THE FOUNDATION
FOR SECURE
MARKETS

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August 1, 2018

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-2017-020 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, as subsequently amended,[1] has been submitted to the SEC under the Exchange Act.

OCC has requested confidential treatment for Exhibit 5C to SR-OCC-2017-020 (the Default Management Policy) and the amendments thereto.

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[1] On December 18, 2017, OCC filed a proposed rule change with the SEC that would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. See Securities Exchange Act Release No. 82351 (December 19, 2017), 82 FR 61107 (December 26, 2017) (SR-OCC-2017-020) (hereinafter referred to as the "Initial Filing"). On March 22, 2018, the SEC instituted proceedings to determine whether to approve or disapprove the proposed rule change. See Securities Exchange Act Release No. 82926 (March 22, 2018), 83 FR 13171 (March 27, 2018) (SR-OCC-2017-020). On July 11, 2018, OCC filed Amendment No. 1 to SR-OCC-2018-020, which was intended to supersede the Initial Filing in its entirety. On July 12, 2018, OCC filed Amendment No. 2 to correct certain inadvertent omissions from the Form 19b-4 and Exhibit 1A of Amendment No. 1. This filing discusses the proposed rule change as amended by Amendment No. 2 and includes explanatory footnotes to highlight each amendment to the Initial Filing.

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

Explanation and Analysis

The purpose of this proposed rule change is to make certain revisions to OCC's Rules and By-Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. Each of the proposed revisions also is designed to further OCC's compliance, in whole or in part, with the [CFTC's derivatives clearing organization ("DCO") core principles ("Core Principles") and] provisions of the SEC's rules identified immediately below.

The proposed revisions to OCC's By-Laws and Rules are attached hereto as Exhibits 5A and 5B, and the proposed changes to OCC's Default Management Policy are included as confidential Exhibit 5C. Material proposed to be added to OCC's By-Laws, Rules, and Default Management Policy is marked by underlining and material proposed to be deleted is marked by strikethrough text.[2]

On September 28, 2016, the SEC adopted amendments to Rule 17Ad-22[3] and added new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii)[4] pursuant to Section 17A of the Exchange Act[5] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Payment, Clearing and Settlement Supervision Act").[6] In relevant part, these new rules collectively require a covered clearing agency ("CCA"), as defined by Rule 17Ad-22(a)(5),[7] to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (1) maintain a risk management framework including plans for recovery and orderly wind-down necessitated by credit losses, liquidity shortfalls, general business risk losses or any other losses, (2) effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing and settlement processes, including by addressing the allocation of credit losses a CCA might face if its collateral and other resources are insufficient to fully cover its credit exposures, (3) effectively identify, measure, monitor and manage credit exposures, including by describing the process to replenish any financial resource that a CCA may use

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2 The attached filing also includes as Exhibits 4A and 4B the proposed amendments to the rule text in Exhibits 5A and 5B of the Initial Filing, respectively. Material proposed to be added to the proposed rule text in the Initial Filing is marked by double underlining and material proposed to be deleted is marked by double strikethrough text.

3 17 CFR 240.17Ad-22.

4 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

5 15 U.S.C. 78q-1.

6 12 U.S.C. 5461 et. seq.

7 17 CFR 240.17Ad-22(a)(5).

following a default event or other event in which use of such resource is contemplated, (4) effectively identify, measure, monitor and manage liquidity risks that arises or is borne by the CCA by, at a minimum, describing the process for replenishing any liquid resource that a CCA may employ during a stress event, (5) ensure it has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations, (6) publicly disclose relevant rules and material procedures, including key aspects of its default rules and procedures, and (7) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the CCA. The relevant portions of each of these new requirements is restated below:

- Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[m]aintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the [CCA], which…[i]ncludes plans for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[8]

- Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…[a]ddressing allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures, including the repayment of any funds the [CCA] may borrow from liquidity providers."[9]

- Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by …[d]escribing the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[10]

- Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively measure, monitor, and manage the liquidity risk that arises in or is borne by the [CCA], including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, doing the following...[d]escribing the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[11]

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8 17 CFR 240.17Ad-22(e)(3)(ii).

9 17 CFR 240.17Ad-22(e)(v)(viii).

10 17 CFR 240.17Ad-22(e)(4)(ix).

11 17 CFR 240.17Ad-22(e)(7)(ix).

- Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure 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…"[12]

- Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[13]

- Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[14]

OCC meets the definition of a CCA and is therefore subject to the requirements of the CCA rules, including new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).[15]

Proposed Changes

Summary of Proposed Changes

In order to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default, OCC is proposing to make the following revisions to its Rules and By-Laws:

(1) Revise the existing assessment powers in Section 6 of Article VIII of OCC's By-Laws, specifically to:

(a) Establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge;

(b) Clarify that a Clearing Member that chooses to terminate its membership status during a cooling-off period will not be liable for replenishment of the Clearing Fund immediately following the expiration of such cooling-off period, provided that the withdrawing Clearing Member satisfies enumerated criteria, including providing notice of

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12 17 CFR 240.17Ad-22(e)(13).

13 17 CFR 240.17Ad-22(e)(23)(i).

14 17 CFR 240.17Ad-22(e)(23)(ii).

15 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

such termination by no later than the end of the cooling-off period and by closing-out and/or transferring of all its open positions with OCC by no later than the last day of the cooling-off period; and

(c) Delineate between the obligation of a Clearing Member to replenish its contributions to the Clearing Fund and its obligations to meet additional "assessments" that may be levied following a proportionate charge to the Clearing Fund.

(2) Adopt a new Rule 1011[16] that would provide OCC with discretionary authority to call for voluntary payments from non-defaulting Clearing Members in a circumstance where one or more Clearing Members has already defaulted and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[17] Rule 1011 also would establish that OCC would prioritize compensation of Clearing Members that made voluntary payments from any amounts recovered from the defaulted Clearing Members.

(3) Adopt a new Rule 1111 that would provide authority to:

(a) Allow OCC to call for voluntary tear-ups ("Voluntary Tear-Up," as defined below) of non-defaulting Clearing Member and/or customer positions at any time following the suspension or default of a Clearing Member, with the scope of any such Voluntary Tear-Ups being determined by the Risk Committee of OCC's Board ("Risk Committee");

(b) Allow OCC's Board to vote to tear-up the "Remaining Open Positions" (defined below) of a defaulted Clearing Member, as well as any "Related Open Positions" (defined below) in a circumstance where OCC has attempted one or more auctions of such defaulted Clearing Member's remaining open positions and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default with the scope of any such tear-up ("Partial Tear-Up") being determined by the Risk Committee; and

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16 OCC amended the Initial Filing to renumber proposed Rule 1009 to proposed Rule 1011 and updated related cross references in Rule 1111 to reflect this renumbering. OCC also amended the Default Management Policy as submitted in the Initial Filing to update similar cross references.

17 Under the Initial Filing, OCC's authority to conduct Partial Tear-Ups, as well as call for voluntary payments or to conduct Voluntary Tear-Ups, would be conditioned in part on OCC having determined that, notwithstanding the availability of any remaining resources, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under the Initial Filing, the proposed text of Rules 1009(a), 1111(a) and 1111(b) incorrectly transcribed this condition to require that OCC determine that, notwithstanding the availability of any remaining resources, OCC *does* not have sufficient resources to satisfy its obligations and liabilities resulting from such default (emphasis added). In each such instance, OCC amended the proposed text of Rules 1009(a) (which is being renumbered as Rule 1011(a)), 1111(a) and 1111(b) in Exhibit 5B of the Initial Filing to delete the word "does" and insert in its place the word "may."

(c) Allow OCC's Board to vote to re-allocate losses, costs and fees imposed upon holders of positions extinguished in a Partial Tear-Up through a special charge levied against remaining non-defaulting Clearing Members.

(4) Revise the descriptions and authorizations in Article VIII of OCC's By-Laws concerning the use of the Clearing Fund to reflect the discretion of OCC to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from a Voluntary Tear-Up or a mandatory tear-up ("Partial Tear-Up," as defined below).

Discussion of Proposed Changes

Each of the proposed revisions to OCC's Rules and By-Laws is described in more detail in the following sub-sections:

1. Proposed Changes to OCC's Assessment Powers

a. Current Assessment Powers

OCC's current assessment powers are described in Section 6 of Article VIII of OCC's By-Laws. Section 6 establishes a general requirement for each Clearing Member to promptly make good any deficiency in its required contribution to the Clearing Fund whenever an amount is paid out of its Clearing Fund contribution (whether by proportionate charge or otherwise).[18] In this regard, a Clearing Member's obligation to replenish the Clearing Fund is not currently subject to any pre-determined limit. Notwithstanding the foregoing, a Clearing Member can limit the amount of its liability for replenishing the Clearing Fund (at an additional 100% of the amount of its then-required Clearing Fund contribution) by winding-down its clearing activities and terminating its status as a Clearing Member. Any Clearing Member seeking to so limit its liability for replenishing the Clearing Fund must: (i) notify OCC in writing not later than the fifth business day after the proportionate charge that it is terminating its status as a Clearing Member, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan

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[18] Under Article VIII, Section 6 of OCC's By-Laws, OCC currently has authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund in certain enumerated situations. For example, Section 6 generally provides that if the conditions regarding a Clearing Member default specified in subparagraphs (a)(i) through (vi) of Article VIII, Section 5 of OCC's By-Laws are satisfied, OCC will make good resulting losses or expenses that are suffered by OCC by applying the defaulting Clearing Member's Clearing Fund contribution after first applying other funds available to OCC in the accounts of the Clearing Member. If the sum of the obligations, however, exceeds the total Clearing Fund contribution and other funds of the defaulting Clearing Member available to OCC, then OCC will charge the amount of the remaining deficiency on a proportionate basis against all non-defaulting Clearing Members' required contributions to the Clearing Fund at the time. Section 5(b) of Article VIII of OCC's By-Laws similarly provides for proportionate charges against Clearing Members' contributions to the Clearing Fund when certain conditions are met that involve a failure by a bank or a securities or commodities clearing organization to perform obligations to OCC when they are due.

Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close out or transfer all of its open positions as promptly as practicable after giving notice to OCC. Thus, withdrawal from clearing membership is the only means by which a Clearing Member currently can limit its liability for replenishing the Clearing Fund.

b. Proposed Changes to Assessment Powers

OCC proposes to revise Section 6 of Article VIII of OCC's By-Laws to make three primary modifications regarding its existing authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund. First, the proposal introduces an automatic minimum fifteen calendar day "cooling-off" period that begins when a proportionate charge is assessed by OCC against Clearing Members' Clearing Fund contributions. While the cooling-off period will continue for a minimum of fifteen consecutive calendar days, if one or more of the events described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws occur(s) during that fifteen calendar day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through either (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth day from the date of the proportionate charge that initiated the cooling-off period, whichever is sooner.

During a cooling-off period, each Clearing Member would have its aggregate liability to replenish the Clearing Fund capped at 200% of the Clearing Member's then-required contribution to the Clearing Fund. Once the cooling-off period ends each remaining Clearing Member would be required to replenish the Clearing Fund in the amount necessary to meet its then-required contribution. Once the cooling-off period ends, any remaining losses or expenses suffered by OCC as a result of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that occurred during such cooling-off period could not be charged against the amounts Clearing Members have contributed to replenish the Clearing Fund upon the expiration of the cooling-off period.[19]

Second, in connection with the cooling-off period, the proposal would extend the time frame within which a Clearing Member may provide a termination notice to OCC to avoid liability for replenishment of the Clearing Fund after the cooling-off period and would modify the obligations of such a terminating Clearing Member for closing-out and transferring its remaining open positions. Specifically, to effectively terminate its status as a Clearing Member and not be liable for replenishing the Clearing Fund after the cooling-off period, a Clearing Member would be required to: (i) notify OCC in writing of its intent to terminate not later than the last day of the cooling-off period, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock

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19 After a cooling-off period has ended, the occurrence of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that results in a proportionate charge against the Clearing Fund would trigger a new cooling off period, and thusly, a cap of 200% of each Clearing Member's then-required contribution would again apply.

Loan transaction, through any of its accounts, and (iii) close-out or transfer all of its open positions by no later than the last day of the cooling-off period. If a Clearing Member fails to satisfy all of these conditions by the end of a given cooling-off period, it would not have completed all of the requirements necessary to terminate its status as a Clearing Member under Article VIII, Section 6 of OCC's By-Laws and therefore it would remain subject to the obligation to replenish the Clearing Fund after the end of the cooling-off period.

Third, the proposal would clarify the distinction between "replenishment" of the Clearing Fund and a Clearing Member's obligation to answer "assessments." In this context, the term "replenish" (and its variations) shall to refer to a Clearing Member's standing duty, following any proportionate charge against the Clearing Fund, to return its Clearing Fund contribution to the amount required from such Clearing Member for the month in question.[20] The term "assessment" (and its variations) shall refer to the amount, during any cooling-off period, that a Clearing Member would be required to contribute to the Clearing Fund in excess of the amount of the Clearing Member's pre-funded required Clearing Fund contribution.

Proposed Addition of Ability to Request Voluntary Payments

OCC proposes to add new Rule 1011, which will provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[21] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under new Rule 1011, OCC will initiate a call for voluntary payments by issuing a "Voluntary Payment Notice" inviting all non-defaulting Clearing Members to make payments to the Clearing Fund in addition to any amounts they are otherwise required to contribute pursuant to Rule 1001. The Voluntary Payment Notice would specify the terms applicable to any voluntary payment, including but not limited to, that any voluntary payment may not be withdrawn once made, that no Clearing Member shall be obligated to make a voluntary payment and that OCC shall retain full discretion to accept or reject any voluntary payment. Rule 1011 specifies that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s), OCC would seek to compensate first from such recovery all non-defaulting Clearing Members that made voluntary payments (and if the amount recovered from the defaulted Clearing Member(s) is less than the aggregate amount of voluntary payments, non-defaulting Clearing Members that made voluntary payments each would

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20 This assumes that the proportionate charge resulted in the Clearing Member's actual Clearing Fund contribution dropping below the amount of its required contribution (*i.e.*, that the Clearing Member did not have excess above its required contribution that was sufficient to cover the amount of the proportionate charge allocated to such Clearing Member).

21 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

receive a percentage of the recovery that corresponds to that Clearing Member's percentage of the total amount of voluntary payments received).

Proposed Addition of Ability to Conduct Voluntary Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to voluntarily extinguish (i.e., voluntarily tear-up) their open positions at OCC in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.

While Risk Committee approval is not needed to commence a voluntary tear-up, the Risk Committee would be responsible for determining the appropriate scope of each voluntary tear-up. To ensure OCC retains sufficient flexibility to effectively deploy this tool in an extreme stress event, proposed Rule 1111(c) is drafted to provide the Risk Committee with discretion to determine the appropriate scope of each voluntary tear-up.[22] New Rule 1111(c) also would impose standards designed to circumscribe the Risk Committee's discretion, requiring that any determination regarding the scope of a voluntary tear-up shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

Once the Risk Committee has determined the scope of the Voluntary Tear-Up, OCC will initiate the call for voluntary tear-ups by issuing a "Voluntary Tear-Up Notice." The Voluntary Tear-Up Notice shall inform all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear-Up.[23] The Voluntary Tear-Up Notice would specify the terms applicable to any voluntary tear-up, including but not limited to, that no Clearing Member or customers of a Clearing Member shall be obligated to participate in a voluntary tear-up and that OCC shall retain full discretion to accept or reject any voluntary tear-up.

OCC is not proposing a tear-up process that would require the imposition of "gains haircutting" (*i.e.*, the reduction of unpaid gains) on a portion of OCC's cleared contracts.[24] Instead,

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22 Notwithstanding the discretion that would be afforded by the text of proposed Rule 1111(c), OCC anticipates that the scope of voluntary tear-ups likely would be dictated by the cleared contracts remaining in the portfolio(s) of the defaulted Clearing Member(s).

23 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Voluntary Tear-Up of the opportunity to participate in such tear-up.

24 In general, forced gains haircutting is a tool that can be more easily applied to products whose gains are settled at least daily, like futures through an exchange of variation margin, and by central counterparties with comparatively large daily settlement flows. Listed options, which constitute the

OCC has determined that its tear-up process – for both Voluntary Tear-Ups as well as Partial Tear-Ups – should be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC would be expected to have adequate remaining resources to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.[25]

In OCC's proposed tear-up process, the holders of torn-up positions would be assigned a Tear-Up Price and OCC would draw on its remaining financial resources in order to extinguish the torn-up positions at the assigned Tear-Up Price without forcing a reduction in the amount of unpaid value of such positions. OCC is amending the Initial Filing to clarify that while OCC does not intend, in the first instance, for its tear-up process to serve as a means of loss allocation, circumstances may arise such that, despite best efforts, OCC has inadequate remaining financial resources to extinguish torn-up positions at their assigned Tear-Up Price without forcing a reduction in the amount of unpaid value of such positions (e.g., despite best efforts, market movements not accounted for by monitoring, additional Clearing Member defaults occur immediately preceding a tear-up). In such circumstances, despite best efforts, OCC would use its partial tear-up process as a means of loss allocation.

The proposed changes would provide OCC with two separate and non-exclusive means of equitably re-allocating the losses, costs or expenses imposed upon the holders of torn-up positions as a result of the tear-up(s). First, the proposed changes to Article VIII would provide OCC discretion to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from such tear-up(s). Second, Rule 1111(a) would provide that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s) and the amount of such recovery exceeds the amount OCC received in voluntary payments, then non-defaulting Clearing Members and non-defaulting customers that voluntarily tore-up open positions and incurred losses from such tear-ups would be repaid from the amount of the recovery in excess of the amount OCC received in voluntary payments.[26] If the amount recovered is less than the aggregate amount of Voluntary Tear-Up, each

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vast majority of the contracts cleared by OCC, do not have daily settlement flows and any attempt to reduce the "unrealized gains" of a listed options contract would require the reduction of the option premium that is embedded within the required margin (such a process would effectively require haircutting the listed option's initial margin).

25 OCC anticipates that it would determine the date on which to initiate Partial Tear-Ups by monitoring its remaining financial resources against the potential exposure of the remaining unauctioned positions from the portfolio(s) of the defaulted Clearing Member(s).

26 In order to effect re-allocation of the losses, costs or expenses imposed upon the holders of torn-up positions, OCC expects that after it has completed its tear-up process and re-established a matched book, holders of both voluntarily torn-up and mandatorily torn-up positions would be provided with a limited opportunity to re-establish positions in the contracts that were voluntarily or mandatorily extinguished. After the expiration of such period, OCC would seek to collect the information on the losses, costs or expenses that had been imposed on the holders of torn-up positions. Based on the

non-defaulting Clearing Member and non-defaulting customer that incurred losses from voluntarily torn-up positions would be repaid in an amount proportionate to the percentage of its total amount of losses, costs and fees imposed on Clearing Members or customers as a result of the Voluntary Tear-Ups.

With respect to Voluntary Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

Proposed Addition of Ability to Conduct Partial Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will provide the Board with discretion to extinguish the remaining open positions of any defaulted Clearing Member or customer of such defaulted Clearing Member(s) (such positions, "Remaining Open Positions"), as well as any related open positions as necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions (such positions, "Related Open Positions"), in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default (such tear-ups hereinafter collectively referred to as "Partial Tear-Ups"). Like the determination for Voluntary Tear-Ups, the Risk Committee shall determine the appropriate scope of each Partial Tear-Up and such determination shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants. Once the Risk Committee has determined the scope of the Partial Tear-Up, OCC will initiate the Partial Tear-Up process by issuing a "Partial Tear-Up Notice." The Partial Tear-Up Notice shall (i) identify the Remaining Open Positions and Related Open Positions designated for tear-up, (ii) identify the open positions of non-defaulting Clearing Members and non-defaulting customers that will be subject to Partial Tear-Up (such positions, "Tear-Up Positions"), (iii) specify the termination price ("Partial Tear-Up Price") for each position to be torn-up, and (iv) list the date and time as of which the Partial Tear-Up will occur.[27] With regard to the date and time of a Partial Tear-Up, Rule 1111(d) specifies that the Risk Committee shall set the date and time. With regard to the Partial Tear-Up Price, OCC anticipates that it is likely to use the last established end-of-day settlement price, in accordance with its existing practices concerning pricing and valuation. However, given that it is not possible to know in advance the precise circumstances that would cause OCC to conduct a tear-up, Rule 1111(f) has been drafted to allow OCC to exercise reasonable discretion, if necessary, in establishing the Partial Tear-Up Price by some means other than its existing practices concerning pricing and

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information collected, OCC would determine whether it can reasonably determine the losses, costs and expenses sufficiently to re-allocate such amounts.

[27] Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Partial Tear-Up of the possibility of tear-up.

valuation.[28] Specifically, Rule 1111(f) would require that OCC, in exercising any such discretion, would act in good faith and in a commercially reasonable manner to adopt methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models that use the market price of the underlying interest or the market prices of its components. Rule 1111(f) further specifies that OCC may consider the same information set forth in subpart (c) of Section 27, Article VI of OCC's By-Laws.[29]

The scope of any Partial Tear-Up will be determined in accordance with Rule 1111(e).[30] With respect to the extinguishment of Remaining Open Positions, OCC will designate Tear-Up Positions in identical Cleared Contracts and Cleared Securities on the opposite side of the market and in an aggregate amount equal to that of the Remaining Open Positions. OCC will only designate Tear-Up Positions in the accounts of non-defaulting Clearing Members (inclusive of such Clearing Members' customer accounts) with an open position in the applicable Cleared Contract or Cleared Security.[31] Tear-Up Positions shall be designated and applied by OCC on a pro rata basis across all

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28 For example, OCC has observed certain rare circumstances in which a closing price for an underlying security of an option may be stale or unavailable. A stale or unavailable closing price could be the result of a halt on trading in the underlying security, or a corporate action resulting in a cash-out or conversion of the underlying security (but that has not yet been finalized), or the result of an ADR whose underlying security is being impacted by certain provisions under foreign laws. OCC would consider the presence of these factors on its end-of-day prices in determining whether use of the discretion that would be afforded under proposed Rule 1111(f) might be warranted.

29 In relevant part, subpart (c) reads as follows: "In determining a close-out amount, the Corporation may consider any information that it deems relevant, including, but not limited to, any of the following: (1) prices for underlying interests in recent transactions, as reported by the market or markets for such interests; (2) quotations from leading dealers in the underlying interest, setting forth the price (which may be a dealing price or an indicative price) that the quoting dealer would charge or pay for a specified quantity of the underlying interest; (3) relevant historical and current market data for the relevant market, provided by reputable outside sources or generated internally; and (4) values derived from theoretical pricing models using available prices for the underlying interest or a related interest and other relevant data. Amounts stated in a currency other than U.S. Dollars shall be converted to U.S. Dollars at the current rate of exchange, as determined by the Corporation. A position having a positive close-out value shall be an 'asset position' and a position having a negative close-out value shall be a 'liability position.'"

30 OCC amended the Initial Filing to reflect that after further evaluation of its proposed recovery tools and the proposed tear-up process, OCC does not believe there would be a need to assign or transfer any hedging transactions established with relation to tear-up positions. OCC therefore amended the Initial Filing to remove text in proposed Rule 1111(e) concerning proposed authority for OCC to offer to assign or transfer any hedging transactions related to Remaining Open Positions with related Tear-Up Positions.

31 Since the objective of Partial Tear-Ups is to extinguish the Remaining Open Positions cleared by the defaulted Clearing Member(s) *or customer of such defaulted Clearing Member(s)* (emphasis added), OCC amended the Initial Filing to remove references to non-defaulted customers of defaulted

the identical positions in Cleared Contracts and Cleared Securities on the opposite side of the market in the accounts of non-defaulted Clearing Members and their customers.[32]

Rule 1111(e)(iii) provides that every Partial Tear-Up position is automatically terminated upon and with effect from the Partial Tear-Up Time, without the need for any further step by any party to such Cleared Contract or Cleared Security, and that upon termination, either OCC or the relevant Clearing Member (as the case may be) shall be obligated to pay the other the applicable Partial Tear-Up Price. Rule 1111(e)(iii) further provides that the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.[33]

Rule 1111(g) provides that to the extent losses imposed upon non-defaulting Clearing Members and non-defaulting customers resulting from a Partial Tear-Up can reasonably be determined, the Board may elect to re-allocate such losses among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.[34]

With respect to Partial Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

OCC reviewed the DCO Core Principles as set forth in the Act. During this review, OCC identified the following Core Principles as potentially being impacted:

Clearing Members (OCC does not believe there would be a need to designate Tear-Up Positions to the non-defaulted customers of a defaulted Clearing Member).

32 OCC amended the Initial Filing to clarify that a non-defaulted Clearing Member would be required to allocate the assigned Tear-Up Positions on a pro rata basis across those customers that have open positions in such Cleared Contract or Cleared Security in such account, and for any listed option positions being extinguished, allocation across customer accounts should occur in accordance with such Clearing Member's procedures for allocating exercises and assignments.

33 OCC amended the Initial Filing and the proposed text of Rule 1111(e)(iii) to clarify that if OCC, in its discretion, determines that its remaining resources are inadequate to pay the applicable Partial Tear-Up Price for each position being extinguished in the Partial Tear-Up, OCC shall be obligated to pay each relevant Clearing Member a pro rata amount of the applicable Partial Tear-Up Price based on OCC's remaining resources, and the relevant Clearing Member shall have an unsecured claim against the Corporation for the value of the difference between the pro rata amount received and the Partial Tear-Up Price. With regard to amounts recovered from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) Rules 1011(b) and 111(a)(ii) would continue to apply.

34 For the avoidance of doubt, the special charge would be distinct and separate from a Clearing Member's obligation to satisfy Clearing Fund assessments, and therefore, would not be subject to the aforementioned assessment cap in the amount of 200% of a Clearing Member's then-required contribution to the Clearing Fund.

Financial Resources. OCC believes that implementing the proposed rule change will be consistent with the requirement in Core Principle B that each DCO have adequate financial, operational and managerial resources to discharge each of its responsibilities.[35] Rule 39.11(a) further implements Core Principle B by requiring a DCO to maintain sufficient financial resources to cover its exposures with a high degree of confidence and to enable it to perform its functions in compliance with the Core Principles.[36] The proposed changes to Section 6(a) and (b) of Article VIII of OCC's By-Laws would establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge. If adopted, the total amount of OCC's Clearing Fund resources (inclusive of assessments) would continue be sufficient to cover its exposures with a high degree of confidence. In this regard, the proposed changes would further OCC's compliance with Core Principle B and Rule 39.11(a).

Risk Management. OCC believes that implementing the proposed rule change will be aligned with the requirement in Core Principle D that a DCO limit its potential losses from defaults by members and participants of the DCO to ensure that its operations would not be disrupted and that its non-defaulting members or participants are not exposed to losses they cannot anticipate or control.[37] Rule 39.13(f) further implements Core Principle D by requiring each DCO to limit its exposure to potential losses from defaults by its clearing members to ensure that its operations would not be disrupted and that its non-defaulting members or participants are not exposed to losses they cannot anticipate or control.[38] The proposed changes to Section 6(a) and (b) of Article VIII of OCC's By-Laws would establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge. The proposed changes to Section 6(c) of Article VIII of OCC's By-Laws would clarify the requirements for a Clearing Member that chooses to terminate its membership during a cooling-off period (and thusly, cease liability for replenishment of the Clearing Fund immediately following the expiration of the cooling-off period). Further, new Rules 1011 and 1111 would establish OCC's authority to call for voluntary payments and conduct Voluntary Tear-Ups and Partial Tear-Ups. Collectively, these proposed changes would provide OCC with improved tools by which to limit its potential losses from defaults by Clearing Members and would provide OCC's Clearing Members with improved ability to anticipate and

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35 7 U.S.C. 7a-1(c)(2)(B)(i).

