required to initiate new stock loans to replace the closed out positions. Throughout this process of terminating and reestablishing stock loan positions, a number of operational steps are required to effectuate and settle those transactions, which introduce the potential for execution and operational risks and thereby pose risks to the prompt and accurate clearance and settlement of securities transactions and the safeguarding of securities and funds associated therewith. The proposed rule change

¹³ 15 U.S.C. 78q-1(b)(3)(F).

would eliminate these risks by allowing OCC and its Hedge Clearing Members to close out Matched-Book Positions through a process of termination by offset and re-matching without requiring the transfer of securities and funds. Moreover, due to the nature of Matched-Book Positions, the proposed position adjustments would enable the requesting Hedge Clearing Member to orderly wind down its Matched-Book Positions while ensuring the Matched-Book Borrowing and Matched-Book Lending Clearing Members' positions are continuously protected by OCC's guaranty. OCC therefore believes the proposed rule change is designed to promote the prompt and accurate clearance of settlement of securities transactions, the safeguarding of securities and funds in the custody or control of OCC or for which it is responsible and, in general, to protect investors and the public interest in accordance with Section 17A(b)(3)(F) of the Act.¹⁴

(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 competition.¹⁵ The proposed rules would be equally applicable to all Hedge Clearing Members at OCC. The proposed rule change is designed to allow for the termination by offset and re-matching of Matched-Book Positions without requiring the transfer of securities and funds between Hedge Clearing Members and exposing OCC's members to the risks attendant to such transfers (as described in detail above). Accordingly, OCC does not believe that the proposed rule change would have any impact or impose any burden on competition.

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

¹⁴ *Id.*

¹⁵ 15 U.S.C. 78q-1(b)(3)(I).

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 filing¹⁶ pursuant to Section 19(b)(3)(A)(iii) of the Act¹⁷ and Rule 19b-4(f)(4)(i) thereunder¹⁸ as it effects a change in an existing service of a registered clearing agency that (1) 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 (2) 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

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 Number SR-OCC-2016-006 on the subject line.

¹⁶ Notwithstanding its immediate effectiveness, implementation of this rule change will be delayed until this change is deemed certified under CFTC Regulation §40.6.

¹⁷ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁸ 17 CFR 240.19b-4(f)(4)(i).

Paper Comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-OCC-2016-006. 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 filing 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_006.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-2016-006 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.¹⁹

Robert W. Errett
Deputy Secretary

Action as set forth recommended herein
APPROVED pursuant to authority delegated by
the Commission under Public Law 87-592.
For: Division of Trading and Markets

By: _____

Print Name: _____

Date: _____

¹⁹ 17 CFR 200.30-3(a)(12).