



March 28, 2017

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-2017-003 Rule Certification

Dear Secretary Kirkpatrick:

Pursuant to Section 5c(c)(1) of the Commodity Exchange Act, as amended (“Act”), and Commodity Futures Trading Commission (“CFTC”) Regulation 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 (“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

On September 28, 2016 the SEC adopted amendments to Rule 17Ad-22¹ and added new Rule 17Ad-22(e)(13)² pursuant to Section 17A of the Securities Exchange Act of 1934³ and the Payment, Clearing, and Settlement Supervision Act of 2010 (“Payment, Clearing and Settlement Supervision Act”)⁴ to require that a “covered clearing agency,” as defined by Rule 17Ad-22(a)(5),⁵ has the authority and operational capacity, among other things, to require that participants, and other stakeholders when practicable, participate in the review and testing of the

¹ 17 CFR 240.17Ad-22.

² 17 CFR 240.17Ad-22(e)(13).

³ 15 U.S.C. 78q-1.

⁴ 12 U.S.C. 5461 *et. seq.*

⁵ 17 CFR 240.17Ad-22(a)(5).

covered clearing agency's default procedures (collectively, the new and amended rules are herein referred to as "CCA" rules). Specifically, Rule 17Ad-22(e)(13) requires that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to:

Ensure the covered clearing agency has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations by, at a minimum, requiring the covered clearing agency's participants and, when practicable, other stakeholders to participate in the testing and review of its default procedures, including any close-out procedure, at least annually and following material changes thereto.⁶

OCC meets the definition of a covered clearing agency and is therefore subject to the requirements of the CCA rules, including Rule 17Ad-22(e)(13).⁷

Current Practice

As a matter of current practice, OCC already involves certain of its Clearing Members in testing of OCC's default management procedures. Article V of OCC's By-Laws sets forth OCC's initial membership requirements. Pursuant to Interpretation and Policy .02(b) of Article V, Section 1 of OCC's By-Laws, an applicant must demonstrate that it is operationally capable of, among other things, participating in applicable default management activities as required by OCC and in accordance with applicable laws and regulations.⁸

Once an applicant becomes a Clearing Member, Chapter II of OCC's Rules also sets forth operational requirements that address default management procedure testing. In particular, OCC Rule 214(d) requires Clearing Members to maintain certain operational capabilities as a continuing obligation of participating in OCC as a Clearing Member. This includes "the ability to participate in default management activities, including auctions, as may be required by the Corporation and in accordance with applicable laws and regulations."⁹

As contemplated by Interpretation and Policy .02(b) of Article V, Section 1 and Rule 214(d), OCC already conducts periodic default management testing, which includes the participation of certain Clearing Members.

⁶ 17 CFR 240.17Ad-22(e)(13).

⁷ Id.

⁸ See OCC By-Laws Article V, Section 1, Interpretation and Policy .02(b).

⁹ See OCC Rule 214(d).

Proposed Rules 218(c) and (d)

To comply with certain requirements in Rule 17Ad-22(e)(13) that the SEC recently adopted as part of the CCA rules, OCC is proposing to implement Rules 218(c) and (d) to establish a requirement that Clearing Members participate periodically in testing of OCC's default procedures, including any close-out procedures. Proposed Rules 218(c) and (d) would make clear, consistent with the CCA rules, OCC's right to designate Clearing Members that are required to participate in default procedure testing and require designated Clearing Members to comply with the default procedure testing within specified timeframes.

OCC maintains a Default Management Policy ("Policy") that also addresses its default procedure testing requirements. Specifically, the Policy notes, among other things, that OCC's default management testing will occur on at least an annual basis, or more frequently if a material change is made to OCC's default management procedures or as may be deemed necessary by OCC's internal "Default Management Working Group."¹⁰ In addition, the Policy provides that certain Clearing Members would be required to participate in OCC's default management testing, consistent with proposed Rules 218(c) and (d).