36 17 C.F.R. 39.11(a).

37 7 U.S.C. 7a-1(c)(2)(D)(iii).

38 17 C.F.R. 39.13(f).

control their default-related losses. In this regard, the proposed changes would further OCC's compliance with Core Principle D and Rule 39.13(f).

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 clearly state its default procedures, make its default rules publicly available and ensure that it may take timely action to contain losses and liquidity pressures and continue meeting each of its obligation.[39] Rule 39.16(c)(2)(ii) and (iv) further implement Core Principle G by requiring a DCO to adopt rules that set forth its default procedures, including the actions the DCO may take upon a default and the sequence in which the funds and assets of the defaulting clearing member and its customers and the financial resources maintained by the DCO in the event of a default.[40] Rule 39.16(c)(3) further implements Core Principle G by requiring a DCO to make its default rules publicly available.[41] The proposed changes to Sections 1(a), 5(a) and 6(a), (b) and (c) of Article VIII of OCC's By-Laws and proposed new Rules 1011 and 1111 would set forth certain of the actions OCC may take upon a default and the sequence in which OCC would deploy certain of its financial resources in the event of a default, and each of the proposed changes would be published on OCC's publicly accessible website. In this regard, the proposed changes would further OCC's compliance with Core Principle G and Rule 39.16(c)(2)(ii), (iv) and (3).

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 operating and default procedures governing the clearing and settlement systems of the DCO available to market participants and to disclose publicly information relevant to participation in the settlement and clearing activities of the DCO.[42] Rule 39.21(b) and (c)(6) further implement Core Principle L by requiring a DCO to make available its rules concerning default to market participants and publicly disclosing its rules and procedures for defaults.[43] The proposed changes to Sections 1(a), 5(a) and 6(a), (b) and (c) of Article VIII of OCC's By-Laws and proposed new Rules 1011 and 1111 would be published on OCC's publicly accessible website.

Opposing Views

No opposing views were expressed related to the rule amendments.

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39 7 U.S.C. 7a-1(c)(2)(G)(ii).

40 17 C.F.R. 39.16(c)(2)(ii) and (iv).

41 17 C.F.R. 39.16(c)(3).

42 7 U.S.C. 7a-1(c)(2)(L)(ii) and (iii)(V).

43 17 C.F.R. 39.21(b) and (c)(6).

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.

Certification

OCC hereby certifies that the rule set forth at Item 1 of the enclosed filings 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,

Daniel S. Konar II
Vice President, Assistant General Counsel

Enclosure

OMB APPROVAL
OMB Number: 3235-0045 Estimated average burden hours per response.....38

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 96

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2017 - * 020
Amendment No. (req. for Amendments *)

Filing by Options Clearing Corporation

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

Initial * ☑ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

19b-4(f)(1) 19b-4(f)(4)
19b-4(f)(2) 19b-4(f)(5)
19b-4(f)(3) 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document

Exhibit 3 Sent As Paper Document

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed rule change by The Options Clearing Corporation concerning enhanced and new tools for recovery scenarios.

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Justin Last Name * Byrne
Title * Vice President, Regulatory Filings
E-mail * jbyrne@theocc.com
Telephone * (202) 971-7238 Fax (312) 322-6280

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 12/08/2017
By Justin W. Byrne
(Name *)

(Title *)
Vice President, Regulatory Filings

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Justin Byrne, jbyrne@theocc.com

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information *

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

Add Remove View

Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

Add Remove View

Exhibit Sent As Paper Document

☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

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") would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario.

The proposed revisions to OCC's By-Laws and Rules are attached hereto as Exhibits 5A and 5B, and the proposed changes to OCC's Default Management Policy are included as confidential Exhibit 5C. Material proposed to be added to OCC's By-Laws, Rules, and Default Management Policy is marked by underlining and material proposed to be deleted is marked by strikethrough text.

The proposed changes are described in detail in Item 3, below.

All terms with initial capitalization not defined here have the same meaning set forth in OCC's By-Laws and Rules.[1]

Item 2. Procedures of the Self-Regulatory Organization

The proposed rule changes were approved for filing with the Commission by OCC's Board of Directors ("Board") at meetings held on April 4, 2017 and July 12, 2017.

Questions should be addressed to Daniel S. Konar II, Vice President and Associate

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[1] OCC's By-Laws and Rules can be found on OCC's public website: http://optionsclearing.com/about/publications/bylaws.jsp.

General Counsel, at (312) 322-2020.

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

A. Purpose

Background

The purpose of this proposed rule change is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. Each of the proposed revisions also is designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules identified immediately below.

On September 28, 2016, the Commission adopted amendments to Rule 17Ad-22[2] and added new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii)[3] pursuant to Section 17A of the Securities Exchange Act of 1934[4] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Payment, Clearing and Settlement

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2 17 CFR 240.17Ad-22.

3 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

4 15 U.S.C. 78q-1.

Supervision Act").[5] In relevant part, these new rules collectively require a covered clearing agency ("CCA"), as defined by Rule 17Ad-22(a)(5),[6] to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (1) maintain a risk management framework including plans for recovery and orderly wind-down necessitated by credit losses, liquidity shortfalls, general business risk losses or any other losses, (2) effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing and settlement processes, including by addressing the allocation of credit losses a CCA might face if its collateral and other resources are insufficient to fully cover its credit exposures, (3) effectively identify, measure, monitor and manage credit exposures, including by describing the process to replenish any financial resource that a CCA may use following a default event or other event in which use of such resource is contemplated, (4) effectively identify, measure, monitor and manage liquidity risks that arises or is borne by the CCA by, at a minimum, describing the process for replenishing any liquid resource that a CCA may employ during a stress event, (5) ensure it has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations, (6) publicly disclose relevant rules and material procedures, including key aspects of its default rules and procedures, and (7) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the CCA. The relevant portions of each of these new requirements is restated below:

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5 12 U.S.C. 5461 et. seq.

6 17 CFR 240.17Ad-22(a)(5).

- Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[m]aintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the [CCA], which…[i]ncludes plans for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[7]
- Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…[a]ddressing allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures, including the repayment of any funds the [CCA] may borrow from liquidity providers."[8]
- Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by …[d]escribing the [CCA's]

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7 17 CFR 240.17Ad-22(e)(3)(ii).

8 17 CFR 240.17Ad-22(e)(v)(viii).

process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[9]

- Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively measure, monitor, and manage the liquidity risk that arises in or is borne by the [CCA], including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, doing the following...[d]escribing the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[10]
- Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure 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…"[11]
- Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[12]

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9 17 CFR 240.17Ad-22(e)(4)(ix).

10 17 CFR 240.17Ad-22(e)(7)(ix).

11 17 CFR 240.17Ad-22(e)(13).

12 17 CFR 240.17Ad-22(e)(23)(i).

- Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[13]

OCC meets the definition of a CCA and is therefore subject to the requirements of the CCA rules, including new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).[14]

Proposed Changes

Summary of Proposed Changes

In order to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default, OCC is proposing to make the following revisions to its Rules and By-Laws:

(1) Revise the existing assessment powers in Section 6 of Article VIII of OCC's By-Laws, specifically to:

(a) Establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate

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13 17 CFR 240.17Ad-22(e)(23)(ii).

14 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix) and (e)(7)(ix).

charge;

(b) Clarify that a Clearing Member that chooses to terminate its membership status during a cooling-off period will not be liable for replenishment of the Clearing Fund immediately following the expiration of such cooling-off period, provided that the withdrawing Clearing Member satisfies enumerated criteria, including providing notice of such termination by no later than the end of the cooling-off period and by closing-out and/or transferring of all its open positions with OCC by no later than the last day of the cooling-off period; and

(c) Delineate between the obligation of a Clearing Member to replenish its contributions to the Clearing Fund and its obligations to meet additional "assessments" that may be levied following a proportionate charge to the Clearing Fund.

(2) Adopt a new Rule 1009 that would provide OCC with discretionary authority to call for voluntary payments from non-defaulting Clearing Members in a circumstance where one or more Clearing Members has already defaulted and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Rule 1009 also would establish that OCC would prioritize compensation of Clearing Members that made voluntary payments from any amounts recovered from the defaulted Clearing Members.

(3) Adopt a new Rule 1111 that would provide authority to:

(a) Allow OCC to call for voluntary tear-ups ("Voluntary Tear-Up," as defined below) of non-defaulting Clearing Member and/or customer positions at any time following the suspension or default of a Clearing Member, with the scope of any such

Voluntary Tear-Ups being determined by the Risk Committee of OCC's Board ("Risk Committee");

(b) Allow OCC's Board to vote to tear-up the "Remaining Open Positions" (defined below) of a defaulted Clearing Member, as well as any "Related Open Positions" (defined below) in a circumstance where OCC has attempted one or more auctions of such defaulted Clearing Member's remaining open positions and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default with the scope of any such tear-up ("Partial Tear-Up") being determined by the Risk Committee; and

(c) Allow OCC's Board to vote to re-allocate losses, costs and fees imposed upon holders of positions extinguished in a Partial Tear-Up through a special charge levied against remaining non-defaulting Clearing Members.

(4) Revise the descriptions and authorizations in Article VIII of OCC's By-Laws concerning the use of the Clearing Fund to reflect the discretion of OCC to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from a Voluntary Tear-Up or a mandatory tear-up ("Partial Tear-Up," as defined below).

Discussion of Proposed Changes

Each of the proposed revisions to OCC's Rules and By-Laws is described in more detail in the following sub-sections:

1. Proposed Changes to OCC's Assessment Powers

a. Current Assessment Powers

OCC's current assessment powers are described in Section 6 of Article VIII of OCC's By-Laws. Section 6 establishes a general requirement for each Clearing Member to promptly make good any deficiency in its required contribution to the Clearing Fund whenever an amount is paid out of its Clearing Fund contribution (whether by proportionate charge or otherwise).[15] In this regard, a Clearing Member's obligation to replenish the Clearing Fund is not currently subject to any pre-determined limit. Notwithstanding the foregoing, a Clearing Member can limit the amount of its liability for replenishing the Clearing Fund (at an additional 100% of the amount of its then-required Clearing Fund contribution) by winding-down its clearing activities and terminating its status as a Clearing Member. Any Clearing Member seeking to so limit its liability for replenishing the Clearing Fund must: (i) notify OCC in writing not later than the fifth business day after the proportionate charge that it is terminating its status as a Clearing Member,

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15 Under Article VIII, Section 6 of OCC's By-Laws, OCC currently has authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund in certain enumerated situations. For example, Section 6 generally provides that if the conditions regarding a Clearing Member default specified in subparagraphs (a)(i) through (vi) of Article VIII, Section 5 of OCC's By-Laws are satisfied, OCC will make good resulting losses or expenses that are suffered by OCC by applying the defaulting Clearing Member's Clearing Fund contribution after first applying other funds available to OCC in the accounts of the Clearing Member. If the sum of the obligations, however, exceeds the total Clearing Fund contribution and other funds of the defaulting Clearing Member available to OCC, then OCC will charge the amount of the remaining deficiency on a proportionate basis against all non-defaulting Clearing Members' required contributions to the Clearing Fund at the time. Section 5(b) of Article VIII of OCC's By-Laws similarly provides for proportionate charges against Clearing Members' contributions to the Clearing Fund when certain conditions are met that involve a failure by a bank or a securities or commodities clearing organization to perform obligations to OCC when they are due.

(ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close out or transfer all of its open positions as promptly as practicable after giving notice to OCC. Thus, withdrawal from clearing membership is the only means by which a Clearing Member currently can limit its liability for replenishing the Clearing Fund.

b. Proposed Changes to Assessment Powers

OCC proposes to amend Section 6 of Article VIII of OCC's By-Laws to make three primary modifications regarding its existing authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund. First, the proposal introduces an automatic minimum fifteen calendar day "cooling-off" period that begins when a proportionate charge is assessed by OCC against Clearing Members' Clearing Fund contributions. While the cooling-off period will continue for a minimum of fifteen consecutive calendar days, if one or more of the events described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws occur(s) during that fifteen calendar day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through either (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth day from the date of the proportionate charge that initiated the cooling-off period, whichever is sooner.

During a cooling-off period, each Clearing Member would have its aggregate liability to replenish the Clearing Fund capped at 200% of the Clearing Member's then-required

contribution to the Clearing Fund. Once the cooling-off period ends each remaining Clearing Member would be required to replenish the Clearing Fund in the amount necessary to meet its then-required contribution. Once the cooling-off period ends, any remaining losses or expenses suffered by OCC as a result of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that occurred during such cooling-off period could not be charged against the amounts Clearing Members have contributed to replenish the Clearing Fund upon the expiration of the cooling-off period.[16]

Second, in connection with the cooling-off period, the proposal would extend the time frame within which a Clearing Member may provide a termination notice to OCC to avoid liability for replenishment of the Clearing Fund after the cooling-off period and would modify the obligations of such a terminating Clearing Member for closing-out and transferring its remaining open positions. Specifically, to effectively terminate its status as a Clearing Member and not be liable for replenishing the Clearing Fund after the cooling-off period, a Clearing Member would be required to: (i) notify OCC in writing of its intent to terminate not later than the last day of the cooling-off period, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close-out or transfer all of its open positions by no later than the last day of the cooling-off period. If a

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16 After a cooling-off period has ended, the occurrence of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that results in a proportionate charge against the Clearing Fund would trigger a new cooling off period, and thusly, a cap of 200% of each Clearing Member's then-required contribution would again apply.

Clearing Member fails to satisfy all of these conditions by the end of a given cooling-off period, it would not have completed all of the requirements necessary to terminate its status as a Clearing Member under Article VIII, Section 6 of OCC's By-Laws and therefore it would remain subject to the obligation to replenish the Clearing Fund after the end of the cooling-off period.

Third, the proposal would clarify the distinction between "replenishment" of the Clearing Fund and a Clearing Member's obligation to answer "assessments." In this context, the term "replenish" (and its variations) shall to refer to a Clearing Member's standing duty, following any proportionate charge against the Clearing Fund, to return its Clearing Fund contribution to the amount required from such Clearing Member for the month in question.[17] The term "assessment" (and its variations) shall refer to the amount, during any cooling-off period, that a Clearing Member would be required to contribute to the Clearing Fund in excess of the amount of the Clearing Member's pre-funded required Clearing Fund contribution.

Proposed Addition of Ability to Request Voluntary Payments

OCC proposes to add new Rule 1009, which will provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under

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17 This assumes that the proportionate charge resulted in the Clearing Member's actual Clearing Fund contribution dropping below the amount of its required contribution (*i.e.*, that the Clearing Member did not have excess above its required contribution that was sufficient to cover the amount of the proportionate charge allocated to such Clearing Member).

OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[18] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under new Rule 1009, OCC will initiate a call for voluntary payments by issuing a "Voluntary Payment Notice" inviting all non-defaulting Clearing Members to make payments to the Clearing Fund in addition to any amounts they are otherwise required to contribute pursuant to Rule 1001. The Voluntary Payment Notice would specify the terms applicable to any voluntary payment, including but not limited to, that any voluntary payment may not be withdrawn once made, that no Clearing Member shall be obligated to make a voluntary payment and that OCC shall retain full discretion to accept or reject any voluntary payment. Rule 1009 specifies that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s), OCC would seek to compensate first from such recovery all non-defaulting Clearing Members that made voluntary payments (and if the amount recovered from the defaulted Clearing Member(s) is less than the aggregate amount of voluntary payments, non-defaulting Clearing Members that made voluntary payments each would receive a percentage of the recovery that corresponds to that Clearing Member's percentage of the total amount of voluntary payments received).

Proposed Addition of Ability to Conduct Voluntary Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will establish a framework

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18 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to voluntarily extinguish (i.e., voluntarily tear-up) their open positions at OCC in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.

While Risk Committee approval is not needed to commence a voluntary tear-up, the Risk Committee would be responsible for determining the appropriate scope of each voluntary tear-up. To ensure OCC retains sufficient flexibility to effectively deploy this tool in an extreme stress event, proposed Rule 1111(c) is drafted to provide the Risk Committee with discretion to determine the appropriate scope of each voluntary tear-up.[19] New Rule 1111(c) also would impose standards designed to circumscribe the Risk Committee's discretion, requiring that any determination regarding the scope of a voluntary tear-up shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

Once the Risk Committee has determined the scope of the Voluntary Tear-Up, OCC will initiate the call for voluntary tear-ups by issuing a "Voluntary Tear-Up Notice." The Voluntary Tear-Up Notice shall inform all non-defaulting Clearing Members of the opportunity to

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19 Notwithstanding the discretion that would be afforded by the text of proposed Rule 1111(c), OCC anticipates that the scope of voluntary tear-ups likely would be dictated by the cleared contracts remaining in the portfolio(s) of the defaulted Clearing Member(s).

participate in a Voluntary Tear-Up.[20] The Voluntary Tear-Up Notice would specify the terms applicable to any voluntary tear-up, including but not limited to, that no Clearing Member or customers of a Clearing Member shall be obligated to participate in a voluntary tear-up and that OCC shall retain full discretion to accept or reject any voluntary tear-up.

OCC is not proposing a tear-up process that would require the imposition of "gains haircutting" (*i.e.*, the reduction of unpaid gains) on a portion of OCC's cleared contracts.[21] Instead, OCC has determined that its tear-up process – for both Voluntary Tear-Ups as well as Partial Tear-Ups – should be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC would be expected to have adequate remaining resources to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.[22]

In OCC's proposed tear-up process, the holders of torn-up positions would be assigned a

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20 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Voluntary Tear-Up of the opportunity to participate in such tear-up.

21 In general, forced gains haircutting is a tool that can be more easily applied to products whose gains are settled at least daily, like futures through an exchange of variation margin, and by central counterparties with comparatively large daily settlement flows. Listed options, which constitute the vast majority of the contracts cleared by OCC, do not have daily settlement flows and any attempt to reduce the "unrealized gains" of a listed options contract would require the reduction of the option premium that is embedded within the required margin (such a process would effectively require haircutting the listed option's initial margin).

22 OCC anticipates that it would determine the date on which to initiate Partial Tear-Ups by monitoring its remaining financial resources against the potential exposure of the remaining unauctioned positions from the portfolio(s) of the defaulted Clearing Member(s).

Tear-Up Price and OCC would draw on its remaining financial resources in order to extinguish the torn-up positions at the assigned Tear-Up Price without forcing a reduction in the amount unpaid gains on such positions. The proposed changes would provide OCC with two separate and non-exclusive means of equitably re-allocating the losses, costs or expenses imposed upon the holders of torn-up positions as a result of the tear-up(s). First, the proposed changes to Article VIII would provide OCC discretion to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from such tear-up(s). Second, Rule 1111(a) would provide that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s) and the amount of such recovery exceeds the amount OCC received in voluntary payments, then non-defaulting Clearing Members and non-defaulting customers that voluntarily tore-up open positions and incurred losses from such tear-ups would be repaid from the amount of the recovery in excess of the amount OCC received in voluntary payments.[23] If the amount recovered is less than the aggregate amount of Voluntary Tear-Up, each non-defaulting Clearing Member and non-defaulting customer that incurred losses from voluntarily torn-up positions would be repaid in an amount proportionate to the percentage of its total amount of losses, costs and fees imposed on

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[23] In order to effect re-allocation of the losses, costs or expenses imposed upon the holders of torn-up positions, OCC expects that after it has completed its tear-up process and re-established a matched book, holders of both voluntarily torn-up and mandatorily torn-up positions would be provided with a limited opportunity to re-establish positions in the contracts that were voluntarily or mandatorily extinguished. After the expiration of such period, OCC would seek to collect the information on the losses, costs or expenses that had been imposed on the holders of torn-up positions. Based on the information collected, OCC would determine whether it can reasonably determine the losses, costs and expenses sufficiently to re-allocate such amounts.

Clearing Members or customers as a result of the Voluntary Tear-Ups.

With respect to Voluntary Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

Proposed Addition of Ability to Conduct Partial Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will provide the Board with discretion to extinguish the remaining open positions of any defaulted Clearing Member or customer of such defaulted Clearing Member(s) (such positions, "Remaining Open Positions"), as well as any related open positions as necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions (such positions, "Related Open Positions"), in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default (such tear-ups hereinafter collectively referred to as "Partial Tear-Ups"). Like the determination for Voluntary Tear-Ups, the Risk Committee shall determine the appropriate scope of each Partial Tear-Up and such determination shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants. Once the Risk Committee has determined the scope of the Partial Tear-Up, OCC will initiate the Partial Tear-Up process by issuing a "Partial Tear-Up Notice." The Partial Tear-Up Notice shall (i) identify the Remaining Open Positions and Related Open Positions designated for tear-up, (ii) identify the open positions of non-defaulting

Clearing Members and non-defaulting customers that will be subject to Partial Tear-Up (such positions, "Tear-Up Positions"), (iii) specify the termination price ("Partial Tear-Up Price") for each position to be torn-up, and (iv) list the date and time as of which the Partial Tear-Up will occur.[24] With regard to the date and time of a Partial Tear-Up, Rule 1111(d) specifies that the Risk Committee shall set the date and time. With regard to the Partial Tear-Up Price, OCC anticipates that it is likely to use the last established end-of-day settlement price, in accordance with its existing practices concerning pricing and valuation. However, given that it is not possible to know in advance the precise circumstances that would cause OCC to conduct a tear-up, Rule 1111(f) has been drafted to allow OCC to exercise reasonable discretion, if necessary, in establishing the Partial Tear-Up Price by some means other than its existing practices concerning pricing and valuation. Specifically, Rule 1111(f) would require that OCC, in exercising any such discretion, would act in good faith and in a commercially reasonable manner to adopt methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models that use the market price of the underlying interest or the market prices of its components. Rule 1111(f) further specifies that OCC may consider the same information set forth in subpart (c) of Section 27, Article VI of OCC's By-Laws.[25]

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[24] Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Partial Tear-Up of the possibility of tear-up.

[25] In relevant part, subpart (c) reads as follows: "In determining a close-out amount, the Corporation may consider any information that it deems relevant, including, but not limited to, any of the following: (1) prices for underlying interests in recent transactions,

The scope of any Partial Tear-Up will be determined in accordance with Rule 1111(e). With respect to the extinguishment of Remaining Open Positions, OCC will designate Tear-Up Positions in identical Cleared Contracts and Cleared Securities on the opposite side of the market and in an aggregate amount equal to that of the Remaining Open Positions. OCC will only designate Tear-Up Positions in the accounts of non-defaulting Clearing Members (inclusive of such Clearing Members' customer accounts) with an open position in the applicable Cleared Contract or Cleared Security and of non-defaulted customers of a defaulted Clearing Member. Tear-Up Positions shall be designated and applied by OCC on a pro rata basis across all the identical positions in Cleared Contracts and Cleared Securities on the opposite side of the market in the accounts of non-defaulted Clearing Members and non-defaulted customers (including the non-defaulted customers of defaulted Clearing Members).

Rule 1111(e)(iii) provides that every Partial Tear-Up position is automatically terminated upon and with effect from the Partial Tear-Up Time, without the need for any further step by any party to such Cleared Contract or Cleared Security, and that upon termination, either OCC or the relevant Clearing Member (as the case may be) shall be obligated to pay the other the applicable

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as reported by the market or markets for such interests; (2) quotations from leading dealers in the underlying interest, setting forth the price (which may be a dealing price or an indicative price) that the quoting dealer would charge or pay for a specified quantity of the underlying interest; (3) relevant historical and current market data for the relevant market, provided by reputable outside sources or generated internally; and (4) values derived from theoretical pricing models using available prices for the underlying interest or a related interest and other relevant data. Amounts stated in a currency other than U.S. Dollars shall be converted to U.S. Dollars at the current rate of exchange, as determined by the Corporation. A position having a positive close-out value shall be an 'asset position' and a position having a negative close-out value shall be a 'liability position.'"

Partial Tear-Up Price. Rule 1111(e)(iii) further provides that the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.

Rule 1111(g) provides that to the extent losses imposed upon non-defaulting Clearing Members and non-defaulting customers resulting from a Partial Tear-Up can reasonably be determined, the Board may elect to re-allocate such losses among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.[26]

With respect to Partial Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

B. Statutory Basis

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934 ("Act"),[27] requires, among other things, that the rules of a clearing agency be designed to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest. OCC believes that the proposed rule change is consistent with the

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26 For the avoidance of doubt, the special charge would be distinct and separate from a Clearing Member's obligation to satisfy Clearing Fund assessments, and therefore, would not be subject to the aforementioned assessment cap in the amount of 200% of a Clearing Member's then-required contribution to the Clearing Fund.

27 15 U.S.C. 78q-1(b)(3)(F).

requirements of Section 17A(b)(3)(F) of the Act[28] and the rules thereunder applicable to OCC for the reasons set forth below.

As stated above, each of the changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario. In this regard, the proposed changes are designed to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to establish tools to enable OCC to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC's process in crafting the proposed changes was informed by published guidance from OCC's primary regulators (the Commission and the Commodity Futures Trading Commission), the publications of key international organizations (including the Bank for International Settlements, the International Organization of Securities Commissions and the Financial Stability Board) and the publications of key industry trade organizations. OCC's proposal was further informed by conversations with, among others, OCC's Board, OCC's Risk Committee, Clearing Members and market participants.

Informed by these perspectives, OCC has crafted the proposed changes with the aim of enhancing its ability to address an unprecedented loss event but also, to the extent possible, providing a reasonable amount of certainty to Clearing Members, customers and other stakeholders about the potential consequences of such an event and the resources and tools that

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28 Id.

would be expected to be available to OCC in support of its clearing operations.[29] Accordingly, the proposed changes should leave Clearing Members, customers and other stakeholders in a position to better evaluate the risks and benefits of clearing in order to facilitate their own risk management, and to the extent applicable, their own regulatory and capital considerations. The proposed changes also seek to avoid a result that would force only particular clearing participants to shoulder certain losses in an extreme stress scenario (*i.e.*, holders of positions extinguished in Partial Tear-Ups),[30] and instead leaves OCC and its Board with discretionary tools that could provide a more equitable method of allocating the losses from such an event more broadly, consistent with the general principle of mutualized loss that upon which central clearing rests. In this regard, OCC believes the proposed changes foster cooperation and coordination with participants in the clearing system, consistent with Section 17A(b)(3)(F) of the Act.[31]

As stated above, the proposed changes are designed to enable OCC to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures.

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29 OCC notes that the very nature of an extreme stress and unprecedented loss event means that its impact is difficult to predict and quantify in advance.

30 Absent a means of re-allocating the potential losses, costs and fees imposed upon holders of positions extinguished during tear-ups, the holders of such positions would be left to individually address such losses, costs and fees.

31 15 U.S.C. 78q-1(b)(3)(F).

OCC believes that the proposed changes will facilitate its ability to fully allocate, and ultimately extinguish, the loss so that it has a better opportunity of withstanding an extreme stress scenario without sacrificing its viability as a going concern or its ability to continue to provide its critical clearing services. In this regard, OCC believes that the proposed changes remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.[32]

The proposed changes are designed to enhance the stability of the clearing system generally and are aimed at ensuring that OCC has adequate tools and resources to better protect market participants from the risks of extreme stress scenarios and unprecedented loss events. In this regard, OCC believes that the proposed changes are reasonably designed to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.[33]

The proposed changes also are designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules discussed immediately below:

Recovery and Orderly Wind-Down

In relevant part, Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…plan[] for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[34] As stated above, each of the proposed

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32 Id.

33 Id.

34 17 CFR 240.17Ad-22(e)(3)(ii).

changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario.[35] Consistent with the requirements of Rule 17Ad-22(e)(3)(ii), the proposed tools would enable OCC to better address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and, if necessary, to ultimately re-establish a matched book in a recovery or orderly wind-down scenario.[36] In this context, the proposed changes serve as a critical component of OCC's recovery and orderly wind-down plan. As a result, in OCC's view, the proposed changes are consistent with the requirements of Rule 17Ad-22(e)(3)(ii) as to the recovery and orderly wind-down plan.[37]

Allocation of Credit Losses Above Available Resources

In relevant part, Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to …[a]ddress[] allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures…"[38] The proposed changes would provide OCC with three distinct tools that could be used to allocate any credit losses OCC may face in excess of

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35 Indeed, the OCC's separately filed recovery and orderly wind-down plan identifies OCC's assessment powers, ability to call for voluntary payments, ability to call for Voluntary Tear-Ups and ability to impose Partial Tear-Ups among its "Recovery Tools." OCC has filed a proposed rule change with the Commission in connection with this proposal. See SR-OCC-2017-021.

36 17 CFR 240.17Ad-22(e)(3)(ii).

37 17 CFR 240.17Ad-22(e)(3)(ii).

38 17 CFR 240.17Ad-22(e)(v)(viii).

collateral and other resources available to OCC. First, new Rule 1009 would provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[39] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Second, new Rule 1111 would establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to participate in Voluntarily Tear-Ups in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Finally, new Rule 1111 also would provide the Board with discretion to mandatorily tear-up Remaining Open Positions and Related Open Positions, in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[40] In OCC's view,

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39 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

40 Rule 1010(g), which would provide the Board authority to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting

each of these tools could be deployed by OCC, if necessary, to allocate credit losses in excess of the collateral and other resources available to OCC, in accordance with Rule 17Ad-22(e)(4)(viii).[41]

Replenishment of Financial Resources Following a Default

In relevant part, Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[42] OCC's Clearing Members have a standing obligation to replenish the Clearing Fund following any proportionate charge. The proposed changes would establish a rolling cooling-off period, triggered by the payment of a proportionate charge against the Clearing Fund, during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge. Compared to the current requirement under which a Clearing Member may cap its liability to proportionate charges at an additional 100% of its then-required contribution, a Clearing Member would instead be permitted to cap its liability for proportionate charges at an additional 200% of its then-required Clearing Fund contribution.

Clearing Members through a special charge, would serve as a discretionary tool to redistribute the credit losses allocated through Partial Tear-Up.

41 17 CFR 240.17Ad-22(e)(v)(viii).

42 17 CFR 240.17Ad-22(e)(4)(ix).

OCC believes that the proposed approach improves predictability for OCC and for Clearing Members regarding the size of Clearing Fund contributions that are likely to be subject to assessments for proportionate charges. Additionally, replacing the five business day withdrawal period with the withdrawal period commensurate with the cooling-off period (which, as proposed would be a minimum of fifteen calendar days) would give Clearing Members a more reasonable period in which to meet the wind-down and termination requirements necessary to cap their liability. OCC believes that this would afford them greater certainty regarding their maximum liability with respect to the Clearing Fund during extreme stress events, which in turn, facilitates Clearing Members' management of their own risk management, and to the extent applicable, regulatory capital considerations. And OCC believes this increased predictability would also be beneficial to OCC by helping it to more reliably understand the amount of Clearing Fund contributions that will likely be available to it after a proportionate charge is assessed.[43]

OCC believes that the relative certainty provided by the proposed cooling-off period and 200% cap on assessments ultimately could reduce the risks of successive or "cascading" defaults, in which the financial demands on remaining non-defaulting Clearing Members to continually replenish OCC's Clearing Fund (and similar guaranty funds at other CCPs to which such Clearing Members might belong) have the effect of further weakening such Clearing Members to the point of default. In this regard, the proposed changes are designed to provide OCC, Clearing

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43 Under the existing approach, it is less certain from OCC's standpoint regarding whether Clearing Members would reasonably be able to cap their liability to proportionate charges within five business days.

Members and other stakeholders with sufficient time to manage the ongoing default(s) without further aggravating the extreme stresses facing market participants.

OCC recognizes that the proposed changes would limit the maximum amount of Clearing Fund resources that could be available to OCC in an extreme stress scenario, which introduces the possibility, however remote, that the proposed 200% cap ultimately could be reached. If during any cooling-off period the amount of aggregate proportionate charges against the Clearing Fund approaches the 200% cap, the amount remaining in the Clearing Fund may no longer be sufficient to comply with the applicable minimum regulatory financial resources requirements in the CCAs. In any such event, OCC's existing authority under Rule 603 would permit OCC to call on participants for additional initial margin, which could ensure that OCC's minimum financial resources remain in excess of applicable CCA requirements.[44] OCC recognizes that the imposition of increased margin requirements could have an immediate pro-cyclical impact on participants (and consequential impacts on the broader financial system) that is potentially greater than the impact of replenishing the Clearing Fund. These risks would be limited to a specific extreme stress event and could be mitigated by certain factors. First, OCC, in coordination with its regulators, would carefully evaluate any potential increase in the context of then-existing facts and circumstances. Second, during the cooling-off period, Clearing Members and their customers will have the opportunity to reduce or rebalance their respective portfolios in

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44 Rule 603 provides that "[t]he Risk Committee may, from time to time, increase the amount of margin which may be required in respect of a cleared contract, open short position or exercised contract if, in its discretion, it determines that such increase is advisable for the protection of [OCC], the Clearing Members or the general public."

order to mitigate their exposures to stress losses and initial margin increases. Finally, since initial margin is not designed to be subject to mutualized loss, the risk of loss faced by Clearing Members for amounts posted as additional margin would be substantially less than for replenishments of the Clearing Fund.

Given the products cleared by OCC and the composition of its clearing membership, OCC has determined that a minimum 15-calendar day cooling-off period, rolling up to a maximum of 20 calendar days, is likely to be a sufficient amount of time for OCC to manage the ongoing default(s) and take necessary steps in furtherance of stabilizing the clearing system. Further, through conversations with Clearing Members, OCC believes that the proposed cooling-off period is likely to be a sufficient amount for Clearing Members (and their customers) to orderly reduce or rebalance their positions, in an attempt to mitigate stress losses and exposure to potential initial margin increases as they navigate the stress event. Through conversations with Clearing Members, OCC also believes that the proposed cooling-off period is likely to be a sufficient amount for certain Clearing Members to orderly close-out their positions and transfer customer positions as they withdraw from clearing membership. OCC believes the proposed cooling-off period, coupled with the other proposed changes to OCC's assessment powers, is likely to provide Clearing Members with an adequate measure of stability and predictability as to the potential use of Clearing Fund resources, which OCC believes removes the existing incentive for Clearing Members to withdraw following a proportionate charge.[45]

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45 OCC initially considered a fixed 15-calendar day cooling-off period; however, OCC concluded that a fixed 15-calendar day cooling-off period may increase the risks of

In light of the foregoing, OCC believes that the proposed changes would enhance and strengthen its process to replenish the Clearing Fund following a default or other event in which use of the Clearing Fund is contemplated, in accordance with Rule 17Ad-22(e)(4)(ix).[46]

Replenishment of Liquid Resources

In relevant part, Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[47] Since the use any part of the cash portion of OCC's Clearing Fund would constitute a depletion of one of OCC's liquid resources, OCC's assessment power, discussed above, is the primary means of replenishing the Clearing Fund cash that OCC used to address the stress event. For the same reasons stated above, OCC believes that the proposed changes enhance and strengthen its process to replenish the Clearing Fund, as necessary, following a default or other stress event in which the Clearing Fund is used, and therefore, OCC views the proposed changes as consistent with Rule 17Ad-22(e)(7)(ix).[48]

Timely Action to Contain Losses

In relevant part, Rule 17Ad-22(e)(13) requires that each CCA "establish, implement,

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successive or cascading Clearing Member defaults and may perversely incentivize Clearing Members to seek to withdraw from clearing membership. Through conversations with Clearing Members, OCC believes that these potentially disruptive consequences are mitigated by the proposed rolling cooling-off period.

46 17 CFR 240.17Ad-22(e)(4)(ix).

47 17 CFR 240.17Ad-22(e)(7)(ix).

48 17 CFR 240.17Ad-22(e)(7)(ix).

maintain and enforce written policies and procedures reasonably designed to…[e]nsure the [CCA] has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations…"[49] The proposed changes would provide OCC with the authority to call for Voluntary Tear-Ups and OCC's Board with the discretion to impose Partial Tear-Ups, which would provide OCC with authority necessary to extinguish certain losses (and attendant liquidity demands) thereby potentially enabling OCC to continue to meet its remaining obligations to participants. As designed, Voluntary Tear-Ups and Partial Tear-Ups would be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC is expected to have adequate resources remaining to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains. Accordingly, OCC believes that its authority and capacity to conduct a Partial Tear-Up should be timely, relative to the adequacy of OCC's remaining financial resources. Finally, OCC believes it has the operational and systems capacity sufficient to support the proposed changes, and OCC's policies and procedures will be updated accordingly to reflect the existence of these new tools. As a result, OCC believes that the proposed changes conform to the relevant requirements in Rule 17Ad-22(e)(13).[50]

Public Disclosure of Key Aspects of Default Rules

In relevant part, Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly

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49 17 CFR 240.17Ad-22(e)(13).

50 17 CFR 240.17Ad-22(e)(13).

disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[51] As stated above, each of the tools discussed herein are contemplated to be deployed by OCC if an extreme stress event has placed OCC into a recovery or orderly wind-down scenario, and therefore, the tools discussed herein constitute key aspects of OCC's default rules. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that proposed changes would conform to the relevant requirements in Rule 17Ad-22(e)(23)(i).[52]

Sufficient Information Regarding the Risks, Fees and Costs of Clearing

In relevant part, Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[53] The proposed changes would clearly explain to Clearing Members and market participants that an extreme stress scenario could result in the use – and theoretically the exhaustion – of OCC's financial resources, inclusive of OCC's proposed assessment powers. Proposed changes to Section 6, Article VIII of OCC's By-Laws would explain Clearing Members' replenishment obligation and liability for assessments. The proposed changes also would clearly explain, through proposed Rules 1009 and 1111, that as OCC nears the exhaustion of its assessment powers, Clearing

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51 17 CFR 240.17Ad-22(e)(23)(i).

52 17 CFR 240.17Ad-22(e)(13).

53 17 CFR 240.17Ad-22(e)(23)(ii).

Members may be asked for voluntary payments and, if necessary, Clearing Members and customers may be asked to participate in a Voluntary Tear-Up and/or subject to a Partial Tear-Up. Proposed Rules 1009(b) and 1111(a)(ii) also would make clear that Clearing Members that made voluntary payments and Clearing Members and customers whose tendered positions were extinguished in the Voluntary Tear-Up would be prioritized in the distribution of any recovery from the defaulted Clearing Member(s). Proposed changes to Article VIII would clarify that the Clearing Fund contributions remaining after OCC has conducted a Voluntary Tear-Up or Partial Tear-Up could be used to compensate the non-defaulting Clearing Members and non-defaulting customers for the losses, costs or fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up. Proposed Rule 1111(g) would make clear that, following a Partial Tear-Up, OCC's Board may seek to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that is has provided sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they could incur by participating OCC, consistent with the requirements in Rule 17Ad-22(e)(23)(ii).[54]

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54 17 CFR 240.17Ad-22(e)(23)(ii).

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

Section 17A(b)(3)(I) of the Act[55] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. OCC does not believe the proposed rule change would have any impact or impose any burden on competition. The primary purpose of the proposed changes is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. As explained above, each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. The proposed rule change is intended to provide Clearing Members, market participants and other stakeholders with greater certainty as to their liabilities and potential exposure to OCC in the event of an unprecedented loss scenario. OCC does not believe that the proposed changes would discriminatorily impact any Clearing Member's access to OCC's services or unnecessarily disadvantage or favor any particular user in relationship to another user. OCC recognizes that the nature of a Partial Tear-Up means that only particular Clearing Members and market participants holding certain positions may be impacted; however, the risk of Partial Tear-Ups is extremely remote, and even then, the proposed changes seek to provide means of equitably re-allocating the losses, costs and fees imposed by Voluntary Tear-Up or Partial Tear-Up. Therefore, OCC believes that the proposed changes would not have any impact or impose any burden on competition.

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55 15 U.S.C. 78q-1(b)(3)(I).

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 change and none have been received. OCC will notify the Commission of any written comments received by OCC.

Item 6. **Extension of Time Period for Commission Action**

Not applicable.

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)**

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

(d) Not applicable.

Item 8. **Proposed Rule Change Based on Rule 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 Proposed Rule Change for publication in the Federal Register.

Exhibit 5A. OCC By-Laws

Exhibit 5B. OCC Rules

Exhibit 5C. Default Management Policy

CONFIDENTIAL TREATMENT IS REQUESTED FOR EXHIBIT 5C

PURSUANT TO SEC RULE 24b-2

SIGNATURES

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

THE OPTIONS CLEARING CORPORATION

By:_____
Daniel S. Konar
Vice President and Associate General Counsel

EXHIBIT 1A

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-[_____]; File No. SR-OCC-2017-020)

December __, 2017

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of a Proposed Rule Change Concerning Enhanced and New Tools for Recovery Scenarios

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 December 18, 2017, 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. Clearing Agency's Statement of the Terms of Substance of the Proposed Rule Change

This proposed rule change by the OCC would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario.

II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

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. All terms with initial capitalization not defined here have the same meaning set forth in OCC's By-Laws and Rules.[3]

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

1. Purpose

Background

The purpose of this proposed rule change is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. Each of the proposed revisions also is designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules identified immediately below.

On September 28, 2016, the Commission adopted amendments to Rule 17Ad-22[4] and added new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13),

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3 OCC's By-Laws and Rules can be found on OCC's public website: http://optionsclearing.com/about/publications/bylaws.jsp.

4 17 CFR 240.17Ad-22.

(e)(23)(i) and (e)(23)(ii)[5] pursuant to Section 17A of the Securities Exchange Act of 1934[6] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Payment, Clearing and Settlement Supervision Act").[7] In relevant part, these new rules collectively require a covered clearing agency ("CCA"), as defined by Rule 17Ad-22(a)(5),[8] to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (1) maintain a risk management framework including plans for recovery and orderly wind-down necessitated by credit losses, liquidity shortfalls, general business risk losses or any other losses, (2) effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing and settlement processes, including by addressing the allocation of credit losses a CCA might face if its collateral and other resources are insufficient to fully cover its credit exposures, (3) effectively identify, measure, monitor and manage credit exposures, including by describing the process to replenish any financial resource that a CCA may use following a default event or other event in which use of such resource is contemplated, (4) effectively identify, measure, monitor and manage liquidity risks that arises or is borne by the CCA by, at a minimum, describing the process for replenishing any liquid resource that a CCA may employ during a stress event, (5) ensure it has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations, (6) publicly disclose relevant rules and material

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5 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

6 15 U.S.C. 78q-1.

7 12 U.S.C. 5461 et. seq.

8 17 CFR 240.17Ad-22(a)(5).

procedures, including key aspects of its default rules and procedures, and (7) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the CCA. The relevant portions of each of these new requirements is restated below:

- Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[m]aintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the [CCA], which…[i]ncludes plans for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[9]
- Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…[a]ddressing allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures, including the repayment of any funds the [CCA] may borrow from liquidity providers."[10]
- Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and

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9 17 CFR 240.17Ad-22(e)(3)(ii).

10 17 CFR 240.17Ad-22(e)(v)(viii).

those arising from its payment, clearing, and settlement processes, including by …[d]escribing the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[11]

- Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively measure, monitor, and manage the liquidity risk that arises in or is borne by the [CCA], including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, doing the following...[d]escribing the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[12]
- Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure 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…"[13]
- Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[14]

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11 17 CFR 240.17Ad-22(e)(4)(ix).

12 17 CFR 240.17Ad-22(e)(7)(ix).

13 17 CFR 240.17Ad-22(e)(13).

14 17 CFR 240.17Ad-22(e)(23)(i).

- Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[15]

OCC meets the definition of a CCA and is therefore subject to the requirements of the CCA rules, including new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).[16]

Proposed Changes

Summary of Proposed Changes

In order to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default, OCC is proposing to make the following revisions to its Rules and By-Laws:

(1) Revise the existing assessment powers in Section 6 of Article VIII of OCC's By-Laws, specifically to:

(a) Establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be

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15 17 CFR 240.17Ad-22(e)(23)(ii).

16 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix) and (e)(7)(ix).

200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge;

(b) Clarify that a Clearing Member that chooses to terminate its membership status during a cooling-off period will not be liable for replenishment of the Clearing Fund immediately following the expiration of such cooling-off period, provided that the withdrawing Clearing Member satisfies enumerated criteria, including providing notice of such termination by no later than the end of the cooling-off period and by closing-out and/or transferring of all its open positions with OCC by no later than the last day of the cooling-off period; and

(c) Delineate between the obligation of a Clearing Member to replenish its contributions to the Clearing Fund and its obligations to meet additional "assessments" that may be levied following a proportionate charge to the Clearing Fund.

(2) Adopt a new Rule 1009 that would provide OCC with discretionary authority to call for voluntary payments from non-defaulting Clearing Members in a circumstance where one or more Clearing Members has already defaulted and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Rule 1009 also would establish that OCC would prioritize compensation of Clearing Members that made voluntary payments from any amounts recovered from the defaulted Clearing Members.

(3) Adopt a new Rule 1111 that would provide authority to:

(a) Allow OCC to call for voluntary tear-ups ("Voluntary Tear-Up," as defined below) of non-defaulting Clearing Member and/or customer positions at

any time following the suspension or default of a Clearing Member, with the scope of any such Voluntary Tear-Ups being determined by the Risk Committee of OCC's Board ("Risk Committee");

(b) Allow OCC's Board to vote to tear-up the "Remaining Open Positions" (defined below) of a defaulted Clearing Member, as well as any "Related Open Positions" (defined below) in a circumstance where OCC has attempted one or more auctions of such defaulted Clearing Member's remaining open positions and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default with the scope of any such tear-up ("Partial Tear-Up") being determined by the Risk Committee; and

(c) Allow OCC's Board to vote to re-allocate losses, costs and fees imposed upon holders of positions extinguished in a Partial Tear-Up through a special charge levied against remaining non-defaulting Clearing Members.

(4) Revise the descriptions and authorizations in Article VIII of OCC's By-Laws concerning the use of the Clearing Fund to reflect the discretion of OCC to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from a Voluntary Tear-Up or a mandatory tear-up ("Partial Tear-Up," as defined below).

Discussion of Proposed Changes

Each of the proposed revisions to OCC's Rules and By-Laws is described in more detail in the following sub-sections:

1. Proposed Changes to OCC's Assessment Powers

a. Current Assessment Powers

OCC's current assessment powers are described in Section 6 of Article VIII of OCC's By-Laws. Section 6 establishes a general requirement for each Clearing Member to promptly make good any deficiency in its required contribution to the Clearing Fund whenever an amount is paid out of its Clearing Fund contribution (whether by proportionate charge or otherwise).[17] In this regard, a Clearing Member's obligation to replenish the Clearing Fund is not currently subject to any pre-determined limit. Notwithstanding the foregoing, a Clearing Member can limit the amount of its liability for replenishing the Clearing Fund (at an additional 100% of the amount of its then-required Clearing Fund contribution) by winding-down its clearing activities and terminating its status as a Clearing Member. Any Clearing Member seeking to so limit its liability for replenishing the Clearing Fund must: (i) notify OCC in writing not later than the fifth business day after the proportionate charge that it is terminating its status as a Clearing Member, (ii) not initiate any opening purchase or opening writing transaction,

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17 Under Article VIII, Section 6 of OCC's By-Laws, OCC currently has authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund in certain enumerated situations. For example, Section 6 generally provides that if the conditions regarding a Clearing Member default specified in subparagraphs (a)(i) through (vi) of Article VIII, Section 5 of OCC's By-Laws are satisfied, OCC will make good resulting losses or expenses that are suffered by OCC by applying the defaulting Clearing Member's Clearing Fund contribution after first applying other funds available to OCC in the accounts of the Clearing Member. If the sum of the obligations, however, exceeds the total Clearing Fund contribution and other funds of the defaulting Clearing Member available to OCC, then OCC will charge the amount of the remaining deficiency on a proportionate basis against all non-defaulting Clearing Members' required contributions to the Clearing Fund at the time. Section 5(b) of Article VIII of OCC's By-Laws similarly provides for proportionate charges against Clearing Members' contributions to the Clearing Fund when certain conditions are met that involve a failure by a bank or a securities or commodities clearing organization to perform obligations to OCC when they are due.

and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close out or transfer all of its open positions as promptly as practicable after giving notice to OCC. Thus, withdrawal from clearing membership is the only means by which a Clearing Member currently can limit its liability for replenishing the Clearing Fund.

b. Proposed Changes to Assessment Powers

OCC proposes to amend Section 6 of Article VIII of OCC's By-Laws to make three primary modifications regarding its existing authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund. First, the proposal introduces an automatic minimum fifteen calendar day "cooling-off" period that begins when a proportionate charge is assessed by OCC against Clearing Members' Clearing Fund contributions. While the cooling-off period will continue for a minimum of fifteen consecutive calendar days, if one or more of the events described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws occur(s) during that fifteen calendar day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through either (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth day from the date of the proportionate charge that initiated the cooling-off period, whichever is sooner.

During a cooling-off period, each Clearing Member would have its aggregate liability to replenish the Clearing Fund capped at 200% of the Clearing Member's then-required contribution to the Clearing Fund. Once the cooling-off period ends each remaining Clearing Member would be required to replenish the Clearing Fund in the

amount necessary to meet its then-required contribution. Once the cooling-off period ends, any remaining losses or expenses suffered by OCC as a result of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that occurred during such cooling-off period could not be charged against the amounts Clearing Members have contributed to replenish the Clearing Fund upon the expiration of the cooling-off period.[18]

Second, in connection with the cooling-off period, the proposal would extend the time frame within which a Clearing Member may provide a termination notice to OCC to avoid liability for replenishment of the Clearing Fund after the cooling-off period and would modify the obligations of such a terminating Clearing Member for closing-out and transferring its remaining open positions. Specifically, to effectively terminate its status as a Clearing Member and not be liable for replenishing the Clearing Fund after the cooling-off period, a Clearing Member would be required to: (i) notify OCC in writing of its intent to terminate not later than the last day of the cooling-off period, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close-out or transfer all of its open positions by no later than the last day of the cooling-off period. If a Clearing Member fails to satisfy all of these conditions by the end of a given cooling-off period, it would not have completed all of the requirements necessary to terminate its status as a Clearing

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[18] After a cooling-off period has ended, the occurrence of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that results in a proportionate charge against the Clearing Fund would trigger a new cooling off period, and thusly, a cap of 200% of each Clearing Member's then-required contribution would again apply.

Member under Article VIII, Section 6 of OCC's By-Laws and therefore it would remain subject to the obligation to replenish the Clearing Fund after the end of the cooling-off period.

Third, the proposal would clarify the distinction between "replenishment" of the Clearing Fund and a Clearing Member's obligation to answer "assessments." In this context, the term "replenish" (and its variations) shall to refer to a Clearing Member's standing duty, following any proportionate charge against the Clearing Fund, to return its Clearing Fund contribution to the amount required from such Clearing Member for the month in question.[19] The term "assessment" (and its variations) shall refer to the amount, during any cooling-off period, that a Clearing Member would be required to contribute to the Clearing Fund in excess of the amount of the Clearing Member's pre-funded required Clearing Fund contribution.

Proposed Addition of Ability to Request Voluntary Payments

OCC proposes to add new Rule 1009, which will provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[20]

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19 This assumes that the proportionate charge resulted in the Clearing Member's actual Clearing Fund contribution dropping below the amount of its required contribution (*i.e.*, that the Clearing Member did not have excess above its required contribution that was sufficient to cover the amount of the proportionate charge allocated to such Clearing Member).

20 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under new Rule 1009, OCC will initiate a call for voluntary payments by issuing a "Voluntary Payment Notice" inviting all non-defaulting Clearing Members to make payments to the Clearing Fund in addition to any amounts they are otherwise required to contribute pursuant to Rule 1001. The Voluntary Payment Notice would specify the terms applicable to any voluntary payment, including but not limited to, that any voluntary payment may not be withdrawn once made, that no Clearing Member shall be obligated to make a voluntary payment and that OCC shall retain full discretion to accept or reject any voluntary payment. Rule 1009 specifies that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s), OCC would seek to compensate first from such recovery all non-defaulting Clearing Members that made voluntary payments (and if the amount recovered from the defaulted Clearing Member(s) is less than the aggregate amount of voluntary payments, non-defaulting Clearing Members that made voluntary payments each would receive a percentage of the recovery that corresponds to that Clearing Member's percentage of the total amount of voluntary payments received).

Proposed Addition of Ability to Conduct Voluntary Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to voluntarily extinguish (i.e., voluntarily tear-up) their open positions at OCC in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and

2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.

While Risk Committee approval is not needed to commence a voluntary tear-up, the Risk Committee would be responsible for determining the appropriate scope of each voluntary tear-up. To ensure OCC retains sufficient flexibility to effectively deploy this tool in an extreme stress event, proposed Rule 1111(c) is drafted to provide the Risk Committee with discretion to determine the appropriate scope of each voluntary tear-up.[21] New Rule 1111(c) also would impose standards designed to circumscribe the Risk Committee's discretion, requiring that any determination regarding the scope of a voluntary tear-up shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

Once the Risk Committee has determined the scope of the Voluntary Tear-Up, OCC will initiate the call for voluntary tear-ups by issuing a "Voluntary Tear-Up Notice." The Voluntary Tear-Up Notice shall inform all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear-Up.[22] The Voluntary Tear-Up Notice would specify the terms applicable to any voluntary tear-up, including but not limited to, that no Clearing Member or customers of a Clearing Member shall be

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21 Notwithstanding the discretion that would be afforded by the text of proposed Rule 1111(c), OCC anticipates that the scope of voluntary tear-ups likely would be dictated by the cleared contracts remaining in the portfolio(s) of the defaulted Clearing Member(s).

22 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Voluntary Tear-Up of the opportunity to participate in such tear-up.

obligated to participate in a voluntary tear-up and that OCC shall retain full discretion to accept or reject any voluntary tear-up.