Proposed Rules 218(c) and (d) would establish flexible and transparent key factors that OCC would use to determine which Clearing Members are required to participate in default management testing. Proposed Rules 218(c) and (d) would require OCC to use the key factors to select Clearing Members that, taken as a whole, OCC determines are the minimum necessary for the maintenance of fair and orderly markets, the promotion of robust risk management, the support of stability of the broader financial system and the protection investors and the public interest. OCC's key factors in determining which Clearing Members will be selected for testing in any given testing event would include but not be limited to: (i) suitability of business activities and anticipated impact on resources;¹¹ (ii) historical open interest and volume in asset classes, where appropriate;¹² and (iii) participation in previous tests. In adopting the CCA rules, the SEC

¹⁰ The "Default Management Working Group" is a staff-level working group chaired by the Vice President of Default Management and composed of staff from other OCC departments involved in default management testing.

¹¹ OCC's Clearing Members vary in their size, capacity, and participation in OCC's services from large, active members to smaller members that may not participate in certain services or may have less resources, personnel, or capacity to engage in default procedure testing at a given time. Consequently, OCC needs to preserve reasonable flexibility in considering the suitability of business activities and anticipated impact on resources of a Clearing Member considered for participation in a particular default management testing exercise. OCC notes, however, that this in no way abrogates a Clearing Member's obligations to maintain the minimal operational capabilities, including the ability to participate in default management activities, as required by OCC's rules. See, e.g., OCC Rule 214(d).

¹² See, e.g., OCC Rule 1104.02(d), noting that in a default scenario OCC will pre-qualify certain potential bidders in an auction based on, among other things, demonstrated activity in the

provided guidance that clarifies that “[a] covered clearing agency may designate in its policies and procedures that certain participants, or certain categories of participants, be designated for participation in certain tests.”¹³ OCC’s key factors to determine which Clearing Members are selected for participation in a given test of a default procedure are designed to provide flexibility to OCC while also ensuring that the appropriate Clearing Members participate in tests relevant to their business activities as relevant to OCC. Any Clearing Members designated to participate in a test of OCC’s default procedures would be notified in advance and provided details concerning the nature of such testing as the particular test plans are determined.

As stated above, OCC already conducts periodic default management testing and includes certain Clearing Members in such testing under Rule 214(d). Accordingly, OCC believes the proposed rule would have comparatively little impact on its Clearing Members relative to OCC’s existing practice. As previously noted, the proposed rule is intended to establish clear authority in accordance with Rule 17Ad-22(e)(13)¹⁴ for OCC to require Clearing Member participation in default procedure testing.

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:

Participant and Product Eligibility. OCC believes that implementing the proposed rule change will be consistent with the requirement in Core Principle C that participation and membership requirements of each DCO be objective, publicly disclosed and permit fair and open access.¹⁵ Proposed Rules 218(c) and (d) would publicly disclose the requirement for Clearing Member participation in default management testing, as well as the key factors used by OCC in the selection of participants for particular default management testing exercises.

Default Rules and Procedures. OCC believes that implementing the proposed rule change will be aligned with the requirement in Core Principle G that a DCO ensure it may take timely action to contain losses and liquidity pressures and continue to meet each of its obligations as a DCO.¹⁶ Proposed Rules 218(c) and (d) would make clear that Clearing Members are required to participate, if selected, in default management testing. OCC’s default management tests are designed to ensure that OCC would be able to take timely action to contain losses and liquidity pressures related to or arising from a default. Adopting a rule to ensure

products being auctioned and qualification to clear transactions in the asset class in which the Clearing Member proposes to submit bids before inviting a bidder to participate in the auction.

¹³ Securities Exchange Act Release No. 78961 (September 28, 2016), 81 FR 70786, 70830 (October 13, 2016).

¹⁴ 17 CFR 240.17Ad-22(e)(13).

¹⁵ 7 U.S.C. 7a-1(c)(2)(C)(iii).

¹⁶ 7 U.S.C. 7a-1(c)(2)(G)(ii).

participation in default management testing inures to the benefit of OCC's obligations under Core Principle G.

Public Information. OCC believes that implementing the proposed rule change will be aligned with the requirement in Core Principle L that a DCO make information concerning the rules and the operating and default procedures governing the clearing and settlement systems of the DCO available to market participants.¹⁷ Proposed Rules 218(c) and (d) would be published in OCC's publicly available rules.

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 be 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.

¹⁷ 7 U.S.C. 7a-1(c)(2)(L)(ii).

Christopher J. Kirkpatrick
March 28, 2017
Page 6

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,

A handwritten signature in blue ink, appearing to read "Justin W. Byrne".

Justin W. Byrne
Vice President, Regulatory Filings

Enclosure