OCC is not proposing a tear-up process that would require the imposition of "gains haircutting" (*i.e.*, the reduction of unpaid gains) on a portion of OCC's cleared contracts.[23] Instead, OCC has determined that its tear-up process – for both Voluntary Tear-Ups as well as Partial Tear-Ups – should be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC would be expected to have adequate remaining resources to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.[24]

In OCC's proposed tear-up process, the holders of torn-up positions would be assigned a Tear-Up Price and OCC would draw on its remaining financial resources in order to extinguish the torn-up positions at the assigned Tear-Up Price without forcing a reduction in the amount unpaid gains on such positions. The proposed changes would provide OCC with two separate and non-exclusive means of equitably re-allocating the losses, costs or expenses imposed upon the holders of torn-up positions as a result of the tear-up(s). First, the proposed changes to Article VIII would provide OCC discretion to

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23 In general, forced gains haircutting is a tool that can be more easily applied to products whose gains are settled at least daily, like futures through an exchange of variation margin, and by central counterparties with comparatively large daily settlement flows. Listed options, which constitute the vast majority of the contracts cleared by OCC, do not have daily settlement flows and any attempt to reduce the "unrealized gains" of a listed options contract would require the reduction of the option premium that is embedded within the required margin (such a process would effectively require haircutting the listed option's initial margin).

24 OCC anticipates that it would determine the date on which to initiate Partial Tear-Ups by monitoring its remaining financial resources against the potential exposure of the remaining unauctioned positions from the portfolio(s) of the defaulted Clearing Member(s).

use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from such tear-up(s). Second, Rule 1111(a) would provide that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s) and the amount of such recovery exceeds the amount OCC received in voluntary payments, then non-defaulting Clearing Members and non-defaulting customers that voluntarily tore-up open positions and incurred losses from such tear-ups would be repaid from the amount of the recovery in excess of the amount OCC received in voluntary payments.[25] If the amount recovered is less than the aggregate amount of Voluntary Tear-Up, each non-defaulting Clearing Member and non-defaulting customer that incurred losses from voluntarily torn-up positions would be repaid in an amount proportionate to the percentage of its total amount of losses, costs and fees imposed on Clearing Members or customers as a result of the Voluntary Tear-Ups.

With respect to Voluntary Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

Proposed Addition of Ability to Conduct Partial Tear-Ups

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25 In order to effect re-allocation of the losses, costs or expenses imposed upon the holders of torn-up positions, OCC expects that after it has completed its tear-up process and re-established a matched book, holders of both voluntarily torn-up and mandatorily torn-up positions would be provided with a limited opportunity to re-establish positions in the contracts that were voluntarily or mandatorily extinguished. After the expiration of such period, OCC would seek to collect the information on the losses, costs or expenses that had been imposed on the holders of torn-up positions. Based on the information collected, OCC would determine whether it can reasonably determine the losses, costs and expenses sufficiently to re-allocate such amounts.

OCC proposes to add new Rule 1111, which, in relevant part, will provide the Board with discretion to extinguish the remaining open positions of any defaulted Clearing Member or customer of such defaulted Clearing Member(s) (such positions, "Remaining Open Positions"), as well as any related open positions as necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions (such positions, "Related Open Positions"), in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default (such tear-ups hereinafter collectively referred to as "Partial Tear-Ups"). Like the determination for Voluntary Tear-Ups, the Risk Committee shall determine the appropriate scope of each Partial Tear-Up and such determination shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants. Once the Risk Committee has determined the scope of the Partial Tear-Up, OCC will initiate the Partial Tear-Up process by issuing a "Partial Tear-Up Notice." The Partial Tear-Up Notice shall (i) identify the Remaining Open Positions and Related Open Positions designated for tear-up, (ii) identify the open positions of non-defaulting Clearing Members and non-defaulting customers that will be subject to Partial Tear-Up (such positions, "Tear-Up Positions"), (iii) specify the termination price ("Partial Tear-Up Price") for each position to be torn-up, and (iv) list the date and time as of which the Partial Tear-Up will occur.[26]

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[26] Since OCC does not know the identities of Clearing Members' customers, OCC

With regard to the date and time of a Partial Tear-Up, Rule 1111(d) specifies that the Risk Committee shall set the date and time. With regard to the Partial Tear-Up Price, OCC anticipates that it is likely to use the last established end-of-day settlement price, in accordance with its existing practices concerning pricing and valuation. However, given that it is not possible to know in advance the precise circumstances that would cause OCC to conduct a tear-up, Rule 1111(f) has been drafted to allow OCC to exercise reasonable discretion, if necessary, in establishing the Partial Tear-Up Price by some means other than its existing practices concerning pricing and valuation. Specifically, Rule 1111(f) would require that OCC, in exercising any such discretion, would act in good faith and in a commercially reasonable manner to adopt methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models that use the market price of the underlying interest or the market prices of its components. Rule 1111(f) further specifies that OCC may consider the same information set forth in subpart (c) of Section 27, Article VI of OCC's By-Laws.[27]

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would depend on each Clearing Member to notify its customers with positions in scope of the Partial Tear-Up of the possibility of tear-up.

[27] In relevant part, subpart (c) reads as follows: "In determining a close-out amount, the Corporation may consider any information that it deems relevant, including, but not limited to, any of the following: (1) prices for underlying interests in recent transactions, as reported by the market or markets for such interests; (2) quotations from leading dealers in the underlying interest, setting forth the price (which may be a dealing price or an indicative price) that the quoting dealer would charge or pay for a specified quantity of the underlying interest; (3) relevant historical and current market data for the relevant market, provided by reputable outside sources or generated internally; and (4) values derived from theoretical pricing models using available prices for the underlying interest or a related interest and other relevant data. Amounts stated in a currency other than

The scope of any Partial Tear-Up will be determined in accordance with Rule 1111(e). With respect to the extinguishment of Remaining Open Positions, OCC will designate Tear-Up Positions in identical Cleared Contracts and Cleared Securities on the opposite side of the market and in an aggregate amount equal to that of the Remaining Open Positions. OCC will only designate Tear-Up Positions in the accounts of non-defaulting Clearing Members (inclusive of such Clearing Members' customer accounts) with an open position in the applicable Cleared Contract or Cleared Security and of non-defaulted customers of a defaulted Clearing Member. Tear-Up Positions shall be designated and applied by OCC on a pro rata basis across all the identical positions in Cleared Contracts and Cleared Securities on the opposite side of the market in the accounts of non-defaulted Clearing Members and non-defaulted customers (including the non-defaulted customers of defaulted Clearing Members).

Rule 1111(e)(iii) provides that every Partial Tear-Up position is automatically terminated upon and with effect from the Partial Tear-Up Time, without the need for any further step by any party to such Cleared Contract or Cleared Security, and that upon termination, either OCC or the relevant Clearing Member (as the case may be) shall be obligated to pay the other the applicable Partial Tear-Up Price. Rule 1111(e)(iii) further provides that the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.

Rule 1111(g) provides that to the extent losses imposed upon non-defaulting Clearing Members and non-defaulting customers resulting from a Partial Tear-Up can

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U.S. Dollars shall be converted to U.S. Dollars at the current rate of exchange, as determined by the Corporation. A position having a positive close-out value shall be an 'asset position' and a position having a negative close-out value shall be a 'liability position.'"

reasonably be determined, the Board may elect to re-allocate such losses among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.[28]

With respect to Partial Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

2. Statutory Basis

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934 ("Act"),[29] requires, among other things, that the rules of a clearing agency be designed to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest. OCC believes that the proposed rule change is consistent with the requirements of Section 17A(b)(3)(F) of the Act[30] and the rules thereunder applicable to OCC for the reasons set forth below.

As stated above, each of the changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario. In

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28 For the avoidance of doubt, the special charge would be distinct and separate from a Clearing Member's obligation to satisfy Clearing Fund assessments, and therefore, would not be subject to the aforementioned assessment cap in the amount of 200% of a Clearing Member's then-required contribution to the Clearing Fund.

29 15 U.S.C. 78q-1(b)(3)(F).

30 Id.

this regard, the proposed changes are designed to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to establish tools to enable OCC to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC's process in crafting the proposed changes was informed by published guidance from OCC's primary regulators (the Commission and the Commodity Futures Trading Commission), the publications of key international organizations (including the Bank for International Settlements, the International Organization of Securities Commissions and the Financial Stability Board) and the publications of key industry trade organizations. OCC's proposal was further informed by conversations with, among others, OCC's Board, OCC's Risk Committee, Clearing Members and market participants.

Informed by these perspectives, OCC has crafted the proposed changes with the aim of enhancing its ability to address an unprecedented loss event but also, to the extent possible, providing a reasonable amount of certainty to Clearing Members, customers and other stakeholders about the potential consequences of such an event and the resources and tools that would be expected to be available to OCC in support of its clearing operations.[31] Accordingly, the proposed changes should leave Clearing Members, customers and other stakeholders in a position to better evaluate the risks and benefits of clearing in order to facilitate their own risk management, and to the extent applicable, their own regulatory and capital considerations. The proposed changes also seek to avoid

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[31] OCC notes that the very nature of an extreme stress and unprecedented loss event means that its impact is difficult to predict and quantify in advance.

a result that would force only particular clearing participants to shoulder certain losses in an extreme stress scenario (*i.e.*, holders of positions extinguished in Partial Tear-Ups),[32] and instead leaves OCC and its Board with discretionary tools that could provide a more equitable method of allocating the losses from such an event more broadly, consistent with the general principle of mutualized loss that upon which central clearing rests. In this regard, OCC believes the proposed changes foster cooperation and coordination with participants in the clearing system, consistent with Section 17A(b)(3)(F) of the Act.[33]

As stated above, the proposed changes are designed to enable OCC to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC believes that the proposed changes will facilitate its ability to fully allocate, and ultimately extinguish, the loss so that it has a better opportunity of withstanding an extreme stress scenario without sacrificing its viability as a going concern or its ability to continue to provide its critical clearing services. In this regard, OCC believes that the proposed changes remove impediments to and perfect the mechanism of a national system for the prompt and

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32 Absent a means of re-allocating the potential losses, costs and fees imposed upon holders of positions extinguished during tear-ups, the holders of such positions would be left to individually address such losses, costs and fees.

33 15 U.S.C. 78q-1(b)(3)(F).

accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.[34]

The proposed changes are designed to enhance the stability of the clearing system generally and are aimed at ensuring that OCC has adequate tools and resources to better protect market participants from the risks of extreme stress scenarios and unprecedented loss events. In this regard, OCC believes that the proposed changes are reasonably designed to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.[35]

The proposed changes also are designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules discussed immediately below:

Recovery and Orderly Wind-Down

In relevant part, Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…plan[] for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[36] As stated above, each of the proposed changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario.[37] Consistent with the requirements of Rule 17Ad-22(e)(3)(ii), the proposed tools would

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34 Id.

35 Id.

36 17 CFR 240.17Ad-22(e)(3)(ii).

37 Indeed, the OCC's separately filed recovery and orderly wind-down plan identifies OCC's assessment powers, ability to call for voluntary payments, ability to call for Voluntary Tear-Ups and ability to impose Partial Tear-Ups among its "Recovery Tools." OCC has filed a proposed rule change with the Commission in connection with this proposal. See SR-OCC-2017-021.

enable OCC to better address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and, if necessary, to ultimately re-establish a matched book in a recovery or orderly wind-down scenario.[38] In this context, the proposed changes serve as a critical component of OCC's recovery and orderly wind-down plan. As a result, in OCC's view, the proposed changes are consistent with the requirements of Rule 17Ad-22(e)(3)(ii) as to the recovery and orderly wind-down plan.[39]

Allocation of Credit Losses Above Available Resources

In relevant part, Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to …[a]ddress[] allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures…"[40] The proposed changes would provide OCC with three distinct tools that could be used to allocate any credit losses OCC may face in excess of collateral and other resources available to OCC. First, new Rule 1009 would provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[41] OCC may not have sufficient

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38 17 CFR 240.17Ad-22(e)(3)(ii).

39 17 CFR 240.17Ad-22(e)(3)(ii).

40 17 CFR 240.17Ad-22(e)(v)(viii).

41 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

resources to satisfy its obligations and liabilities resulting from such default. Second, new Rule 1111 would establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to participate in Voluntarily Tear-Ups in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Finally, new Rule 1111 also would provide the Board with discretion to mandatorily tear-up Remaining Open Positions and Related Open Positions, in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[42] In OCC's view, each of these tools could be deployed by OCC, if necessary, to allocate credit losses in excess of the collateral and other resources available to OCC, in accordance with Rule 17Ad-22(e)(4)(viii).[43]

Replenishment of Financial Resources Following a Default

In relevant part, Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed

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42 Rule 1111(g), which would provide the Board authority to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge, would serve as a discretionary tool to redistribute the credit losses allocated through Partial Tear-Up.

43 17 CFR 240.17Ad-22(e)(v)(viii).

to…[d]escrib[e] the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[44] OCC's Clearing Members have a standing obligation to replenish the Clearing Fund following any proportionate charge. The proposed changes would establish a rolling cooling-off period, triggered by the payment of a proportionate charge against the Clearing Fund, during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge. Compared to the current requirement under which a Clearing Member may cap its liability to proportionate charges at an additional 100% of its then-required contribution, a Clearing Member would instead be permitted to cap its liability for proportionate charges at an additional 200% of its then-required Clearing Fund contribution.

OCC believes that the proposed approach improves predictability for OCC and for Clearing Members regarding the size of Clearing Fund contributions that are likely to be subject to assessments for proportionate charges. Additionally, replacing the five business day withdrawal period with the withdrawal period commensurate with the cooling-off period (which, as proposed would be a minimum of fifteen calendar days) would give Clearing Members a more reasonable period in which to meet the wind-down and termination requirements necessary to cap their liability. OCC believes that this would afford them greater certainty regarding their maximum liability with respect to the Clearing Fund during extreme stress events, which in turn, facilitates Clearing Members'

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44 17 CFR 240.17Ad-22(e)(4)(ix).

management of their own risk management, and to the extent applicable, regulatory capital considerations. And OCC believes this increased predictability would also be beneficial to OCC by helping it to more reliably understand the amount of Clearing Fund contributions that will likely be available to it after a proportionate charge is assessed.[45]

OCC believes that the relative certainty provided by the proposed cooling-off period and 200% cap on assessments ultimately could reduce the risks of successive or "cascading" defaults, in which the financial demands on remaining non-defaulting Clearing Members to continually replenish OCC's Clearing Fund (and similar guaranty funds at other CCPs to which such Clearing Members might belong) have the effect of further weakening such Clearing Members to the point of default. In this regard, the proposed changes are designed to provide OCC, Clearing Members and other stakeholders with sufficient time to manage the ongoing default(s) without further aggravating the extreme stresses facing market participants.

OCC recognizes that the proposed changes would limit the maximum amount of Clearing Fund resources that could be available to OCC in an extreme stress scenario, which introduces the possibility, however remote, that the proposed 200% cap ultimately could be reached. If during any cooling-off period the amount of aggregate proportionate charges against the Clearing Fund approaches the 200% cap, the amount remaining in the Clearing Fund may no longer be sufficient to comply with the applicable minimum regulatory financial resources requirements in the CCAs. In any such event, OCC's existing authority under Rule 603 would permit OCC to call on participants for additional

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45 Under the existing approach, it is less certain from OCC's standpoint regarding whether Clearing Members would reasonably be able to cap their liability to proportionate charges within five business days.

initial margin, which could ensure that OCC's minimum financial resources remain in excess of applicable CCA requirements.[46] OCC recognizes that the imposition of increased margin requirements could have an immediate pro-cyclical impact on participants (and consequential impacts on the broader financial system) that is potentially greater than the impact of replenishing the Clearing Fund. These risks would be limited to a specific extreme stress event and could be mitigated by certain factors. First, OCC, in coordination with its regulators, would carefully evaluate any potential increase in the context of then-existing facts and circumstances. Second, during the cooling-off period, Clearing Members and their customers will have the opportunity to reduce or rebalance their respective portfolios in order to mitigate their exposures to stress losses and initial margin increases. Finally, since initial margin is not designed to be subject to mutualized loss, the risk of loss faced by Clearing Members for amounts posted as additional margin would be substantially less than for replenishments of the Clearing Fund.

Given the products cleared by OCC and the composition of its clearing membership, OCC has determined that a minimum 15-calendar day cooling-off period, rolling up to a maximum of 20 calendar days, is likely to be a sufficient amount of time for OCC to manage the ongoing default(s) and take necessary steps in furtherance of stabilizing the clearing system. Further, through conversations with Clearing Members, OCC believes that the proposed cooling-off period is likely to be a sufficient amount for

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46 Rule 603 provides that "[t]he Risk Committee may, from time to time, increase the amount of margin which may be required in respect of a cleared contract, open short position or exercised contract if, in its discretion, it determines that such increase is advisable for the protection of [OCC], the Clearing Members or the general public."

Clearing Members (and their customers) to orderly reduce or rebalance their positions, in an attempt to mitigate stress losses and exposure to potential initial margin increases as they navigate the stress event. Through conversations with Clearing Members, OCC also believes that the proposed cooling-off period is likely to be a sufficient amount for certain Clearing Members to orderly close-out their positions and transfer customer positions as they withdraw from clearing membership. OCC believes the proposed cooling-off period, coupled with the other proposed changes to OCC's assessment powers, is likely to provide Clearing Members with an adequate measure of stability and predictability as to the potential use of Clearing Fund resources, which OCC believes removes the existing incentive for Clearing Members to withdraw following a proportionate charge.[47]

In light of the foregoing, OCC believes that the proposed changes would enhance and strengthen its process to replenish the Clearing Fund following a default or other event in which use of the Clearing Fund is contemplated, in accordance with Rule 17Ad-22(e)(4)(ix).[48]

Replenishment of Liquid Resources

In relevant part, Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any liquid resources that the clearing

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47 OCC initially considered a fixed 15-calendar day cooling-off period; however, OCC concluded that a fixed 15-calendar day cooling-off period may increase the risks of successive or cascading Clearing Member defaults and may perversely incentivize Clearing Members to seek to withdraw from clearing membership. Through conversations with Clearing Members, OCC believes that these potentially disruptive consequences are mitigated by the proposed rolling cooling-off period.

48 17 CFR 240.17Ad-22(e)(4)(ix).

agency may employ during a stress event."[49] Since the use any part of the cash portion of OCC's Clearing Fund would constitute a depletion of one of OCC's liquid resources, OCC's assessment power, discussed above, is the primary means of replenishing the Clearing Fund cash that OCC used to address the stress event. For the same reasons stated above, OCC believes that the proposed changes enhance and strengthen its process to replenish the Clearing Fund, as necessary, following a default or other stress event in which the Clearing Fund is used, and therefore, OCC views the proposed changes as consistent with Rule 17Ad-22(e)(7)(ix).[50]

Timely Action to Contain Losses

In relevant part, Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure the [CCA] has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations…"[51] The proposed changes would provide OCC with the authority to call for Voluntary Tear-Ups and OCC's Board with the discretion to impose Partial Tear-Ups, which would provide OCC with authority necessary to extinguish certain losses (and attendant liquidity demands) thereby potentially enabling OCC to continue to meet its remaining obligations to participants. As designed, Voluntary Tear-Ups and Partial Tear-Ups would be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC is expected to have adequate resources remaining to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.

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49 17 CFR 240.17Ad-22(e)(7)(ix).

50 17 CFR 240.17Ad-22(e)(7)(ix).

51 17 CFR 240.17Ad-22(e)(13).

Accordingly, OCC believes that its authority and capacity to conduct a Partial Tear-Up should be timely, relative to the adequacy of OCC's remaining financial resources. Finally, OCC believes it has the operational and systems capacity sufficient to support the proposed changes, and OCC's policies and procedures will be updated accordingly to reflect the existence of these new tools. As a result, OCC believes that the proposed changes conform to the relevant requirements in Rule 17Ad-22(e)(13).[52]

Public Disclosure of Key Aspects of Default Rules

In relevant part, Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[53] As stated above, each of the tools discussed herein are contemplated to be deployed by OCC if an extreme stress event has placed OCC into a recovery or orderly wind-down scenario, and therefore, the tools discussed herein constitute key aspects of OCC's default rules. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that proposed changes would conform to the relevant requirements in Rule 17Ad-22(e)(23)(i).[54]

Sufficient Information Regarding the Risks, Fees and Costs of Clearing

In relevant part, Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the

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52 17 CFR 240.17Ad-22(e)(13).

53 17 CFR 240.17Ad-22(e)(23)(i).

54 17 CFR 240.17Ad-22(e)(13).

risks, fees, and other material costs they incur by participating in the covered clearing agency."[55] The proposed changes would clearly explain to Clearing Members and market participants that an extreme stress scenario could result in the use – and theoretically the exhaustion – of OCC's financial resources, inclusive of OCC's proposed assessment powers. Proposed changes to Section 6, Article VIII of OCC's By-Laws would explain Clearing Members' replenishment obligation and liability for assessments. The proposed changes also would clearly explain, through proposed Rules 1009 and 1111, that as OCC nears the exhaustion of its assessment powers, Clearing Members may be asked for voluntary payments and, if necessary, Clearing Members and customers may be asked to participate in a Voluntary Tear-Up and/or subject to a Partial Tear-Up. Proposed Rules 1009(b) and 1111(a)(ii) also would make clear that Clearing Members that made voluntary payments and Clearing Members and customers whose tendered positions were extinguished in the Voluntary Tear-Up would be prioritized in the distribution of any recovery from the defaulted Clearing Member(s). Proposed changes to Article VIII would clarify that the Clearing Fund contributions remaining after OCC has conducted a Voluntary Tear-Up or Partial Tear-Up could be used to compensate the non-defaulting Clearing Members and non-defaulting customers for the losses, costs or fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up. Proposed Rule 1111(g) would make clear that, following a Partial Tear-Up, OCC's Board may seek to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge. By incorporating the proposed changes into OCC's Rules and By-Laws, as further

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55 17 CFR 240.17Ad-22(e)(23)(ii).

supplemented by the discussion in OCC's public rule filing, OCC believes that is has provided sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they could incur by participating OCC, consistent with the requirements in Rule 17Ad-22(e)(23)(ii).[56]

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

Section 17A(b)(3)(I) of the Act[57] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. OCC does not believe the proposed rule change would have any impact or impose any burden on competition. The primary purpose of the proposed changes is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. As explained above, each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. The proposed rule change is intended to provide Clearing Members, market participants and other stakeholders with greater certainty as to their liabilities and potential exposure to OCC in the event of an unprecedented loss scenario. OCC does not believe that the proposed changes would discriminatorily impact any Clearing Member's access to OCC's services or unnecessarily disadvantage or favor any particular user in relationship to another user. OCC recognizes that the nature of a Partial Tear-Up means that only particular Clearing

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56 17 CFR 240.17Ad-22(e)(23)(ii).

57 15 U.S.C. 78q-1(b)(3)(I).

Members and market participants holding certain positions may be impacted; however, the risk of Partial Tear-Ups is extremely remote, and even then, the proposed changes seek to provide means of equitably re-allocating the losses, costs and fees imposed by Voluntary Tear-Up or Partial Tear-Up. Therefore, OCC believes that the proposed changes would not 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

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 e-mail to rule-comments@sec.gov. Please include File Number SR-OCC-2017-020 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2017-020. 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, N.E., 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 https://www.theocc.com/about/publications/bylaws.jsp.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal or identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-OCC-2017-020 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.[58]

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:_____

58 17 CFR 200.30-3(a)(12).

EXHIBIT 5A

Underlined text indicates new text
~~Strikethrough~~ text indicates deleted text

THE OPTIONS CLEARING CORPORATION

* * *

BY-LAWS

* * *

Article VIII - Clearing Fund

* * *

By-Laws, Article VIII – Purpose and Use of Clearing Fund

Maintenance and Purpose of the Clearing Fund
SECTION 1. (a) The Corporation shall maintain a Clearing Fund to which each Clearing Member shall contribute, as provided in this Article VIII, to make good losses suffered by the Corporation, or losses suffered by the Clearing Fund resulting from borrowings pursuant to the authority in Section 5(e) of this Article, (i) as a result of the failure of any Clearing Member to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation, (ii) as a result of the failure of any Clearing Member (including any Appointed Clearing Member) or of CDS to perform its obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued, undertaken, or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable, (iii) as a result of the failure of any Clearing Member to perform any of its obligations to the Corporation in respect of the stock loan and borrow positions of such Clearing Member, (iv) in connection with any liquidation of a Clearing Member's open positions, (v) in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, (vi) as a result of the failure of any Clearing Member to make any other required payment or render any other required performance, or (vii) as a result of the failure of any bank or securities or commodities clearing organization to perform its obligations to the Corporation for reasons specified in Section 5 of this Article, or (viii) as a result of a borrowing by the Corporation for liquidity needs for same day settlement pursuant to the authority in Section 5(e) of this Article. Notwithstanding the foregoing, in the event that the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rule 1111, the Clearing Fund may be used to provide compensation to non-defaulting Clearing Members and their customers as a means of re-allocating the losses, costs

and fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up, but only to the extent that such losses, costs and fees can be reasonably determined by the Corporation.

* * *

Application of the Clearing Fund
SECTION 5. (a) If:

(i) any Clearing Member shall fail to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation,
(ii) any Clearing Member, (including any Appointed Clearing Member) or of CDS shall fail to perform any obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable,
(iii) any Clearing Member shall fail to perform any obligation to the Corporation in respect of the stock loan and borrow positions of such Clearing Member,
(iv) the Corporation shall suffer any loss or expense upon any liquidation of a Clearing Member's open positions,
(v) the Corporation shall suffer any loss or expense in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, or
(vi) any Clearing Member shall fail to make any other payment or render any other performance required under the By-Laws or the Rules,

then the Corporation shall (after appropriate application of other funds in the accounts of the Clearing Member) apply the Clearing Member's Clearing Fund contribution to the discharge of such obligation, the reimbursement of such loss or expense, or the making of such payment or the funding of such performance. If the sum of all such obligations, losses or expenses, and payments exceeds the sum of the amount of the Clearing Member's total Clearing Fund contribution and the amount of the other funds of the Clearing Member available to the Corporation, and if the Clearing Member fails to pay the Corporation the amount of any such deficiency on demand, the amount of the deficiency shall be paid out of the Clearing Fund and charged on a proportionate basis against all other Clearing Members' computed contributions as fixed at the time, but the Clearing Member who failed to pay the deficiency shall remain liable to the Corporation for the full amount of such deficiency until repayment thereof by such Clearing Member, or

(vii) the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rue 1111,

then, the Corporation may elect to proportionately charge the Clearing Fund in the amount(s) the Corporation reasonably determines necessary to compensate non-

defaulting Clearing Members and their customers for the losses, costs or fees imposed upon them as a directly result of such Voluntary Tear-Up or Partial Tear-Up, but only to the extent that such losses, costs and fees can be reasonably determined by the Corporation.

* * *

Making Good of Charges to the Clearing Fund
SECTION 6.

* * *

(a) *Making Good of Charges to the Clearing Fund.* Whenever an amount is paid out of the Clearing Fund contribution of a Clearing Member, whether by proportionate charge or otherwise, such Clearing Member shall be liable to promptly make good the deficiency in its required contribution resulting from such payment by replenishment of the Clearing Fund. ~~Notwithstanding the foregoing and except as provided for below, if the payment is made as a result of a proportionate charge, a Clearing Member will not be liable to make good more than an additional 100% of the amount of its then required contribution if (i) within five business days following such proportionate charge the Clearing Member notifies the Corporation in writing that it is terminating its status as a Clearing Member, (ii) no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case as promptly as practicable after the giving of such notice; provided that a Clearing Member which so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with the preceding sentence, and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.~~ Each Clearing Member shall have and shall at all times maintain the ability to ~~make good~~ replenish any deficiency described in this Section 6(a) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(b) *Cooling-Off Period; Assessments.* Notwithstanding anything in Section 6 and except as provided for below, if an amount is paid out of the Clearing Fund as a result of a proportionate charge resulting from any of the events described in clauses (i) through (iv) of Section 5(a), then starting on the date of such proportionate charge there shall automatically commence a cooling-off period during which a Clearing Member will not be liable to make good more than an

additional 200% of the amount of its then required contribution (for definitional purposes, amounts in excess of a Clearing Member's then required contribution shall be "assessments"). The cooling-off period shall be fifteen consecutive calendar days from the date of such proportionate charge; provided however, that if one or more subsequent events described in clauses (i) through (iv) of Section 5(a) occur during the fifteen-day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth calendar day from the date of the initial proportionate charge, whichever is sooner. After the cooling-off period ends, Clearing Members shall not be liable for any deficiency arising from losses or expenses suffered by the Corporation as a result of any event described in clauses (i) through (iv) of Section 5(a) that occurred during the cooling-off period. Each Clearing Member shall have and shall at all times maintain the ability to make good any deficiency described in this Section 6(b) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(c) *Termination During Cooling-Off Period.* After the expiration of the cooling-off period, a Clearing Member will not be liable for replenishment of the Clearing Fund as required by Section 6(a) or assessments as contemplated by Section 6(b), if (i) not later than the last day of the cooling-off period the Clearing Member notifies the Secretary of the Corporation in writing that it is terminating its status as a Clearing Member, (ii) after giving such notice no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case not later than the last day of the cooling off period. A Clearing Member that so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with this Section 6(c), and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.

EXHIBIT 5B

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~~Strikethrough~~ text indicates deleted text

THE OPTIONS CLEARING CORPORATION

RULES

* * *

CHAPTER X
Clearing Fund Contributions

* * *

[RESERVED: RULES 1005 – 1008]

RULE 1009 – Voluntary Payments

(a) Where, after the default of a Clearing Member, the Corporation determines that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1104 through 1107, 2210 and 2211, the Corporation does not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Corporation will issue a notice (a "**Voluntary Payment Notice**") inviting all non-defaulting Clearing Members to make a payment to the Clearing Fund in addition to amounts required under Rule 1001 (a "Voluntary Payment") to make up for the relevant shortfall. Terms for Voluntary Payments shall be set forth in the Voluntary Payment Notice and shall include, without limitation, the following:

(i) no Clearing Member shall be obliged to make a Voluntary Payment;

(ii) no Voluntary Payment may be withdrawn once made; and

(iii) the Corporation shall have full discretion whether or not to accept a particular Voluntary Payment.

(b) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member), the Corporation shall seek to compensate first from any such recovery the non-defaulting Clearing Members that made voluntary payments, in the amount of each such Clearing Member's voluntary payment. If the amount of any such recovery is less than the amount the Corporation received in voluntary payments, then each non-defaulting Clearing Member shall be compensated from the recovery pro rata according to the relative size of its voluntary payment.

* * *

CHAPTER XI
Suspension of a Clearing Member

* * *

RULE 1111 – Voluntary Tear-Ups and Partial Tear Ups

(a) (i) The Corporation may notify Clearing Members and provide an opportunity for Clearing Members to voluntarily agree to have positions of a Clearing Member or, with the consent of customers of such Clearing Member, to agree to have each such customer's position, extinguished by the Corporation (a "**Voluntary Tear Up**") at any time following the suspension or default of a Clearing Member and after the Corporation has attempted one or more auctions pursuant to Rule 1104 or Rule 1106, and after the Corporation has determined that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1009, 1104 through 1107, 2210 and 2211 the Corporation does not have sufficient resources to satisfy its obligations and liabilities as a result of such default,. The Corporation will issue a notice (a "**Voluntary Tear Up Notice**") informing all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear Up. Terms for Voluntary Tear Ups shall be set forth in the Voluntary Tear Up Notice and shall include, without limitation, the following:

(x) no Clearing Member, or customers of a Clearing Member, shall be obliged to participate in a Voluntary Tear Up; and

(y) the Corporation shall have full discretion whether or not to accept a particular Voluntary Tear Up offer.

(ii) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) and the amount of such recovery exceeds the amount the Corporation received in voluntary payments, the Corporation shall compensate from such remaining amounts of the recovery the non-defaulting Clearing Members and non-defaulting customers that voluntarily extinguished open positions in the amount of losses, costs or fees directly resulting from the Voluntary Tear-Up, but only after the Corporation has fully compensated non-defaulting Clearing Members that made voluntary payments in the amount of such voluntary payments and only to the extent that such losses, costs and fees can reasonably be determined by the Corporation. If the remaining amount of any such recovery is less than the amount of losses, costs and fees incurred by non-defaulting Clearing Members and non-defaulting customers participated in the Voluntary Tear-Up, then each such non-defaulting Clearing Member and non-defaulting customer shall be compensated pro rata according to the relative size of its incurred losses, costs and fees from the Voluntary Tear-Ups.

(b) If Clearing Member or customer positions of a defaulted Clearing Member remain open ("**Remaining Open Positions**") after the Corporation has attempted one or more auctions

pursuant to Rule 1104 or Rule 1106 and after the Corporation has accounted for any positions voluntary extinguished in accordance with subparagraph (a), and the Corporation determines that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1009, 1104 through 1107, 2210 and 2211, the Corporation does not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Board of Directors of the Corporation may elect to extinguish (i) the Remaining Open Positions, and/or (ii) any related open positions deemed necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions ("**Related Open Positions**"), through a partial tear-up process ("**Partial Tear Up**"). The Corporation will notify the staff of the SEC and the CFTC of a determination that Partial Tear-Up will apply.

(c) The Risk Committee shall determine the appropriate scope of each Voluntary Tear Up under subpart (a) of this Rule and Partial Tear Up under subpart (b) of this Rule. Each determination of the Risk Committee made for purposes of this Rule 1111 shall (i) be based upon then-existing facts and circumstances, (ii) be in furtherance of the integrity of the Corporation and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

(d) For a Partial Tear Up under subpart (b) of this Rule, the Corporation will issue a notice (a "**Partial Tear-Up Notice**") identifying:

(i) The Remaining Open Positions and any Related Open Positions;

(ii) With respect to each other Clearing Member, the open positions of such Clearing Member and its customers (if any) that will be subject to Partial Tear-Up (the "**Tear-Up Positions**");

(iii) The termination price (the "**Partial Tear-Up Price**") for each Tear-Up Position; and

(iv) The date and time as of which Partial Tear-Up will occur, as determined by the Risk Committee (the "**Partial Tear-Up Time**").

(e) For a Partial Tear Up under subpart (b) of this Rule, the Corporation will determine and designate the Tear-Up Positions pursuant to the following methodology:

(i) With respect to Remaining Open Positions, the Corporation will designate Tear-Up Positions in the identical Cleared Contracts and Cleared Securities (on the opposite side of the market) and in an aggregate amount equal to that of the Remaining Open Positions. The Corporation will designate Tear-Up Positions in a particular Cleared Contract or Cleared Security only for non-defaulted Clearing Members that have an open position in such Cleared Contract or Cleared Security, whether for their Clearing Member accounts and/or customer accounts, and for non-defaulted customers of a defaulted Clearing Member, as follows: the Corporation shall designate Tear-Up Positions in the non-defaulted Clearing Member accounts and non-defaulted customer accounts with open positions in the relevant Cleared Contracts and Cleared Securities in such accounts, on a pro rata basis (provided that solely to the extent such pro rata determination would result in creation of a Tear-Up Position which is a fraction of a Cleared Contract or Cleared Security, the Corporation will reallocate such fractional position among

non-defaulted Clearing Members on a random basis to avoid such result). With respect to a Tear-Up Position designated in a non-defaulted customer account of a Clearing Member (including, without limitation, a non-defaulted customer account of a defaulted Clearing Member), the Tear-Up Position shall be allocated on a pro rata basis across any customers that have open positions in such Cleared Contract or Cleared Security in such account. Where the Corporation has in effect one or more hedging transactions related to the Remaining Open Positions which hedging transactions will not themselves be subject to Partial Tear-Up, the Corporation may offer to assign or transfer such hedging transactions with related Tear-Up Positions, on such basis as the Corporation may reasonably determine.

(ii) With respect to Related Open Positions, a Partial Tear-Up would involve extinguishment of all open positions in those Cleared Contracts and Cleared Securities identified by the Risk Committee as within the appropriate scope of the Partial Tear-Up pursuant to this Rule 1111.

(iii) Upon and with effect from the Partial Tear-Up Time, every Tear-Up Position shall be automatically terminated at the Partial Tear-Up Price, without the need for any further step by any party to such Cleared Contract or Cleared Security. Upon such termination, either the Corporation or the relevant Clearing Member, as the case may be, shall be obligated to pay to the other the applicable Partial Tear-Up Price. Upon the termination of a Tear-Up Position, the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.

(f) For a Partial Tear Up under subpart (b) of this Rule, in determining the Partial Tear-Up Price for each Tear-Up Position, the Corporation shall exercise its discretion, acting in good faith and in a commercially reasonable manner, in adopting methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models to determine a value for a cleared contract based on the market price of the underlying interest or the market prices of its components. In determining a Partial Tear-Up Price, the Corporation may consider the same information set forth in subpart (c) of Section 27, Article VI of the By-Laws for determining a close-out amount.

(g) Notwithstanding any provision of this Rule 1111, to the extent that the losses, costs and fees imposed upon non-defaulting Clearing Members and their customers directly resulting from a Partial Tear-Up reasonably can be determined by the Corporation, the Board of Directors may elect to re-allocate such losses, costs and fees among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.

(h) No action or omission by the Corporation pursuant to and in accordance with this Rule 1111 shall constitute a default by the Corporation.

OMB APPROVAL
OMB Number: 3235-0045 Estimated average burden hours per response.....38

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 113

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2017 - * 020
Amendment No. (req. for Amendments *) 2

Filing by Options Clearing Corporation

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

Initial * ☐ Amendment * ☑ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

- 19b-4(f)(1)
- 19b-4(f)(2)
- 19b-4(f)(3)
- 19b-4(f)(4)
- 19b-4(f)(5)
- 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document

Exhibit 3 Sent As Paper Document

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Justin Last Name * Byrne

Title * Vice President, Regulatory Filings

E-mail * jbyrne@theocc.com

Telephone * (202) 971-7238 Fax (312) 322-6280

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 07/12/2018

By Justin W. Byrne

(Name *)

(Title *)

Vice President, Regulatory Filings

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Justin Byrne, jbyrne@theocc.com

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information *

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

Add Remove View

Exhibit Sent As Paper Document

☐

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

Add Remove View

Exhibit Sent As Paper Document

☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

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") would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. This Amendment No. 2 supersedes and replaces the original filing and Amendment No. 1 in their entirety.[1]

The proposed revisions to OCC's By-Laws and Rules are attached hereto as Exhibits 5A and 5B, and the proposed changes to OCC's Default Management Policy are included as confidential Exhibit 5C. Material proposed to be added to OCC's By-Laws, Rules, and Default Management Policy is marked by underlining and material proposed to be deleted is marked by strikethrough text. OCC also has attached as Exhibits 4A and 4B the proposed amendments to the rule text in Exhibits 5A and 5B of the Initial Filing, respectively. Material proposed to be

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[1] On December 18, 2017, OCC filed a proposed rule change that would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. See Securities Exchange Act Release No. 82351 (December 19, 2017), 82 FR 61107 (December 26, 2017) (SR-OCC-2017-020) (hereinafter referred to as the "Initial Filing"). On March 22, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change. See Securities Exchange Act Release No. 82926 (March 22, 2018), 83 FR 13171 (March 27, 2018) (SR-OCC-2017-020). On July 11, 2018, OCC filed Amendment No. 1 to SR-OCC-2017-020, which was intended to supersede the Initial Filing in its entirety. OCC is now filing this Amendment No. 2 to correct certain inadvertent omissions from the Form 19b-4 and Exhibit 1A of Amendment No. 1. Substantive changes to the Initial Filing are described in Item 3 below.

added to the proposed rule text in the Initial Filing is marked by double underlining and material proposed to be deleted is marked by double strikethrough text.

The proposed changes are described in detail in Item 3, below. All terms with initial capitalization not defined here have the same meaning set forth in OCC's By-Laws and Rules.[2]

Item 2. Procedures of the Self-Regulatory Organization

The proposed rule changes were approved for filing with the Commission by OCC's Board of Directors ("Board") at meetings held on April 4, 2017 and July 12, 2017.

Questions should be addressed to Daniel S. Konar II, Vice President, Associate General Counsel, at (321) 322-2020.

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

A. Purpose

Background

The purpose of this proposed rule change is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. Each of the proposed revisions also is designed to further OCC's

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[2] OCC's By-Laws and Rules can be found on OCC's public website: http://optionsclearing.com/about/publications/bylaws.jsp.

compliance, in whole or in part, with the provisions of the Commission's rules identified immediately below.

On September 28, 2016, the Commission adopted amendments to Rule 17Ad-22[3] and added new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii)[4] pursuant to Section 17A of the Securities Exchange Act of 1934[5] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Payment, Clearing and Settlement Supervision Act").[6] In relevant part, these new rules collectively require a covered clearing agency ("CCA"), as defined by Rule 17Ad-22(a)(5),[7] to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (1) maintain a risk management framework including plans for recovery and orderly wind-down necessitated by credit losses, liquidity shortfalls, general business risk losses or any other losses, (2) effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing and settlement processes, including by addressing the allocation of credit losses a CCA might face if its collateral and other resources are insufficient to fully cover its credit exposures, (3) effectively identify, measure, monitor and manage credit exposures, including by describing the process to replenish any financial resource that a CCA may use following a default event or other event in which use of such resource is contemplated, (4)

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3 17 CFR 240.17Ad-22.

4 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

5 15 U.S.C. 78q-1.

6 12 U.S.C. 5461 et. seq.

7 17 CFR 240.17Ad-22(a)(5).

effectively identify, measure, monitor and manage liquidity risks that arises or is borne by the CCA by, at a minimum, describing the process for replenishing any liquid resource that a CCA may employ during a stress event, (5) ensure it has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations, (6) publicly disclose relevant rules and material procedures, including key aspects of its default rules and procedures, and (7) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the CCA. The relevant portions of each of these new requirements is restated below:

- Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[m]aintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the [CCA], which…[i]ncludes plans for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[8]
- Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…[a]ddressing allocation of

[8] 17 CFR 240.17Ad-22(e)(3)(ii).

credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures, including the repayment of any funds the [CCA] may borrow from liquidity providers."[9]

- Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by …[d]escribing the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[10]
- Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively measure, monitor, and manage the liquidity risk that arises in or is borne by the [CCA], including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, doing the following...[d]escribing the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[11]
- Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure the covered clearing

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9 17 CFR 240.17Ad-22(e)(v)(viii).

10 17 CFR 240.17Ad-22(e)(4)(ix).

11 17 CFR 240.17Ad-22(e)(7)(ix).

agency has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations…"[12]

- Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[13]
- Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[14]

OCC meets the definition of a CCA and is therefore subject to the requirements of the CCA rules, including new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).[15]

Proposed Changes

Summary of Proposed Changes

In order to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book

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12 17 CFR 240.17Ad-22(e)(13).

13 17 CFR 240.17Ad-22(e)(23)(i).

14 17 CFR 240.17Ad-22(e)(23)(ii).

15 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix) and (e)(7)(ix).

following a default, OCC is proposing to make the following revisions to its Rules and By-Laws:

(1) Revise the existing assessment powers in Section 6 of Article VIII of OCC's By-Laws, specifically to:

(a) Establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge;

(b) Clarify that a Clearing Member that chooses to terminate its membership status during a cooling-off period will not be liable for replenishment of the Clearing Fund immediately following the expiration of such cooling-off period, provided that the withdrawing Clearing Member satisfies enumerated criteria, including providing notice of such termination by no later than the end of the cooling-off period and by closing-out and/or transferring of all its open positions with OCC by no later than the last day of the cooling-off period; and

(c) Delineate between the obligation of a Clearing Member to replenish its contributions to the Clearing Fund and its obligations to meet additional "assessments" that may be levied following a proportionate charge to the Clearing Fund.

(2) Adopt a new Rule 1011[16] that would provide OCC with discretionary authority to call for voluntary payments from non-defaulting Clearing Members in a circumstance where one or more Clearing Members has already defaulted and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[17] Rule 1011 also would establish that OCC would prioritize compensation of Clearing Members that made voluntary payments from any amounts recovered from the defaulted Clearing Members.

(3) Adopt a new Rule 1111 that would provide authority to:

(a) Allow OCC to call for voluntary tear-ups ("Voluntary Tear-Up," as defined below) of non-defaulting Clearing Member and/or customer positions at any time following the suspension or default of a Clearing Member, with the scope of any such Voluntary Tear-Ups being determined by the Risk Committee of OCC's Board ("Risk Committee");

(b) Allow OCC's Board to vote to tear-up the "Remaining Open Positions"

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16 OCC is amending the Initial Filing to renumber proposed Rule 1009 to proposed Rule 1011 and updated related cross references in Rule 1111 to reflect this renumbering. OCC is also amending the Default Management Policy as submitted in the Initial Filing to update similar cross references.

17 Under the Initial Filing, OCC's authority to conduct Partial Tear-Ups, as well as call for voluntary payments or to conduct Voluntary Tear-Ups, would be conditioned in part on OCC having determined that, notwithstanding the availability of any remaining resources, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under the Initial Filing, the proposed text of Rules 1009(a), 1111(a) and 1111(b) incorrectly transcribed this condition to require that OCC determine that, notwithstanding the availability of any remaining resources, OCC *does* not have sufficient resources to satisfy its obligations and liabilities resulting from such default (emphasis added). In each such instance, OCC is amending the proposed text of Rules 1009(a) (which is being renumbered as Rule 1011(a)), 1111(a) and 1111(b) in Exhibit 5B of the Initial Filing to delete the word "does" and insert in its place the word "may."

(defined below) of a defaulted Clearing Member, as well as any "Related Open Positions" (defined below) in a circumstance where OCC has attempted one or more auctions of such defaulted Clearing Member's remaining open positions and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default with the scope of any such tear-up ("Partial Tear-Up") being determined by the Risk Committee; and

(c) Allow OCC's Board to vote to re-allocate losses, costs and fees imposed upon holders of positions extinguished in a Partial Tear-Up through a special charge levied against remaining non-defaulting Clearing Members.

(4) Revise the descriptions and authorizations in Article VIII of OCC's By-Laws concerning the use of the Clearing Fund to reflect the discretion of OCC to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from a Voluntary Tear-Up or a mandatory tear-up ("Partial Tear-Up," as defined below).

Discussion of Proposed Changes

Each of the proposed revisions to OCC's Rules and By-Laws is described in more detail in the following sub-sections:

1. Proposed Changes to OCC's Assessment Powers

a. Current Assessment Powers

OCC's current assessment powers are described in Section 6 of Article VIII of OCC's

By-Laws. Section 6 establishes a general requirement for each Clearing Member to promptly make good any deficiency in its required contribution to the Clearing Fund whenever an amount is paid out of its Clearing Fund contribution (whether by proportionate charge or otherwise).[18] In this regard, a Clearing Member's obligation to replenish the Clearing Fund is not currently subject to any pre-determined limit. Notwithstanding the foregoing, a Clearing Member can limit the amount of its liability for replenishing the Clearing Fund (at an additional 100% of the amount of its then-required Clearing Fund contribution) by winding-down its clearing activities and terminating its status as a Clearing Member. Any Clearing Member seeking to so limit its liability for replenishing the Clearing Fund must: (i) notify OCC in writing not later than the fifth business day after the proportionate charge that it is terminating its status as a Clearing Member, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close out or transfer all of its open positions as

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[18] Under Article VIII, Section 6 of OCC's By-Laws, OCC currently has authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund in certain enumerated situations. For example, Section 6 generally provides that if the conditions regarding a Clearing Member default specified in subparagraphs (a)(i) through (vi) of Article VIII, Section 5 of OCC's By-Laws are satisfied, OCC will make good resulting losses or expenses that are suffered by OCC by applying the defaulting Clearing Member's Clearing Fund contribution after first applying other funds available to OCC in the accounts of the Clearing Member. If the sum of the obligations, however, exceeds the total Clearing Fund contribution and other funds of the defaulting Clearing Member available to OCC, then OCC will charge the amount of the remaining deficiency on a proportionate basis against all non-defaulting Clearing Members' required contributions to the Clearing Fund at the time. Section 5(b) of Article VIII of OCC's By-Laws similarly provides for proportionate charges against Clearing Members' contributions to the Clearing Fund when certain conditions are met that involve a failure by a bank or a securities or commodities clearing organization to perform obligations to OCC when they are due.

promptly as practicable after giving notice to OCC. Thus, withdrawal from clearing membership is the only means by which a Clearing Member currently can limit its liability for replenishing the Clearing Fund.

b. Proposed Changes to Assessment Powers

OCC proposes to revise Section 6 of Article VIII of OCC's By-Laws to make three primary modifications regarding its existing authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund. First, the proposal introduces an automatic minimum fifteen calendar day "cooling-off" period that begins when a proportionate charge is assessed by OCC against Clearing Members' Clearing Fund contributions. While the cooling-off period will continue for a minimum of fifteen consecutive calendar days, if one or more of the events described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws occur(s) during that fifteen calendar day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through either (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth day from the date of the proportionate charge that initiated the cooling-off period, whichever is sooner.

During a cooling-off period, each Clearing Member would have its aggregate liability to replenish the Clearing Fund capped at 200% of the Clearing Member's then-required contribution to the Clearing Fund. Once the cooling-off period ends each remaining Clearing Member would be required to replenish the Clearing Fund in the amount necessary to meet its

then-required contribution. Once the cooling-off period ends, any remaining losses or expenses suffered by OCC as a result of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that occurred during such cooling-off period could not be charged against the amounts Clearing Members have contributed to replenish the Clearing Fund upon the expiration of the cooling-off period.[19]

Second, in connection with the cooling-off period, the proposal would extend the time frame within which a Clearing Member may provide a termination notice to OCC to avoid liability for replenishment of the Clearing Fund after the cooling-off period and would modify the obligations of such a terminating Clearing Member for closing-out and transferring its remaining open positions. Specifically, to effectively terminate its status as a Clearing Member and not be liable for replenishing the Clearing Fund after the cooling-off period, a Clearing Member would be required to: (i) notify OCC in writing of its intent to terminate not later than the last day of the cooling-off period, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close-out or transfer all of its open positions by no later than the last day of the cooling-off period. If a Clearing Member fails to satisfy all of these conditions by the end of a given cooling-off period, it would not have completed all of the requirements necessary to terminate its status as a

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[19] After a cooling-off period has ended, the occurrence of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that results in a proportionate charge against the Clearing Fund would trigger a new cooling off period, and thusly, a cap of 200% of each Clearing Member's then-required contribution would again apply.

Clearing Member under Article VIII, Section 6 of OCC's By-Laws and therefore it would remain subject to the obligation to replenish the Clearing Fund after the end of the cooling-off period.

Third, the proposal would clarify the distinction between "replenishment" of the Clearing Fund and a Clearing Member's obligation to answer "assessments." In this context, the term "replenish" (and its variations) shall to refer to a Clearing Member's standing duty, following any proportionate charge against the Clearing Fund, to return its Clearing Fund contribution to the amount required from such Clearing Member for the month in question.[20] The term "assessment" (and its variations) shall refer to the amount, during any cooling-off period, that a Clearing Member would be required to contribute to the Clearing Fund in excess of the amount of the Clearing Member's pre-funded required Clearing Fund contribution.

Proposed Addition of Ability to Request Voluntary Payments

OCC proposes to add new Rule 1011, which will provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[21] OCC may not have sufficient

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[20] This assumes that the proportionate charge resulted in the Clearing Member's actual Clearing Fund contribution dropping below the amount of its required contribution (*i.e.*, that the Clearing Member did not have excess above its required contribution that was sufficient to cover the amount of the proportionate charge allocated to such Clearing Member).

[21] Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member.

resources to satisfy its obligations and liabilities resulting from such default. Under new Rule 1011, OCC will initiate a call for voluntary payments by issuing a "Voluntary Payment Notice" inviting all non-defaulting Clearing Members to make payments to the Clearing Fund in addition to any amounts they are otherwise required to contribute pursuant to Rule 1001. The Voluntary Payment Notice would specify the terms applicable to any voluntary payment, including but not limited to, that any voluntary payment may not be withdrawn once made, that no Clearing Member shall be obligated to make a voluntary payment and that OCC shall retain full discretion to accept or reject any voluntary payment. Rule 1011 specifies that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s), OCC would seek to compensate first from such recovery all non-defaulting Clearing Members that made voluntary payments (and if the amount recovered from the defaulted Clearing Member(s) is less than the aggregate amount of voluntary payments, non-defaulting Clearing Members that made voluntary payments each would receive a percentage of the recovery that corresponds to that Clearing Member's percentage of the total amount of voluntary payments received).

Proposed Addition of Ability to Conduct Voluntary Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to voluntarily extinguish (i.e., voluntarily tear-up) their open

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Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

positions at OCC in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.

While Risk Committee approval is not needed to commence a voluntary tear-up, the Risk Committee would be responsible for determining the appropriate scope of each voluntary tear-up. To ensure OCC retains sufficient flexibility to effectively deploy this tool in an extreme stress event, proposed Rule 1111(c) is drafted to provide the Risk Committee with discretion to determine the appropriate scope of each voluntary tear-up.[22] New Rule 1111(c) also would impose standards designed to circumscribe the Risk Committee's discretion, requiring that any determination regarding the scope of a voluntary tear-up shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

Once the Risk Committee has determined the scope of the Voluntary Tear-Up, OCC will initiate the call for voluntary tear-ups by issuing a "Voluntary Tear-Up Notice." The Voluntary Tear-Up Notice shall inform all non-defaulting Clearing Members of the opportunity to

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22 Notwithstanding the discretion that would be afforded by the text of proposed Rule 1111(c), OCC anticipates that the scope of voluntary tear-ups likely would be dictated by the cleared contracts remaining in the portfolio(s) of the defaulted Clearing Member(s).

participate in a Voluntary Tear-Up.[23] The Voluntary Tear-Up Notice would specify the terms applicable to any voluntary tear-up, including but not limited to, that no Clearing Member or customers of a Clearing Member shall be obligated to participate in a voluntary tear-up and that OCC shall retain full discretion to accept or reject any voluntary tear-up.

OCC is not proposing a tear-up process that would require the imposition of "gains haircutting" (*i.e.*, the reduction of unpaid gains) on a portion of OCC's cleared contracts.[24] Instead, OCC has determined that its tear-up process – for both Voluntary Tear-Ups as well as Partial Tear-Ups – should be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC would be expected to have adequate remaining resources to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.[25]

In OCC's proposed tear-up process, the holders of torn-up positions would be assigned a Tear-Up Price and OCC would draw on its remaining financial resources in order to extinguish

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23 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Voluntary Tear-Up of the opportunity to participate in such tear-up.

24 In general, forced gains haircutting is a tool that can be more easily applied to products whose gains are settled at least daily, like futures through an exchange of variation margin, and by central counterparties with comparatively large daily settlement flows. Listed options, which constitute the vast majority of the contracts cleared by OCC, do not have daily settlement flows and any attempt to reduce the "unrealized gains" of a listed options contract would require the reduction of the option premium that is embedded within the required margin (such a process would effectively require haircutting the listed option's initial margin).

25 OCC anticipates that it would determine the date on which to initiate Partial Tear-Ups by monitoring its remaining financial resources against the potential exposure of the remaining unauctioned positions from the portfolio(s) of the defaulted Clearing Member(s).

the torn-up positions at the assigned Tear-Up Price without forcing a reduction in the amount of unpaid value of such positions. OCC is amending the Initial Filing to clarify that while OCC does not intend, in the first instance, for its tear-up process to serve as a means of loss allocation, circumstances may arise such that, despite best efforts, OCC has inadequate remaining financial resources to extinguish torn-up positions at their assigned Tear-Up Price without forcing a reduction in the amount of unpaid value of such positions (e.g., despite best efforts, market movements not accounted for by monitoring, additional Clearing Member defaults occur immediately preceding a tear-up). In such circumstances, despite best efforts, OCC would use its partial tear-up process as a means of loss allocation.[26]

The proposed changes would provide OCC with two separate and non-exclusive means of equitably re-allocating the losses, costs or expenses imposed upon the holders of torn-up positions as a result of the tear-up(s). First, the proposed changes to Article VIII would provide OCC discretion to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from such tear-up(s). Second, Rule 1111(a) would provide that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s) and the amount of such recovery exceeds the amount OCC received in voluntary payments, then non-defaulting Clearing Members and non-defaulting customers that voluntarily tore-up open positions and incurred losses from such tear-ups would be repaid from the amount of the recovery in excess of the amount OCC received in

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[26] This change does not impact the statutory basis for the proposed rule change.

voluntary payments.[27] If the amount recovered is less than the aggregate amount of Voluntary Tear-Up, each non-defaulting Clearing Member and non-defaulting customer that incurred losses from voluntarily torn-up positions would be repaid in an amount proportionate to the percentage of its total amount of losses, costs and fees imposed on Clearing Members or customers as a result of the Voluntary Tear-Ups.

With respect to Voluntary Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

Proposed Addition of Ability to Conduct Partial Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will provide the Board with discretion to extinguish the remaining open positions of any defaulted Clearing Member or customer of such defaulted Clearing Member(s) (such positions, "Remaining Open Positions"), as well as any related open positions as necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions (such positions, "Related Open Positions"), in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations

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27 In order to effect re-allocation of the losses, costs or expenses imposed upon the holders of torn-up positions, OCC expects that after it has completed its tear-up process and re-established a matched book, holders of both voluntarily torn-up and mandatorily torn-up positions would be provided with a limited opportunity to re-establish positions in the contracts that were voluntarily or mandatorily extinguished. After the expiration of such period, OCC would seek to collect the information on the losses, costs or expenses that had been imposed on the holders of torn-up positions. Based on the information collected, OCC would determine whether it can reasonably determine the losses, costs and expenses sufficiently to re-allocate such amounts.

and liabilities resulting from such default (such tear-ups hereinafter collectively referred to as "Partial Tear-Ups"). Like the determination for Voluntary Tear-Ups, the Risk Committee shall determine the appropriate scope of each Partial Tear-Up and such determination shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants. Once the Risk Committee has determined the scope of the Partial Tear-Up, OCC will initiate the Partial Tear-Up process by issuing a "Partial Tear-Up Notice." The Partial Tear-Up Notice shall (i) identify the Remaining Open Positions and Related Open Positions designated for tear-up, (ii) identify the open positions of non-defaulting Clearing Members and non-defaulting customers that will be subject to Partial Tear-Up (such positions, "Tear-Up Positions"), (iii) specify the termination price ("Partial Tear-Up Price") for each position to be torn-up, and (iv) list the date and time as of which the Partial Tear-Up will occur.[28] With regard to the date and time of a Partial Tear-Up, Rule 1111(d) specifies that the Risk Committee shall set the date and time. With regard to the Partial Tear-Up Price, OCC anticipates that it is likely to use the last established end-of-day settlement price, in accordance with its existing practices concerning pricing and valuation. However, given that it is not possible to know in advance the precise circumstances that would cause OCC to conduct a tear-up, Rule 1111(f) has been drafted to allow OCC to exercise reasonable discretion, if necessary,

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[28] Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Partial Tear-Up of the possibility of tear-up.

in establishing the Partial Tear-Up Price by some means other than its existing practices concerning pricing and valuation.[29] Specifically, Rule 1111(f) would require that OCC, in exercising any such discretion, would act in good faith and in a commercially reasonable manner to adopt methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models that use the market price of the underlying interest or the market prices of its components. Rule 1111(f) further specifies that OCC may consider the same information set forth in subpart (c) of Section 27, Article VI of OCC's By-Laws.[30]

The scope of any Partial Tear-Up will be determined in accordance with Rule 1111(e).[31]

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29 For example, OCC has observed certain rare circumstances in which a closing price for an underlying security of an option may be stale or unavailable. A stale or unavailable closing price could be the result of a halt on trading in the underlying security, or a corporate action resulting in a cash-out or conversion of the underlying security (but that has not yet been finalized), or the result of an ADR whose underlying security is being impacted by certain provisions under foreign laws. OCC would consider the presence of these factors on its end-of-day prices in determining whether use of the discretion that would be afforded under proposed Rule 1111(f) might be warranted.

30 In relevant part, subpart (c) reads as follows: "In determining a close-out amount, the Corporation may consider any information that it deems relevant, including, but not limited to, any of the following: (1) prices for underlying interests in recent transactions, as reported by the market or markets for such interests; (2) quotations from leading dealers in the underlying interest, setting forth the price (which may be a dealing price or an indicative price) that the quoting dealer would charge or pay for a specified quantity of the underlying interest; (3) relevant historical and current market data for the relevant market, provided by reputable outside sources or generated internally; and (4) values derived from theoretical pricing models using available prices for the underlying interest or a related interest and other relevant data. Amounts stated in a currency other than U.S. Dollars shall be converted to U.S. Dollars at the current rate of exchange, as determined by the Corporation. A position having a positive close-out value shall be an 'asset position' and a position having a negative close-out value shall be a 'liability position.'"

31 OCC is amending the Initial Filing to reflect that after further evaluation of its proposed recovery tools and the proposed tear-up process, OCC does not believe there would be a need to assign or transfer any hedging transactions established with relation to tear-up positions. OCC is therefore

With respect to the extinguishment of Remaining Open Positions, OCC will designate Tear-Up Positions in identical Cleared Contracts and Cleared Securities on the opposite side of the market and in an aggregate amount equal to that of the Remaining Open Positions. OCC will only designate Tear-Up Positions in the accounts of non-defaulting Clearing Members (inclusive of such Clearing Members' customer accounts) with an open position in the applicable Cleared Contract or Cleared Security.[32] Tear-Up Positions shall be designated and applied by OCC on a pro rata basis across all the identical positions in Cleared Contracts and Cleared Securities on the opposite side of the market in the accounts of non-defaulted Clearing Members and their customers.[33]

Rule 1111(e)(iii) provides that every Partial Tear-Up position is automatically terminated upon and with effect from the Partial Tear-Up Time, without the need for any further step by any party to such Cleared Contract or Cleared Security, and that upon termination, either OCC or the

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amending the Initial Filing to remove text in proposed Rule 1111(e) concerning proposed authority for OCC to offer to assign or transfer any hedging transactions related to Remaining Open Positions with related Tear-Up Positions. This change does not impact the statutory basis for the proposed rule change.

[32] Since, as stated in the Initial Filing, the objective of Partial Tear-Ups is to extinguish the Remaining Open Positions cleared by the defaulted Clearing Member(s) *or customer of such defaulted Clearing Member(s)* (emphasis added), OCC does not believe there would be a need to designate Tear-Up Positions to the non-defaulted customers of a defaulted Clearing Member. OCC is therefore amending the Initial Filing to remove references to non-defaulted customers of defaulted Clearing Members.

[33] OCC is amending the Initial Filing to clarify that a non-defaulted Clearing Member would be required to allocate the assigned Tear-Up Positions on a pro rata basis across those customers that have open positions in such Cleared Contract or Cleared Security in such account, and for any listed option positions being extinguished, allocation across customer accounts should occur in accordance with such Clearing Member's procedures for allocating exercises and assignments. This change does not impact the statutory basis for the proposed rule change.

relevant Clearing Member (as the case may be) shall be obligated to pay the other the applicable Partial Tear-Up Price. Rule 1111(e)(iii) further provides that the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.[34]

Rule 1111(g) provides that to the extent losses imposed upon non-defaulting Clearing Members and non-defaulting customers resulting from a Partial Tear-Up can reasonably be determined, the Board may elect to re-allocate such losses among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.[35]

With respect to Partial Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

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[34] OCC is amending the Initial Filing and the proposed text of Rule 1111(e)(iii) to clarify that if, in certain circumstances discussed above (see fn. 26 and associated text), OCC, in its discretion, determines that its remaining resources are inadequate to pay the applicable Partial Tear-Up Price for each position being extinguished in the Partial Tear-Up, OCC shall be obligated to pay each relevant Clearing Member a pro rata amount of the applicable Partial Tear-Up Price based on OCC's remaining resources, and the relevant Clearing Member shall have an unsecured claim against the Corporation for the value of the difference between the pro rata amount received and the Partial Tear-Up Price. With regard to amounts recovered from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) Rules 1011(b) and 111(a)(ii) would continue to apply. This change does not impact the statutory basis for the proposed rule change.

[35] For the avoidance of doubt, the special charge would be distinct and separate from a Clearing Member's obligation to satisfy Clearing Fund assessments, and therefore, would not be subject to the aforementioned assessment cap in the amount of 200% of a Clearing Member's then-required contribution to the Clearing Fund.

B. Statutory Basis

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934 ("Act"),[36] requires, among other things, that the rules of a clearing agency be designed to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest. OCC believes that the proposed rule change is consistent with the requirements of Section 17A(b)(3)(F) of the Act[37] and the rules thereunder applicable to OCC for the reasons set forth below.

As stated above, each of the changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario. In this regard, the proposed changes are designed to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to establish tools to enable OCC to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC's process in crafting the proposed changes was informed by published guidance from OCC's primary regulators (the Commission and the Commodity Futures Trading Commission), the publications of key international organizations (including the Bank for International Settlements, the

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36 15 U.S.C. 78q-1(b)(3)(F).

37 Id.

International Organization of Securities Commissions and the Financial Stability Board) and the publications of key industry trade organizations. OCC's proposal was further informed by conversations with, among others, OCC's Board, OCC's Risk Committee, Clearing Members and market participants.

Informed by these perspectives, OCC has crafted the proposed changes with the aim of enhancing its ability to address an unprecedented loss event but also, to the extent possible, providing a reasonable amount of certainty to Clearing Members, customers and other stakeholders about the potential consequences of such an event and the resources and tools that would be expected to be available to OCC in support of its clearing operations.[38] Accordingly, the proposed changes should leave Clearing Members, customers and other stakeholders in a position to better evaluate the risks and benefits of clearing in order to facilitate their own risk management, and to the extent applicable, their own regulatory and capital considerations. The proposed changes also seek to avoid a result that would force only particular clearing participants to shoulder certain losses in an extreme stress scenario (*i.e.*, holders of positions extinguished in Partial Tear-Ups),[39] and instead leaves OCC and its Board with discretionary tools that could provide a more equitable method of allocating the losses from such an event more broadly, consistent with the general principle of mutualized loss that upon which central clearing rests. In

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[38] OCC notes that the very nature of an extreme stress and unprecedented loss event means that its impact is difficult to predict and quantify in advance.

[39] Absent a means of re-allocating the potential losses, costs and fees imposed upon holders of positions extinguished during tear-ups, the holders of such positions would be left to individually address such losses, costs and fees.

this regard, OCC believes the proposed changes foster cooperation and coordination with participants in the clearing system, consistent with Section 17A(b)(3)(F) of the Act.[40]

As stated above, the proposed changes are designed to enable OCC to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC believes that the proposed changes will facilitate its ability to fully allocate, and ultimately extinguish, the loss so that it has a better opportunity of withstanding an extreme stress scenario without sacrificing its viability as a going concern or its ability to continue to provide its critical clearing services. In this regard, OCC believes that the proposed changes remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.[41]

The proposed changes are designed to enhance the stability of the clearing system generally and are aimed at ensuring that OCC has adequate tools and resources to better protect market participants from the risks of extreme stress scenarios and unprecedented loss events. In this regard, OCC believes that the proposed changes are reasonably designed to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.[42]

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40 15 U.S.C. 78q-1(b)(3)(F).

41 Id.

42 Id.

The proposed changes also are designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules discussed immediately below:

Recovery and Orderly Wind-Down

In relevant part, Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…plan[] for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[43] As stated above, each of the proposed changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario.[44] Consistent with the requirements of Rule 17Ad-22(e)(3)(ii), the proposed tools would enable OCC to better address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and, if necessary, to ultimately re-establish a matched book in a recovery or orderly wind-down scenario.[45] In this context, the proposed changes serve as a critical component of OCC's recovery and orderly wind-down plan. As a result, in OCC's view, the proposed changes are

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43 17 CFR 240.17Ad-22(e)(3)(ii).

44 Indeed, the OCC's separately filed recovery and orderly wind-down plan identifies OCC's assessment powers, ability to call for voluntary payments, ability to call for Voluntary Tear-Ups and ability to impose Partial Tear-Ups among its "Recovery Tools." OCC has filed a proposed rule change with the Commission in connection with this proposal. See Securities Exchange Act Release No. 82352 (December 19, 2017), 82 FR 61072 (December 26, 2017) (SR-OCC-2017-021). On March 22, 2018, the U.S. Securities and Exchange Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change. See Securities Exchange Act Release No. 82927 (March 22, 2018), 83 FR 13176 (March 27, 2018) (SR-OCC-2017-021).

45 17 CFR 240.17Ad-22(e)(3)(ii).

consistent with the requirements of Rule 17Ad-22(e)(3)(ii) as to the recovery and orderly wind-down plan.[46]

Allocation of Credit Losses Above Available Resources

In relevant part, Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to …[a]ddress[] allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures…"[47] The proposed changes would provide OCC with three distinct tools that could be used to allocate any credit losses OCC may face in excess of collateral and other resources available to OCC. First, new Rule 1011 would provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[48] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Second, new Rule 1111 would establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to participate in Voluntarily Tear-Ups in a circumstance where a Clearing Member has defaulted

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46 17 CFR 240.17Ad-22(e)(3)(ii).

47 17 CFR 240.17Ad-22(e)(v)(viii).

48 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Finally, new Rule 1111 also would provide the Board with discretion to mandatorily tear-up Remaining Open Positions and Related Open Positions, in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[49] In OCC's view, each of these tools could be deployed by OCC, if necessary, to allocate credit losses in excess of the collateral and other resources available to OCC, in accordance with Rule 17Ad-22(e)(4)(viii).[50]

Replenishment of Financial Resources Following a Default

In relevant part, Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[51] OCC's Clearing Members have a standing obligation to replenish the Clearing Fund following any proportionate charge. The

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49 Rule 1111(g), which would provide the Board authority to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge, would serve as a discretionary tool to redistribute the credit losses allocated through Partial Tear-Up.

50 17 CFR 240.17Ad-22(e)(v)(viii).

51 17 CFR 240.17Ad-22(e)(4)(ix).

proposed changes would establish a rolling cooling-off period, triggered by the payment of a proportionate charge against the Clearing Fund, during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge. Compared to the current requirement under which a Clearing Member may cap its liability to proportionate charges at an additional 100% of its then-required contribution, a Clearing Member would instead be permitted to cap its liability for proportionate charges at an additional 200% of its then-required Clearing Fund contribution.

OCC believes that the proposed approach improves predictability for OCC and for Clearing Members regarding the size of Clearing Fund contributions that are likely to be subject to assessments for proportionate charges. Additionally, replacing the five business day withdrawal period with the withdrawal period commensurate with the cooling-off period (which, as proposed would be a minimum of fifteen calendar days) would give Clearing Members a more reasonable period in which to meet the wind-down and termination requirements necessary to cap their liability. OCC believes that this would afford them greater certainty regarding their maximum liability with respect to the Clearing Fund during extreme stress events, which in turn, facilitates Clearing Members' management of their own risk management, and to the extent applicable, regulatory capital considerations. And OCC believes this increased predictability would also be beneficial to OCC by helping it to more reliably understand the amount of Clearing Fund contributions that will likely be available to it after a proportionate charge is

assessed.[52]

OCC believes that the relative certainty provided by the proposed cooling-off period and 200% cap on assessments ultimately could reduce the risks of successive or "cascading" defaults, in which the financial demands on remaining non-defaulting Clearing Members to continually replenish OCC's Clearing Fund (and similar guaranty funds at other CCPs to which such Clearing Members might belong) have the effect of further weakening such Clearing Members to the point of default. In this regard, the proposed changes are designed to provide OCC, Clearing Members and other stakeholders with sufficient time to manage the ongoing default(s) without further aggravating the extreme stresses facing market participants.

OCC recognizes that the proposed changes would limit the maximum amount of Clearing Fund resources that could be available to OCC in an extreme stress scenario, which introduces the possibility, however remote, that the proposed 200% cap ultimately could be reached. If during any cooling-off period the amount of aggregate proportionate charges against the Clearing Fund approaches the 200% cap, the amount remaining in the Clearing Fund may no longer be sufficient to comply with the applicable minimum regulatory financial resources requirements in the CCAs. In any such event, OCC's existing authority under Rule 603 would permit OCC to call on participants for additional initial margin, which could ensure that OCC's minimum

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[52] Under the existing approach, it is less certain from OCC's standpoint regarding whether Clearing Members would reasonably be able to cap their liability to proportionate charges within five business days.

financial resources remain in excess of applicable CCA requirements.[53] OCC recognizes that the imposition of increased margin requirements could have an immediate pro-cyclical impact on participants (and consequential impacts on the broader financial system) that is potentially greater than the impact of replenishing the Clearing Fund. These risks would be limited to a specific extreme stress event and could be mitigated by certain factors. First, OCC, in coordination with its regulators, would carefully evaluate any potential increase in the context of then-existing facts and circumstances. Second, during the cooling-off period, Clearing Members and their customers will have the opportunity to reduce or rebalance their respective portfolios in order to mitigate their exposures to stress losses and initial margin increases. Finally, since initial margin is not designed to be subject to mutualized loss, the risk of loss faced by Clearing Members for amounts posted as additional margin would be substantially less than for replenishments of the Clearing Fund.

Given the products cleared by OCC and the composition of its clearing membership, OCC has determined that a minimum 15-calendar day cooling-off period, rolling up to a maximum of 20 calendar days, is likely to be a sufficient amount of time for OCC to manage the ongoing default(s) and take necessary steps in furtherance of stabilizing the clearing system. Further, through conversations with Clearing Members, OCC believes that the proposed cooling-off period is likely to be a sufficient amount for Clearing Members (and their customers) to

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53 Rule 603 provides that "[t]he Risk Committee may, from time to time, increase the amount of margin which may be required in respect of a cleared contract, open short position or exercised contract if, in its discretion, it determines that such increase is advisable for the protection of [OCC], the Clearing Members or the general public."

orderly reduce or rebalance their positions, in an attempt to mitigate stress losses and exposure to potential initial margin increases as they navigate the stress event. Through conversations with Clearing Members, OCC also believes that the proposed cooling-off period is likely to be a sufficient amount for certain Clearing Members to orderly close-out their positions and transfer customer positions as they withdraw from clearing membership. OCC believes the proposed cooling-off period, coupled with the other proposed changes to OCC's assessment powers, is likely to provide Clearing Members with an adequate measure of stability and predictability as to the potential use of Clearing Fund resources, which OCC believes removes the existing incentive for Clearing Members to withdraw following a proportionate charge.[54]

In light of the foregoing, OCC believes that the proposed changes would enhance and strengthen its process to replenish the Clearing Fund following a default or other event in which use of the Clearing Fund is contemplated, in accordance with Rule 17Ad-22(e)(4)(ix).[55]

Replenishment of Liquid Resources

In relevant part, Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a

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54 OCC initially considered a fixed 15-calendar day cooling-off period; however, OCC concluded that a fixed 15-calendar day cooling-off period may increase the risks of successive or cascading Clearing Member defaults and may perversely incentivize Clearing Members to seek to withdraw from clearing membership. Through conversations with Clearing Members, OCC believes that these potentially disruptive consequences are mitigated by the proposed rolling cooling-off period.

55 17 CFR 240.17Ad-22(e)(4)(ix).

stress event."[56] Since the use any part of the cash portion of OCC's Clearing Fund would constitute a depletion of one of OCC's liquid resources, OCC's assessment power, discussed above, is the primary means of replenishing the Clearing Fund cash that OCC used to address the stress event. For the same reasons stated above, OCC believes that the proposed changes enhance and strengthen its process to replenish the Clearing Fund, as necessary, following a default or other stress event in which the Clearing Fund is used, and therefore, OCC views the proposed changes as consistent with Rule 17Ad-22(e)(7)(ix).[57]

Timely Action to Contain Losses

In relevant part, Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure the [CCA] has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations…"[58] The proposed changes would provide OCC with the authority to call for Voluntary Tear-Ups and OCC's Board with the discretion to impose Partial Tear-Ups, which would provide OCC with authority necessary to extinguish certain losses (and attendant liquidity demands) thereby potentially enabling OCC to continue to meet its remaining obligations to participants. As designed, Voluntary Tear-Ups and Partial Tear-Ups would be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC is expected to have adequate resources remaining to cover the

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56 17 CFR 240.17Ad-22(e)(7)(ix).

57 17 CFR 240.17Ad-22(e)(7)(ix).

58 17 CFR 240.17Ad-22(e)(13).

amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains. Accordingly, OCC believes that its authority and capacity to conduct a Partial Tear-Up should be timely, relative to the adequacy of OCC's remaining financial resources. Finally, OCC believes it has the operational and systems capacity sufficient to support the proposed changes, and OCC's policies and procedures will be updated accordingly to reflect the existence of these new tools. As a result, OCC believes that the proposed changes conform to the relevant requirements in Rule 17Ad-22(e)(13).[59]

Public Disclosure of Key Aspects of Default Rules

In relevant part, Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[60] As stated above, each of the tools discussed herein are contemplated to be deployed by OCC if an extreme stress event has placed OCC into a recovery or orderly wind-down scenario, and therefore, the tools discussed herein constitute key aspects of OCC's default rules. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that proposed changes would conform to the relevant requirements in Rule 17Ad-22(e)(23)(i).[61]

Sufficient Information Regarding the Risks, Fees and Costs of Clearing

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59 17 CFR 240.17Ad-22(e)(13).

60 17 CFR 240.17Ad-22(e)(23)(i).

61 17 CFR 240.17Ad-22(e)(13).

In relevant part, Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[62] The proposed changes would clearly explain to Clearing Members and market participants that an extreme stress scenario could result in the use – and theoretically the exhaustion – of OCC's financial resources, inclusive of OCC's proposed assessment powers. Proposed changes to Section 6, Article VIII of OCC's By-Laws would explain Clearing Members' replenishment obligation and liability for assessments. The proposed changes also would clearly explain, through proposed Rules 1011 and 1111, that as OCC nears the exhaustion of its assessment powers, Clearing Members may be asked for voluntary payments and, if necessary, Clearing Members and customers may be asked to participate in a Voluntary Tear-Up and/or subject to a Partial Tear-Up. Proposed Rules 1011(b) and 1111(a)(ii) also would make clear that Clearing Members that made voluntary payments and Clearing Members and customers whose tendered positions were extinguished in the Voluntary Tear-Up would be prioritized in the distribution of any recovery from the defaulted Clearing Member(s). Proposed changes to Article VIII would clarify that the Clearing Fund contributions remaining after OCC has conducted a Voluntary Tear-Up or Partial Tear-Up could be used to compensate the non-defaulting Clearing Members and non-defaulting customers for the losses, costs or fees imposed upon them as a result of such Voluntary Tear-Up

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62 17 CFR 240.17Ad-22(e)(23)(ii).

or Partial Tear-Up. Proposed Rule 1111(g) would make clear that, following a Partial Tear-Up, OCC's Board may seek to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that is has provided sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they could incur by participating OCC, consistent with the requirements in Rule 17Ad-22(e)(23)(ii).[63]

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

Section 17A(b)(3)(I) of the Act[64] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. OCC does not believe the proposed rule change would have any impact or impose any burden on competition. The primary purpose of the proposed changes is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. As explained above, each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. The proposed rule change is intended to provide Clearing Members, market participants and other stakeholders with greater certainty as to their

63 17 CFR 240.17Ad-22(e)(23)(ii).

64 15 U.S.C. 78q-1(b)(3)(I).

liabilities and potential exposure to OCC in the event of an unprecedented loss scenario. OCC does not believe that the proposed changes would discriminatorily impact any Clearing Member's access to OCC's services or unnecessarily disadvantage or favor any particular user in relationship to another user. OCC recognizes that the nature of a Partial Tear-Up means that only particular Clearing Members and market participants holding certain positions may be impacted; however, the risk of Partial Tear-Ups is extremely remote, and even then, the proposed changes seek to provide means of equitably re-allocating the losses, costs and fees imposed by Voluntary Tear-Up or Partial Tear-Up. Therefore, OCC believes that the proposed changes would not 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 change and none have been received. OCC will notify the Commission of any written comments received by OCC.

Item 6. Extension of Time Period for Commission Action

Not applicable.

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)

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

(d) Not applicable.

Item 8. Proposed Rule Change Based on Rule 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 Proposed Rule Change for publication in the Federal Register.

Exhibit 4A. Amended text of OCC By-Laws

Exhibit 4B. Amended text of OCC Rules

Exhibit 5A. OCC By-Laws

Exhibit 5B. OCC Rules

Exhibit 5C. Default Management Policy

CONFIDENTIAL TREATMENT IS REQUESTED FOR EXHIBIT 5C

PURSUANT TO SEC RULE 24b-2

SIGNATURES

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

THE OPTIONS CLEARING CORPORATION

By:_____
Daniel S. Konar II
Vice President, Associate General Counsel

EXHIBIT 1A

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-[_____]; File No. SR-OCC-2017-020)

July __, 2018

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of a Proposed Rule Change Concerning Enhanced and New Tools for Recovery Scenarios

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 July 12, 2018, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") Amendment No. 2 to the proposed rule change as described in Items I, II and III below, which Items have been prepared primarily by OCC. This Amendment No. 2 supersedes and replaces the original filing and Amendment No. 1 in their entirety.[3] The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 On December 18, 2017, OCC filed a proposed rule change that would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. See Securities Exchange Act Release No. 82351 (December 19, 2017), 82 FR 61107 (December 26, 2017) (SR-OCC-2017-020) (hereinafter referred to as the "Initial Filing"). On March 22, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change. See Securities Exchange Act Release No. 82926 (March 22, 2018), 83 FR 13171 (March 27, 2018) (SR-OCC-2017-020). On July 11, 2018, OCC filed Amendment No. 1 to SR-OCC-2017-020, which was intended to supersede the Initial Filing in its entirety. OCC is now filing this Amendment No. 2 to correct certain inadvertent omissions from the Form 19b-4 and Exhibit 1A of Amendment No. 1. Substantive changes to the Initial Filing are described in Item II below.

I. Clearing Agency's Statement of the Terms of Substance of the Proposed Rule Change

This proposed rule change by the OCC would make certain revisions to OCC's Rules and By-Laws to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario.

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

Background

The purpose of this proposed rule change is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. Each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC

into a recovery or orderly wind-down scenario. Each of the proposed revisions also is designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules identified immediately below.

On September 28, 2016, the Commission adopted amendments to Rule 17Ad-22[4] and added new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii)[5] pursuant to Section 17A of the Securities Exchange Act of 1934[6] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Payment, Clearing and Settlement Supervision Act").[7] In relevant part, these new rules collectively require a covered clearing agency ("CCA"), as defined by Rule 17Ad-22(a)(5),[8] to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (1) maintain a risk management framework including plans for recovery and orderly wind-down necessitated by credit losses, liquidity shortfalls, general business risk losses or any other losses, (2) effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing and settlement processes, including by addressing the allocation of credit losses a CCA might face if its collateral and other resources are insufficient to fully cover its credit exposures, (3) effectively identify, measure, monitor and manage credit exposures, including by describing the process to replenish any financial resource that a CCA may use following

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4 17 CFR 240.17Ad-22.

5 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).

6 15 U.S.C. 78q-1.

7 12 U.S.C. 5461 et. seq.

8 17 CFR 240.17Ad-22(a)(5).

a default event or other event in which use of such resource is contemplated, (4) effectively identify, measure, monitor and manage liquidity risks that arises or is borne by the CCA by, at a minimum, describing the process for replenishing any liquid resource that a CCA may employ during a stress event, (5) ensure it has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations, (6) publicly disclose relevant rules and material procedures, including key aspects of its default rules and procedures, and (7) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the CCA. The relevant portions of each of these new requirements is restated below:

- Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[m]aintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the [CCA], which…[i]ncludes plans for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[9]
- Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…[a]ddressing allocation of credit losses the [CCA] may face if its collateral

9 17 CFR 240.17Ad-22(e)(3)(ii).

and other resources are insufficient to fully cover its credit exposures, including the repayment of any funds the [CCA] may borrow from liquidity providers."[10]

- Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by …[d]escribing the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[11]
- Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]ffectively measure, monitor, and manage the liquidity risk that arises in or is borne by the [CCA], including measuring, monitoring, and managing its settlement and funding flows on an ongoing and timely basis, and its use of intraday liquidity by, at a minimum, doing the following...[d]escribing the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[12]
- Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure the covered clearing agency has the authority and operational capacity to take timely

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10 17 CFR 240.17Ad-22(e)(v)(viii).

11 17 CFR 240.17Ad-22(e)(4)(ix).

12 17 CFR 240.17Ad-22(e)(7)(ix).

action to contain losses and liquidity demands and continue to meet its obligations…"[13]

- Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[14]
- Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[15]

OCC meets the definition of a CCA and is therefore subject to the requirements of the CCA rules, including new Rules 17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix), (e)(7)(ix), (e)(13), (e)(23)(i) and (e)(23)(ii).[16]

Proposed Changes

Summary of Proposed Changes

In order to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish new tools by which OCC could re-establish a matched

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13 17 CFR 240.17Ad-22(e)(13).

14 17 CFR 240.17Ad-22(e)(23)(i).

15 17 CFR 240.17Ad-22(e)(23)(ii).

16 17 CFR 240.17Ad-22(e)(3)(ii), (e)(4)(viii), (e)(4)(ix) and (e)(7)(ix).

book following a default, OCC is proposing to make the following revisions to its Rules and By-Laws:

(1) Revise the existing assessment powers in Section 6 of Article VIII of OCC's By-Laws, specifically to:

(a) Establish a rolling "cooling-off period" that would be triggered by the payment of a proportionate charge against the Clearing Fund ("triggering proportionate charge"), during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing Member's required contribution as of the time immediately preceding the triggering proportionate charge;

(b) Clarify that a Clearing Member that chooses to terminate its membership status during a cooling-off period will not be liable for replenishment of the Clearing Fund immediately following the expiration of such cooling-off period, provided that the withdrawing Clearing Member satisfies enumerated criteria, including providing notice of such termination by no later than the end of the cooling-off period and by closing-out and/or transferring of all its open positions with OCC by no later than the last day of the cooling-off period; and

(c) Delineate between the obligation of a Clearing Member to replenish its contributions to the Clearing Fund and its obligations to meet additional "assessments" that may be levied following a proportionate charge to the Clearing Fund.

(2) Adopt a new Rule 1011[17] that would provide OCC with discretionary authority to call for voluntary payments from non-defaulting Clearing Members in a circumstance where one or more Clearing Members has already defaulted and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[18] Rule 1011 also would establish that OCC would prioritize compensation of Clearing Members that made voluntary payments from any amounts recovered from the defaulted Clearing Members.

(3) Adopt a new Rule 1111 that would provide authority to:

(a) Allow OCC to call for voluntary tear-ups ("Voluntary Tear-Up," as defined below) of non-defaulting Clearing Member and/or customer positions at any time following the suspension or default of a Clearing Member, with the scope of any such Voluntary Tear-Ups being determined by the Risk Committee of OCC's Board ("Risk Committee");

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17 OCC is amending the Initial Filing to renumber proposed Rule 1009 to proposed Rule 1011 and updated related cross references in Rule 1111 to reflect this renumbering. OCC is also amending the Default Management Policy as submitted in the Initial Filing to update similar cross references.

18 Under the Initial Filing, OCC's authority to conduct Partial Tear-Ups, as well as call for voluntary payments or to conduct Voluntary Tear-Ups, would be conditioned in part on OCC having determined that, notwithstanding the availability of any remaining resources, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under the Initial Filing, the proposed text of Rules 1009(a), 1111(a) and 1111(b) incorrectly transcribed this condition to require that OCC determine that, notwithstanding the availability of any remaining resources, OCC *does* not have sufficient resources to satisfy its obligations and liabilities resulting from such default (emphasis added). In each such instance, OCC is amending the proposed text of Rules 1009(a) (which is being renumbered as Rule 1011(a)), 1111(a) and 1111(b) in Exhibit 5B of the Initial Filing to delete the word "does" and insert in its place the word "may."

(b) Allow OCC's Board to vote to tear-up the "Remaining Open Positions" (defined below) of a defaulted Clearing Member, as well as any "Related Open Positions" (defined below) in a circumstance where OCC has attempted one or more auctions of such defaulted Clearing Member's remaining open positions and OCC has determined that it may not have sufficient resources to satisfy its obligations and liabilities resulting from such default with the scope of any such tear-up ("Partial Tear-Up") being determined by the Risk Committee; and

(c) Allow OCC's Board to vote to re-allocate losses, costs and fees imposed upon holders of positions extinguished in a Partial Tear-Up through a special charge levied against remaining non-defaulting Clearing Members.

(4) Revise the descriptions and authorizations in Article VIII of OCC's By-Laws concerning the use of the Clearing Fund to reflect the discretion of OCC to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from a Voluntary Tear-Up or a mandatory tear-up ("Partial Tear-Up," as defined below).

Discussion of Proposed Changes

Each of the proposed revisions to OCC's Rules and By-Laws is described in more detail in the following sub-sections:

1. Proposed Changes to OCC's Assessment Powers

a. Current Assessment Powers

OCC's current assessment powers are described in Section 6 of Article VIII of OCC's By-Laws. Section 6 establishes a general requirement for each Clearing Member

to promptly make good any deficiency in its required contribution to the Clearing Fund whenever an amount is paid out of its Clearing Fund contribution (whether by proportionate charge or otherwise).[19] In this regard, a Clearing Member's obligation to replenish the Clearing Fund is not currently subject to any pre-determined limit. Notwithstanding the foregoing, a Clearing Member can limit the amount of its liability for replenishing the Clearing Fund (at an additional 100% of the amount of its then-required Clearing Fund contribution) by winding-down its clearing activities and terminating its status as a Clearing Member. Any Clearing Member seeking to so limit its liability for replenishing the Clearing Fund must: (i) notify OCC in writing not later than the fifth business day after the proportionate charge that it is terminating its status as a Clearing Member, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close out or transfer all of its open positions as promptly as practicable after giving notice

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19 Under Article VIII, Section 6 of OCC's By-Laws, OCC currently has authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund in certain enumerated situations. For example, Section 6 generally provides that if the conditions regarding a Clearing Member default specified in subparagraphs (a)(i) through (vi) of Article VIII, Section 5 of OCC's By-Laws are satisfied, OCC will make good resulting losses or expenses that are suffered by OCC by applying the defaulting Clearing Member's Clearing Fund contribution after first applying other funds available to OCC in the accounts of the Clearing Member. If the sum of the obligations, however, exceeds the total Clearing Fund contribution and other funds of the defaulting Clearing Member available to OCC, then OCC will charge the amount of the remaining deficiency on a proportionate basis against all non-defaulting Clearing Members' required contributions to the Clearing Fund at the time. Section 5(b) of Article VIII of OCC's By-Laws similarly provides for proportionate charges against Clearing Members' contributions to the Clearing Fund when certain conditions are met that involve a failure by a bank or a securities or commodities clearing organization to perform obligations to OCC when they are due.

to OCC. Thus, withdrawal from clearing membership is the only means by which a Clearing Member currently can limit its liability for replenishing the Clearing Fund.

b. Proposed Changes to Assessment Powers

OCC proposes to revise Section 6 of Article VIII of OCC's By-Laws to make three primary modifications regarding its existing authority to assess proportionate charges against Clearing Members' contributions to the Clearing Fund. First, the proposal introduces an automatic minimum fifteen calendar day "cooling-off" period that begins when a proportionate charge is assessed by OCC against Clearing Members' Clearing Fund contributions. While the cooling-off period will continue for a minimum of fifteen consecutive calendar days, if one or more of the events described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws occur(s) during that fifteen calendar day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through either (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth day from the date of the proportionate charge that initiated the cooling-off period, whichever is sooner.

During a cooling-off period, each Clearing Member would have its aggregate liability to replenish the Clearing Fund capped at 200% of the Clearing Member's then-required contribution to the Clearing Fund. Once the cooling-off period ends each remaining Clearing Member would be required to replenish the Clearing Fund in the amount necessary to meet its then-required contribution. Once the cooling-off period ends, any remaining losses or expenses suffered by OCC as a result of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that

occurred during such cooling-off period could not be charged against the amounts Clearing Members have contributed to replenish the Clearing Fund upon the expiration of the cooling-off period.[20]

Second, in connection with the cooling-off period, the proposal would extend the time frame within which a Clearing Member may provide a termination notice to OCC to avoid liability for replenishment of the Clearing Fund after the cooling-off period and would modify the obligations of such a terminating Clearing Member for closing-out and transferring its remaining open positions. Specifically, to effectively terminate its status as a Clearing Member and not be liable for replenishing the Clearing Fund after the cooling-off period, a Clearing Member would be required to: (i) notify OCC in writing of its intent to terminate not later than the last day of the cooling-off period, (ii) not initiate any opening purchase or opening writing transaction, and, if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member, not initiate any Stock Loan transaction, through any of its accounts, and (iii) close-out or transfer all of its open positions by no later than the last day of the cooling-off period. If a Clearing Member fails to satisfy all of these conditions by the end of a given cooling-off period, it would not have completed all of the requirements necessary to terminate its status as a Clearing Member under Article VIII, Section 6 of OCC's By-Laws and therefore it would remain subject to the obligation to replenish the Clearing Fund after the end of the cooling-off period.

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[20] After a cooling-off period has ended, the occurrence of any event described in clauses (i) through (iv) of Article VIII, Section 5(a) of OCC's By-Laws that results in a proportionate charge against the Clearing Fund would trigger a new cooling off period, and thusly, a cap of 200% of each Clearing Member's then-required contribution would again apply.

Third, the proposal would clarify the distinction between "replenishment" of the Clearing Fund and a Clearing Member's obligation to answer "assessments." In this context, the term "replenish" (and its variations) shall to refer to a Clearing Member's standing duty, following any proportionate charge against the Clearing Fund, to return its Clearing Fund contribution to the amount required from such Clearing Member for the month in question.[21] The term "assessment" (and its variations) shall refer to the amount, during any cooling-off period, that a Clearing Member would be required to contribute to the Clearing Fund in excess of the amount of the Clearing Member's pre-funded required Clearing Fund contribution.

Proposed Addition of Ability to Request Voluntary Payments

OCC proposes to add new Rule 1011, which will provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[22] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Under new Rule 1011, OCC will initiate a call for voluntary payments by issuing a "Voluntary Payment Notice" inviting all non-defaulting Clearing Members

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21 This assumes that the proportionate charge resulted in the Clearing Member's actual Clearing Fund contribution dropping below the amount of its required contribution (*i.e.*, that the Clearing Member did not have excess above its required contribution that was sufficient to cover the amount of the proportionate charge allocated to such Clearing Member).

22 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

to make payments to the Clearing Fund in addition to any amounts they are otherwise required to contribute pursuant to Rule 1001. The Voluntary Payment Notice would specify the terms applicable to any voluntary payment, including but not limited to, that any voluntary payment may not be withdrawn once made, that no Clearing Member shall be obligated to make a voluntary payment and that OCC shall retain full discretion to accept or reject any voluntary payment. Rule 1011 specifies that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s), OCC would seek to compensate first from such recovery all non-defaulting Clearing Members that made voluntary payments (and if the amount recovered from the defaulted Clearing Member(s) is less than the aggregate amount of voluntary payments, non-defaulting Clearing Members that made voluntary payments each would receive a percentage of the recovery that corresponds to that Clearing Member's percentage of the total amount of voluntary payments received).

Proposed Addition of Ability to Conduct Voluntary Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to voluntarily extinguish (i.e., voluntarily tear-up) their open positions at OCC in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.

While Risk Committee approval is not needed to commence a voluntary tear-up, the Risk Committee would be responsible for determining the appropriate scope of each voluntary tear-up. To ensure OCC retains sufficient flexibility to effectively deploy this tool in an extreme stress event, proposed Rule 1111(c) is drafted to provide the Risk Committee with discretion to determine the appropriate scope of each voluntary tear-up.[23] New Rule 1111(c) also would impose standards designed to circumscribe the Risk Committee's discretion, requiring that any determination regarding the scope of a voluntary tear-up shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

Once the Risk Committee has determined the scope of the Voluntary Tear-Up, OCC will initiate the call for voluntary tear-ups by issuing a "Voluntary Tear-Up Notice." The Voluntary Tear-Up Notice shall inform all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear-Up.[24] The Voluntary Tear-Up Notice would specify the terms applicable to any voluntary tear-up, including but not limited to, that no Clearing Member or customers of a Clearing Member shall be obligated to participate in a voluntary tear-up and that OCC shall retain full discretion to accept or reject any voluntary tear-up.

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23 Notwithstanding the discretion that would be afforded by the text of proposed Rule 1111(c), OCC anticipates that the scope of voluntary tear-ups likely would be dictated by the cleared contracts remaining in the portfolio(s) of the defaulted Clearing Member(s).

24 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Voluntary Tear-Up of the opportunity to participate in such tear-up.

OCC is not proposing a tear-up process that would require the imposition of "gains haircutting" (*i.e.*, the reduction of unpaid gains) on a portion of OCC's cleared contracts.[25] Instead, OCC has determined that its tear-up process – for both Voluntary Tear-Ups as well as Partial Tear-Ups – should be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC would be expected to have adequate remaining resources to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains.[26]

In OCC's proposed tear-up process, the holders of torn-up positions would be assigned a Tear-Up Price and OCC would draw on its remaining financial resources in order to extinguish the torn-up positions at the assigned Tear-Up Price without forcing a reduction in the amount of unpaid value of such positions. OCC is amending the Initial Filing to clarify that while OCC does not intend, in the first instance, for its tear-up process to serve as a means of loss allocation, circumstances may arise such that, despite best efforts, OCC has inadequate remaining financial resources to extinguish torn-up positions at their assigned Tear-Up Price without forcing a reduction in the amount of

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25 In general, forced gains haircutting is a tool that can be more easily applied to products whose gains are settled at least daily, like futures through an exchange of variation margin, and by central counterparties with comparatively large daily settlement flows. Listed options, which constitute the vast majority of the contracts cleared by OCC, do not have daily settlement flows and any attempt to reduce the "unrealized gains" of a listed options contract would require the reduction of the option premium that is embedded within the required margin (such a process would effectively require haircutting the listed option's initial margin).

26 OCC anticipates that it would determine the date on which to initiate Partial Tear-Ups by monitoring its remaining financial resources against the potential exposure of the remaining unauctioned positions from the portfolio(s) of the defaulted Clearing Member(s).

unpaid value of such positions (e.g., despite best efforts, market movements not accounted for by monitoring, additional Clearing Member defaults occur immediately preceding a tear-up). In such circumstances, despite best efforts, OCC would use its partial tear-up process as a means of loss allocation.[27]

The proposed changes would provide OCC with two separate and non-exclusive means of equitably re-allocating the losses, costs or expenses imposed upon the holders of torn-up positions as a result of the tear-up(s). First, the proposed changes to Article VIII would provide OCC discretion to use remaining Clearing Fund contributions to re-allocate losses imposed on non-defaulting Clearing Members and customers from such tear-up(s). Second, Rule 1111(a) would provide that if OCC subsequently recovers from the defaulted Clearing Member or the estate(s) of the defaulted Clearing Member(s) and the amount of such recovery exceeds the amount OCC received in voluntary payments, then non-defaulting Clearing Members and non-defaulting customers that voluntarily tore-up open positions and incurred losses from such tear-ups would be repaid from the amount of the recovery in excess of the amount OCC received in voluntary payments.[28] If the amount recovered is less than the aggregate amount of Voluntary Tear-Up, each

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27 This change does not impact the statutory basis for the proposed rule change.

28 In order to effect re-allocation of the losses, costs or expenses imposed upon the holders of torn-up positions, OCC expects that after it has completed its tear-up process and re-established a matched book, holders of both voluntarily torn-up and mandatorily torn-up positions would be provided with a limited opportunity to re-establish positions in the contracts that were voluntarily or mandatorily extinguished. After the expiration of such period, OCC would seek to collect the information on the losses, costs or expenses that had been imposed on the holders of torn-up positions. Based on the information collected, OCC would determine whether it can reasonably determine the losses, costs and expenses sufficiently to re-allocate such amounts.

non-defaulting Clearing Member and non-defaulting customer that incurred losses from voluntarily torn-up positions would be repaid in an amount proportionate to the percentage of its total amount of losses, costs and fees imposed on Clearing Members or customers as a result of the Voluntary Tear-Ups.

With respect to Voluntary Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

Proposed Addition of Ability to Conduct Partial Tear-Ups

OCC proposes to add new Rule 1111, which, in relevant part, will provide the Board with discretion to extinguish the remaining open positions of any defaulted Clearing Member or customer of such defaulted Clearing Member(s) (such positions, "Remaining Open Positions"), as well as any related open positions as necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions (such positions, "Related Open Positions"), in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default (such tear-ups hereinafter collectively referred to as "Partial Tear-Ups"). Like the determination for Voluntary Tear-Ups, the Risk Committee shall determine the appropriate scope of each Partial Tear-Up and such determination shall (i) be based on then-existing facts and circumstances, (ii) be in furtherance of the integrity of OCC and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants. Once the Risk

Committee has determined the scope of the Partial Tear-Up, OCC will initiate the Partial Tear-Up process by issuing a "Partial Tear-Up Notice." The Partial Tear-Up Notice shall (i) identify the Remaining Open Positions and Related Open Positions designated for tear-up, (ii) identify the open positions of non-defaulting Clearing Members and non-defaulting customers that will be subject to Partial Tear-Up (such positions, "Tear-Up Positions"), (iii) specify the termination price ("Partial Tear-Up Price") for each position to be torn-up, and (iv) list the date and time as of which the Partial Tear-Up will occur.[29] With regard to the date and time of a Partial Tear-Up, Rule 1111(d) specifies that the Risk Committee shall set the date and time. With regard to the Partial Tear-Up Price, OCC anticipates that it is likely to use the last established end-of-day settlement price, in accordance with its existing practices concerning pricing and valuation. However, given that it is not possible to know in advance the precise circumstances that would cause OCC to conduct a tear-up, Rule 1111(f) has been drafted to allow OCC to exercise reasonable discretion, if necessary, in establishing the Partial Tear-Up Price by some means other than its existing practices concerning pricing and valuation.[30] Specifically, Rule 1111(f) would require that OCC, in exercising any such discretion, would act in

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29 Since OCC does not know the identities of Clearing Members' customers, OCC would depend on each Clearing Member to notify its customers with positions in scope of the Partial Tear-Up of the possibility of tear-up.

30 For example, OCC has observed certain rare circumstances in which a closing price for an underlying security of an option may be stale or unavailable. A stale or unavailable closing price could be the result of a halt on trading in the underlying security, or a corporate action resulting in a cash-out or conversion of the underlying security (but that has not yet been finalized), or the result of an ADR whose underlying security is being impacted by certain provisions under foreign laws. OCC would consider the presence of these factors on its end-of-day prices in determining whether use of the discretion that would be afforded under proposed Rule 1111(f) might be warranted.

good faith and in a commercially reasonable manner to adopt methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models that use the market price of the underlying interest or the market prices of its components. Rule 1111(f) further specifies that OCC may consider the same information set forth in subpart (c) of Section 27, Article VI of OCC's By-Laws.[31]

The scope of any Partial Tear-Up will be determined in accordance with Rule 1111(e).[32] With respect to the extinguishment of Remaining Open Positions, OCC will designate Tear-Up Positions in identical Cleared Contracts and Cleared Securities on the

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31 In relevant part, subpart (c) reads as follows: "In determining a close-out amount, the Corporation may consider any information that it deems relevant, including, but not limited to, any of the following: (1) prices for underlying interests in recent transactions, as reported by the market or markets for such interests; (2) quotations from leading dealers in the underlying interest, setting forth the price (which may be a dealing price or an indicative price) that the quoting dealer would charge or pay for a specified quantity of the underlying interest; (3) relevant historical and current market data for the relevant market, provided by reputable outside sources or generated internally; and (4) values derived from theoretical pricing models using available prices for the underlying interest or a related interest and other relevant data. Amounts stated in a currency other than U.S. Dollars shall be converted to U.S. Dollars at the current rate of exchange, as determined by the Corporation. A position having a positive close-out value shall be an 'asset position' and a position having a negative close-out value shall be a 'liability position.'"

32 OCC is amending the Initial Filing to reflect that after further evaluation of its proposed recovery tools and the proposed tear-up process, OCC does not believe there would be a need to assign or transfer any hedging transactions established with relation to tear-up positions. OCC is therefore amending the Initial Filing to remove text in proposed Rule 1111(e) concerning proposed authority for OCC to offer to assign or transfer any hedging transactions related to Remaining Open Positions with related Tear-Up Positions. This change does not impact the statutory basis for the proposed rule change.

opposite side of the market and in an aggregate amount equal to that of the Remaining Open Positions. OCC will only designate Tear-Up Positions in the accounts of non-defaulting Clearing Members (inclusive of such Clearing Members' customer accounts) with an open position in the applicable Cleared Contract or Cleared Security.[33] Tear-Up Positions shall be designated and applied by OCC on a pro rata basis across all the identical positions in Cleared Contracts and Cleared Securities on the opposite side of the market in the accounts of non-defaulted Clearing Members and their customers.[34]

Rule 1111(e)(iii) provides that every Partial Tear-Up position is automatically terminated upon and with effect from the Partial Tear-Up Time, without the need for any further step by any party to such Cleared Contract or Cleared Security, and that upon termination, either OCC or the relevant Clearing Member (as the case may be) shall be obligated to pay the other the applicable Partial Tear-Up Price. Rule 1111(e)(iii) further

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33 Since, as stated in the Initial Filing, the objective of Partial Tear-Ups is to extinguish the Remaining Open Positions cleared by the defaulted Clearing Member(s) *or customer of such defaulted Clearing Member(s)* (emphasis added), OCC does not believe there would be a need to designate Tear-Up Positions to the non-defaulted customers of a defaulted Clearing Member. OCC is therefore amending the Initial Filing to remove references to non-defaulted customers of defaulted Clearing Members.

34 OCC is amending the Initial Filing to clarify that a non-defaulted Clearing Member would be required to allocate the assigned Tear-Up Positions on a pro rata basis across those customers that have open positions in such Cleared Contract or Cleared Security in such account, and for any listed option positions being extinguished, allocation across customer accounts should occur in accordance with such Clearing Member's procedures for allocating exercises and assignments. This change does not impact the statutory basis for the proposed rule change.

provides that the corresponding open position shall be deemed terminated at the Partial Tear-Up Price.[35]

Rule 1111(g) provides that to the extent losses imposed upon non-defaulting Clearing Members and non-defaulting customers resulting from a Partial Tear-Up can reasonably be determined, the Board may elect to re-allocate such losses among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.[36]

With respect to Partial Tear-Ups, new Rule 1111(h) would clarify that no action or omission by OCC pursuant to and in accordance Rule 1111 shall constitute a default by OCC.

2. Statutory Basis

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35 OCC is amending the Initial Filing and the proposed text of Rule 1111(e)(iii) to clarify that if, in certain circumstances discussed above (see fn. 27 and associated text), OCC, in its discretion, determines that its remaining resources are inadequate to pay the applicable Partial Tear-Up Price for each position being extinguished in the Partial Tear-Up, OCC shall be obligated to pay each relevant Clearing Member a pro rata amount of the applicable Partial Tear-Up Price based on OCC's remaining resources, and the relevant Clearing Member shall have a claim against the Corporation for the value of the difference between the pro rata amount received and the Partial Tear-Up Price. This change does not impact the statutory basis for the proposed rule change.

36 For the avoidance of doubt, the special charge would be distinct and separate from a Clearing Member's obligation to satisfy Clearing Fund assessments, and therefore, would not be subject to the aforementioned assessment cap in the amount of 200% of a Clearing Member's then-required contribution to the Clearing Fund.

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934 ("Act"),[37] requires, among other things, that the rules of a clearing agency be designed to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest. OCC believes that the proposed rule change is consistent with the requirements of Section 17A(b)(3)(F) of the Act[38] and the rules thereunder applicable to OCC for the reasons set forth below.

As stated above, each of the changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario. In this regard, the proposed changes are designed to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to establish tools to enable OCC to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC's process in crafting the proposed changes was informed by published guidance from OCC's primary regulators (the Commission and the Commodity Futures Trading Commission), the publications of key international organizations (including the Bank for International Settlements, the International Organization of Securities Commissions and the Financial Stability Board) and the publications of key industry trade organizations. OCC's proposal was further

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37 15 U.S.C. 78q-1(b)(3)(F).

38 Id.

informed by conversations with, among others, OCC's Board, OCC's Risk Committee, Clearing Members and market participants.

Informed by these perspectives, OCC has crafted the proposed changes with the aim of enhancing its ability to address an unprecedented loss event but also, to the extent possible, providing a reasonable amount of certainty to Clearing Members, customers and other stakeholders about the potential consequences of such an event and the resources and tools that would be expected to be available to OCC in support of its clearing operations.[39] Accordingly, the proposed changes should leave Clearing Members, customers and other stakeholders in a position to better evaluate the risks and benefits of clearing in order to facilitate their own risk management, and to the extent applicable, their own regulatory and capital considerations. The proposed changes also seek to avoid a result that would force only particular clearing participants to shoulder certain losses in an extreme stress scenario (*i.e.*, holders of positions extinguished in Partial Tear-Ups),[40] and instead leaves OCC and its Board with discretionary tools that could provide a more equitable method of allocating the losses from such an event more broadly, consistent with the general principle of mutualized loss that upon which central clearing rests. In this regard, OCC believes the proposed changes foster cooperation and coordination with participants in the clearing system, consistent with Section 17A(b)(3)(F) of the Act.[41]

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39 OCC notes that the very nature of an extreme stress and unprecedented loss event means that its impact is difficult to predict and quantify in advance.

40 Absent a means of re-allocating the potential losses, costs and fees imposed upon holders of positions extinguished during tear-ups, the holders of such positions would be left to individually address such losses, costs and fees.

41 15 U.S.C. 78q-1(b)(3)(F).

As stated above, the proposed changes are designed to enable OCC to further address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and to re-establish a matched book and limit OCC's potential exposure to losses from a Clearing Member default, in each case as might result from an unprecedented loss scenario that exceeds OCC's standard risk management and default management procedures. OCC believes that the proposed changes will facilitate its ability to fully allocate, and ultimately extinguish, the loss so that it has a better opportunity of withstanding an extreme stress scenario without sacrificing its viability as a going concern or its ability to continue to provide its critical clearing services. In this regard, OCC believes that the proposed changes remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.[42]

The proposed changes are designed to enhance the stability of the clearing system generally and are aimed at ensuring that OCC has adequate tools and resources to better protect market participants from the risks of extreme stress scenarios and unprecedented loss events. In this regard, OCC believes that the proposed changes are reasonably designed to protect investors and the public interest, consistent with Section 17A(b)(3)(F) of the Act.[43]

The proposed changes also are designed to further OCC's compliance, in whole or in part, with the provisions of the Commission's rules discussed immediately below:

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42 Id.

43 Id.

Recovery and Orderly Wind-Down

In relevant part, Rule 17Ad-22(e)(3)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…plan[] for the recovery and orderly wind-down of the [CCA] necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses."[44] As stated above, each of the proposed changes is designed to provide OCC with tools to address the risks OCC might confront in a recovery and orderly wind-down scenario.[45] Consistent with the requirements of Rule 17Ad-22(e)(3)(ii), the proposed tools would enable OCC to better address the risks of liquidity shortfalls and credit losses resulting from a Clearing Member default or certain other loss events and, if necessary, to ultimately re-establish a matched book in a recovery or orderly wind-down scenario.[46] In this context, the proposed changes serve as a critical component of OCC's recovery and orderly wind-down plan. As a result, in OCC's view, the proposed changes are consistent with the requirements of Rule 17Ad-22(e)(3)(ii) as to the recovery and orderly wind-down plan.[47]

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44 17 CFR 240.17Ad-22(e)(3)(ii).

45 Indeed, the OCC's separately filed recovery and orderly wind-down plan identifies OCC's assessment powers, ability to call for voluntary payments, ability to call for Voluntary Tear-Ups and ability to impose Partial Tear-Ups among its "Recovery Tools." OCC has filed a proposed rule change with the Commission in connection with this proposal. See Securities Exchange Act Release No. 82352 (December 19, 2017), 82 FR 61072 (December 26, 2017) (SR-OCC-2017-021). On March 22, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change. See Securities Exchange Act Release No. 82927 (March 22, 2018), 83 FR 13176 (March 27, 2018) (SR-OCC-2017-021).

46 17 CFR 240.17Ad-22(e)(3)(ii).

47 17 CFR 240.17Ad-22(e)(3)(ii).

Allocation of Credit Losses Above Available Resources

In relevant part, Rule 17Ad-22(e)(4)(viii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to …[a]ddress[] allocation of credit losses the [CCA] may face if its collateral and other resources are insufficient to fully cover its credit exposures…"[48] The proposed changes would provide OCC with three distinct tools that could be used to allocate any credit losses OCC may face in excess of collateral and other resources available to OCC. First, new Rule 1011 would provide a framework by which OCC could receive voluntary payments in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211,[49] OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Second, new Rule 1111 would establish a framework by which non-defaulting Clearing Members and non-defaulting customers of Clearing Members could be given an opportunity to participate in Voluntarily Tear-Ups in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default. Finally, new Rule 1111 also would provide the Board with discretion

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48 17 CFR 240.17Ad-22(e)(v)(viii).

49 Rule 707 addresses the treatment of funds in a Clearing Member's X-M accounts. Rule 1001 addresses the size of OCC's Clearing Fund and the amount of a Clearing Member's contribution. Rules 1104 through 1107 concern the treatment of the portfolio of a defaulted Clearing Member. Rules 2210 and 2211 concern the treatment of Stock Loan positions of a defaulted Clearing Member.

to mandatorily tear-up Remaining Open Positions and Related Open Positions, in a circumstance where a Clearing Member has defaulted and OCC has determined that, notwithstanding the availability of any remaining resources under OCC Rules 707, 1001, 1104 through 1107, 2210 and 2211, OCC may not have sufficient resources to satisfy its obligations and liabilities resulting from such default.[50] In OCC's view, each of these tools could be deployed by OCC, if necessary, to allocate credit losses in excess of the collateral and other resources available to OCC, in accordance with Rule 17Ad-22(e)(4)(viii).[51]

Replenishment of Financial Resources Following a Default

In relevant part, Rule 17Ad-22(e)(4)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any financial resources it may use following a default or other event in which use of such resources is contemplated."[52] OCC's Clearing Members have a standing obligation to replenish the Clearing Fund following any proportionate charge. The proposed changes would establish a rolling cooling-off period, triggered by the payment of a proportionate charge against the Clearing Fund, during which period the aggregate liability of a Clearing Member to replenish the Clearing Fund (inclusive of assessments) would be 200% of the Clearing

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50 Rule 1111(g), which would provide the Board authority to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge, would serve as a discretionary tool to redistribute the credit losses allocated through Partial Tear-Up.

51 17 CFR 240.17Ad-22(e)(v)(viii).

52 17 CFR 240.17Ad-22(e)(4)(ix).

Member's required contribution as of the time immediately preceding the triggering proportionate charge. Compared to the current requirement under which a Clearing Member may cap its liability to proportionate charges at an additional 100% of its then-required contribution, a Clearing Member would instead be permitted to cap its liability for proportionate charges at an additional 200% of its then-required Clearing Fund contribution.

OCC believes that the proposed approach improves predictability for OCC and for Clearing Members regarding the size of Clearing Fund contributions that are likely to be subject to assessments for proportionate charges. Additionally, replacing the five business day withdrawal period with the withdrawal period commensurate with the cooling-off period (which, as proposed would be a minimum of fifteen calendar days) would give Clearing Members a more reasonable period in which to meet the wind-down and termination requirements necessary to cap their liability. OCC believes that this would afford them greater certainty regarding their maximum liability with respect to the Clearing Fund during extreme stress events, which in turn, facilitates Clearing Members' management of their own risk management, and to the extent applicable, regulatory capital considerations. And OCC believes this increased predictability would also be beneficial to OCC by helping it to more reliably understand the amount of Clearing Fund contributions that will likely be available to it after a proportionate charge is assessed.[53]

OCC believes that the relative certainty provided by the proposed cooling-off period and 200% cap on assessments ultimately could reduce the risks of successive or

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53 Under the existing approach, it is less certain from OCC's standpoint regarding whether Clearing Members would reasonably be able to cap their liability to proportionate charges within five business days.

"cascading" defaults, in which the financial demands on remaining non-defaulting Clearing Members to continually replenish OCC's Clearing Fund (and similar guaranty funds at other CCPs to which such Clearing Members might belong) have the effect of further weakening such Clearing Members to the point of default. In this regard, the proposed changes are designed to provide OCC, Clearing Members and other stakeholders with sufficient time to manage the ongoing default(s) without further aggravating the extreme stresses facing market participants.

OCC recognizes that the proposed changes would limit the maximum amount of Clearing Fund resources that could be available to OCC in an extreme stress scenario, which introduces the possibility, however remote, that the proposed 200% cap ultimately could be reached. If during any cooling-off period the amount of aggregate proportionate charges against the Clearing Fund approaches the 200% cap, the amount remaining in the Clearing Fund may no longer be sufficient to comply with the applicable minimum regulatory financial resources requirements in the CCAs. In any such event, OCC's existing authority under Rule 603 would permit OCC to call on participants for additional initial margin, which could ensure that OCC's minimum financial resources remain in excess of applicable CCA requirements.[54] OCC recognizes that the imposition of increased margin requirements could have an immediate pro-cyclical impact on participants (and consequential impacts on the broader financial system) that is potentially greater than the impact of replenishing the Clearing Fund. These risks would

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54 Rule 603 provides that "[t]he Risk Committee may, from time to time, increase the amount of margin which may be required in respect of a cleared contract, open short position or exercised contract if, in its discretion, it determines that such increase is advisable for the protection of [OCC], the Clearing Members or the general public."

be limited to a specific extreme stress event and could be mitigated by certain factors. First, OCC, in coordination with its regulators, would carefully evaluate any potential increase in the context of then-existing facts and circumstances. Second, during the cooling-off period, Clearing Members and their customers will have the opportunity to reduce or rebalance their respective portfolios in order to mitigate their exposures to stress losses and initial margin increases. Finally, since initial margin is not designed to be subject to mutualized loss, the risk of loss faced by Clearing Members for amounts posted as additional margin would be substantially less than for replenishments of the Clearing Fund.

Given the products cleared by OCC and the composition of its clearing membership, OCC has determined that a minimum 15-calendar day cooling-off period, rolling up to a maximum of 20 calendar days, is likely to be a sufficient amount of time for OCC to manage the ongoing default(s) and take necessary steps in furtherance of stabilizing the clearing system. Further, through conversations with Clearing Members, OCC believes that the proposed cooling-off period is likely to be a sufficient amount for Clearing Members (and their customers) to orderly reduce or rebalance their positions, in an attempt to mitigate stress losses and exposure to potential initial margin increases as they navigate the stress event. Through conversations with Clearing Members, OCC also believes that the proposed cooling-off period is likely to be a sufficient amount for certain Clearing Members to orderly close-out their positions and transfer customer positions as they withdraw from clearing membership. OCC believes the proposed cooling-off period, coupled with the other proposed changes to OCC's assessment powers, is likely to provide Clearing Members with an adequate measure of stability and predictability as

to the potential use of Clearing Fund resources, which OCC believes removes the existing incentive for Clearing Members to withdraw following a proportionate charge.[55]

In light of the foregoing, OCC believes that the proposed changes would enhance and strengthen its process to replenish the Clearing Fund following a default or other event in which use of the Clearing Fund is contemplated, in accordance with Rule 17Ad-22(e)(4)(ix).[56]

Replenishment of Liquid Resources

In relevant part, Rule 17Ad-22(e)(7)(ix) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[d]escrib[e] the [CCA's] process to replenish any liquid resources that the clearing agency may employ during a stress event."[57] Since the use any part of the cash portion of OCC's Clearing Fund would constitute a depletion of one of OCC's liquid resources, OCC's assessment power, discussed above, is the primary means of replenishing the Clearing Fund cash that OCC used to address the stress event. For the same reasons stated above, OCC believes that the proposed changes enhance and strengthen its process to replenish the Clearing Fund, as necessary, following a default or other stress event in

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55 OCC initially considered a fixed 15-calendar day cooling-off period; however, OCC concluded that a fixed 15-calendar day cooling-off period may increase the risks of successive or cascading Clearing Member defaults and may perversely incentivize Clearing Members to seek to withdraw from clearing membership. Through conversations with Clearing Members, OCC believes that these potentially disruptive consequences are mitigated by the proposed rolling cooling-off period.

56 17 CFR 240.17Ad-22(e)(4)(ix).

57 17 CFR 240.17Ad-22(e)(7)(ix).

which the Clearing Fund is used, and therefore, OCC views the proposed changes as consistent with Rule 17Ad-22(e)(7)(ix).[58]

Timely Action to Contain Losses

In relevant part, Rule 17Ad-22(e)(13) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[e]nsure the [CCA] has the authority and operational capacity to take timely action to contain losses and liquidity demands and continue to meet its obligations…"[59] The proposed changes would provide OCC with the authority to call for Voluntary Tear-Ups and OCC's Board with the discretion to impose Partial Tear-Ups, which would provide OCC with authority necessary to extinguish certain losses (and attendant liquidity demands) thereby potentially enabling OCC to continue to meet its remaining obligations to participants. As designed, Voluntary Tear-Ups and Partial Tear-Ups would be initiated on a date sufficiently in advance of the exhaustion of OCC's financial resources such that OCC is expected to have adequate resources remaining to cover the amount it must pay to extinguish the positions of Clearing Members and customers without haircutting gains. Accordingly, OCC believes that its authority and capacity to conduct a Partial Tear-Up should be timely, relative to the adequacy of OCC's remaining financial resources. Finally, OCC believes it has the operational and systems capacity sufficient to support the proposed changes, and OCC's policies and procedures will be updated accordingly to

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58 17 CFR 240.17Ad-22(e)(7)(ix).

59 17 CFR 240.17Ad-22(e)(13).

reflect the existence of these new tools. As a result, OCC believes that the proposed changes conform to the relevant requirements in Rule 17Ad-22(e)(13).[60]

Public Disclosure of Key Aspects of Default Rules

In relevant part, Rule 17Ad-22(e)(23)(i) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]ublicly disclos[e] all relevant rules and material procedures, including key aspects of its default rules and procedures."[61] As stated above, each of the tools discussed herein are contemplated to be deployed by OCC if an extreme stress event has placed OCC into a recovery or orderly wind-down scenario, and therefore, the tools discussed herein constitute key aspects of OCC's default rules. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that proposed changes would conform to the relevant requirements in Rule 17Ad-22(e)(23)(i).[62]

Sufficient Information Regarding the Risks, Fees and Costs of Clearing

In relevant part, Rule 17Ad-22(e)(23)(ii) requires that each CCA "establish, implement, maintain and enforce written policies and procedures reasonably designed to…[p]rovid[e] sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency."[63] The proposed changes would clearly explain to Clearing Members and

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60 17 CFR 240.17Ad-22(e)(13).

61 17 CFR 240.17Ad-22(e)(23)(i).

62 17 CFR 240.17Ad-22(e)(13).

63 17 CFR 240.17Ad-22(e)(23)(ii).

market participants that an extreme stress scenario could result in the use – and theoretically the exhaustion – of OCC's financial resources, inclusive of OCC's proposed assessment powers. Proposed changes to Section 6, Article VIII of OCC's By-Laws would explain Clearing Members' replenishment obligation and liability for assessments. The proposed changes also would clearly explain, through proposed Rules 1011 and 1111, that as OCC nears the exhaustion of its assessment powers, Clearing Members may be asked for voluntary payments and, if necessary, Clearing Members and customers may be asked to participate in a Voluntary Tear-Up and/or subject to a Partial Tear-Up. Proposed Rules 1011(b) and 1111(a)(ii) also would make clear that Clearing Members that made voluntary payments and Clearing Members and customers whose tendered positions were extinguished in the Voluntary Tear-Up would be prioritized in the distribution of any recovery from the defaulted Clearing Member(s). Proposed changes to Article VIII would clarify that the Clearing Fund contributions remaining after OCC has conducted a Voluntary Tear-Up or Partial Tear-Up could be used to compensate the non-defaulting Clearing Members and non-defaulting customers for the losses, costs or fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up. Proposed Rule 1111(g) would make clear that, following a Partial Tear-Up, OCC's Board may seek to equitably re-allocate losses, costs and fees directly imposed as a result of a Partial Tear-Up among all non-defaulting Clearing Members through a special charge. By incorporating the proposed changes into OCC's Rules and By-Laws, as further supplemented by the discussion in OCC's public rule filing, OCC believes that is has provided sufficient information to enable participants to identify and evaluate the risks,

fees, and other material costs they could incur by participating OCC, consistent with the requirements in Rule 17Ad-22(e)(23)(ii).[64]

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

Section 17A(b)(3)(I) of the Act[65] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. OCC does not believe the proposed rule change would have any impact or impose any burden on competition. The primary purpose of the proposed changes is to make certain revisions to OCC's Rules and By-Laws Laws that are designed to enhance OCC's existing tools to address the risks of liquidity shortfalls and credit losses and to establish tools by which OCC could re-establish a matched book following a default. As explained above, each of the tools proposed herein is contemplated to be deployed by OCC in an extreme stress event that has placed OCC into a recovery or orderly wind-down scenario. The proposed rule change is intended to provide Clearing Members, market participants and other stakeholders with greater certainty as to their liabilities and potential exposure to OCC in the event of an unprecedented loss scenario. OCC does not believe that the proposed changes would discriminatorily impact any Clearing Member's access to OCC's services or unnecessarily disadvantage or favor any particular user in relationship to another user. OCC recognizes that the nature of a Partial Tear-Up means that only particular Clearing Members and market participants holding certain positions may be impacted; however, the risk of Partial Tear-Ups is extremely remote, and even then, the proposed changes

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64 17 CFR 240.17Ad-22(e)(23)(ii).

65 15 U.S.C. 78q-1(b)(3)(I).

seek to provide means of equitably re-allocating the losses, costs and fees imposed by Voluntary Tear-Up or Partial Tear-Up. Therefore, OCC believes that the proposed changes would not 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

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 e-mail to rule-comments@sec.gov. Please include File Number SR-OCC-2017-020 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2017-020. 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 Section, 100 F Street, N.E., 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 https://www.theocc.com/about/publications/bylaws.jsp.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal or identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-OCC-2017-020 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.[66]

Robert W. Errett
Deputy Secretary

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66 17 CFR 200.30-3(a)(12).

EXHIBIT 4A

By-Laws

Underlined text indicates text proposed in the Initial Filing

Double underscored text indicates new proposed text

~~Double strikethrough~~ text indicates new deleted text

THE OPTIONS CLEARING CORPORATION

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BY-LAWS

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Article VIII - Clearing Fund

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By-Laws, Article VIII – Purpose and Use of Clearing Fund

Maintenance and Purpose of the Clearing Fund

SECTION 1. (a) The Corporation shall maintain a Clearing Fund to which each Clearing Member shall contribute, as provided in this Article VIII, to make good losses suffered by the Corporation, or losses suffered by the Clearing Fund resulting from borrowings pursuant to the authority in Section 5(e) of this Article, (i) as a result of the failure of any Clearing Member to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation, (ii) as a result of the failure of any Clearing Member (including any Appointed Clearing Member) or of CDS to perform its obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued, undertaken, or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable, (iii) as a result of the failure of any Clearing Member to perform any of its obligations to the Corporation in respect of the stock loan and borrow positions of such Clearing Member, (iv) in connection with any liquidation of a Clearing Member's open positions, (v) in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, (vi) as a result of the failure of any Clearing Member to make any other required payment or render any other required performance, or (vii) as a result of the failure of any bank or securities or commodities clearing organization to perform its obligations to the Corporation for reasons specified in Section 5 of this Article, or (viii) as a result of a borrowing by the Corporation for liquidity needs for same day settlement pursuant to the authority in Section 5(e) of this Article. Notwithstanding the foregoing, in the event that the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rule 1111, the Clearing Fund may be used to provide compensation to non-defaulting Clearing Members and their customers as a means of re-allocating the losses, costs and fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up, but only to the extent that such losses, costs and fees can be reasonably determined by the Corporation.

* * *

Application of the Clearing Fund
SECTION 5. (a) If:

(i) any Clearing Member shall fail to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation,
(ii) any Clearing Member, (including any Appointed Clearing Member) or of CDS shall fail to perform any obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable,
(iii) any Clearing Member shall fail to perform any obligation to the Corporation in respect of the stock loan and borrow positions of such Clearing Member,
(iv) the Corporation shall suffer any loss or expense upon any liquidation of a Clearing Member's open positions,
(v) the Corporation shall suffer any loss or expense in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, or
(vi) any Clearing Member shall fail to make any other payment or render any other performance required under the By-Laws or the Rules,

then the Corporation shall (after appropriate application of other funds in the accounts of the Clearing Member) apply the Clearing Member's Clearing Fund contribution to the discharge of such obligation, the reimbursement of such loss or expense, or the making of such payment or the funding of such performance. If the sum of all such obligations, losses or expenses, and payments exceeds the sum of the amount of the Clearing Member's total Clearing Fund contribution and the amount of the other funds of the Clearing Member available to the Corporation, and if the Clearing Member fails to pay the Corporation the amount of any such deficiency on demand, the amount of the deficiency shall be paid out of the Clearing Fund and charged on a proportionate basis against all other Clearing Members' computed contributions as fixed at the time, but the Clearing Member who failed to pay the deficiency shall remain liable to the Corporation for the full amount of such deficiency until repayment thereof by such Clearing Member, or

(vii) the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rue 1111,

then, the Corporation may elect to proportionately charge the Clearing Fund in the amount(s) the Corporation reasonably determines necessary to compensate non-defaulting Clearing Members and their customers for the losses, costs or fees imposed upon them as a direct~~ly~~ result of such Voluntary Tear-Up or Partial Tear-Up, but only to

the extent that such losses, costs and fees can be reasonably determined by the Corporation.

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Making Good of Charges to the Clearing Fund
SECTION 6.

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(a) *Making Good of Charges to the Clearing Fund.* Whenever an amount is paid out of the Clearing Fund contribution of a Clearing Member, whether by proportionate charge or otherwise, such Clearing Member shall be liable to promptly make good the deficiency in its required contribution resulting from such payment by replenishment of the Clearing Fund. ~~Notwithstanding the foregoing and except as provided for below, if the payment is made as a result of a proportionate charge, a Clearing Member will not be liable to make good more than an additional 100% of the amount of its then required contribution if (i) within five business days following such proportionate charge the Clearing Member notifies the Corporation in writing that it is terminating its status as a Clearing Member, (ii) no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case as promptly as practicable after the giving of such notice; provided that a Clearing Member which so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with the preceding sentence, and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.~~ Each Clearing Member shall have and shall at all times maintain the ability to ~~make good~~ replenish any deficiency described in this Section 6(a) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(b) *Cooling-Off Period; Assessments.* Notwithstanding anything in Section 6 and except as provided for below, if an amount is paid out of the Clearing Fund as a result of a proportionate charge resulting from any of the events described in clauses (i) through (iv) of Section 5(a), then starting on the date of such proportionate charge there shall automatically commence a cooling-off period during which a Clearing Member will not be liable to make good more than an additional 200% of the amount of its then required contribution (for definitional purposes,

amounts in excess of a Clearing Member's then required contribution shall be "assessments"). The cooling-off period shall be fifteen consecutive calendar days from the date of such proportionate charge; provided however, that if one or more subsequent events described in clauses (i) through (iv) of Section 5(a) occur during the fifteen-day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth calendar day from the date of the initial proportionate charge, whichever is sooner. After the cooling-off period ends, Clearing Members shall not be liable for any deficiency arising from losses or expenses suffered by the Corporation as a result of any event described in clauses (i) through (iv) of Section 5(a) that occurred during the cooling-off period. Each Clearing Member shall have and shall at all times maintain the ability to make good any deficiency described in this Section 6(b) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(c) *Termination During Cooling-Off Period.* After the expiration of the cooling-off period, a Clearing Member will not be liable for replenishment of the Clearing Fund as required by Section 6(a) or assessments as contemplated by Section 6(b), if (i) not later than the last day of the cooling-off period the Clearing Member notifies the Secretary of the Corporation in writing that it is terminating its status as a Clearing Member, (ii) after giving such notice no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case not later than the last day of the cooling off period. A Clearing Member that so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with this Section 6(c), and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.

EXHIBIT 4B

OCC RULES

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THE OPTIONS CLEARING CORPORATION

RULES

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CHAPTER X
Clearing Fund Contributions

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[RESERVED: RULES 1005 – 10~~08~~10]

RULE ~~1009~~1011 – Voluntary Payments

(a) Where, after the default of a Clearing Member, the Corporation determines that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1104 through 1107, 2210 and 2211, the Corporation may~~does~~ not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Corporation will issue a notice (a "**Voluntary Payment Notice**") inviting all non-defaulting Clearing Members to make a payment to the Clearing Fund in addition to amounts required under Rule 1001 (a "Voluntary Payment") to make up for the relevant shortfall. Terms for Voluntary Payments shall be set forth in the Voluntary Payment Notice and shall include, without limitation, the following:

(i) no Clearing Member shall be obliged to make a Voluntary Payment;

(ii) no Voluntary Payment may be withdrawn once made; and

(iii) the Corporation shall have full discretion whether or not to accept a particular Voluntary Payment.

(b) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member), the Corporation shall seek to compensate first from any such recovery the non-defaulting Clearing Members that made voluntary payments, in the amount of each such Clearing Member's voluntary payment. If the amount of any such recovery is less than the amount the Corporation received in voluntary payments, then each non-defaulting Clearing Member shall be compensated from the recovery pro rata according to the relative size of its voluntary payment.

* * *

CHAPTER XI
Suspension of a Clearing Member

* * *

RULE 1111 – Voluntary Tear-Ups and Partial Tear-Ups

(a) (i) The Corporation may notify Clearing Members and provide an opportunity for Clearing Members to voluntarily agree to have positions of a Clearing Member or, with the consent of customers of such Clearing Member, to agree to have each such customer's position, extinguished by the Corporation (a "**Voluntary Tear-Up**") at any time following the suspension or default of a Clearing Member and after the Corporation has attempted one or more auctions pursuant to Rule 1104 or Rule 1106, and after the Corporation has determined that, notwithstanding the availability of any resources remaining under Rules 707, 1001, ~~1009~~1011, 1104 through 1107, 2210 and 2211, the Corporation may~~does~~ not have sufficient resources to satisfy its obligations and liabilities as a result of such default~~,~~. The Corporation will issue a notice (a "**Voluntary Tear-Up Notice**") informing all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear-Up. Terms for Voluntary Tear-Ups shall be set forth in the Voluntary Tear-Up Notice and shall include, without limitation, the following:

(x) no Clearing Member, or customers of a Clearing Member, shall be obliged to participate in a Voluntary Tear-Up; and

(y) the Corporation shall have full discretion whether or not to accept a particular Voluntary Tear-Up offer.

(ii) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) and the amount of such recovery exceeds the amount the Corporation received in voluntary payments, the Corporation shall compensate from such remaining amounts of the recovery the non-defaulting Clearing Members and non-defaulting customers that voluntarily extinguished open positions in the amount of losses, costs or fees directly resulting from the Voluntary Tear-Up, but only after the Corporation has fully compensated non-defaulting Clearing Members that made voluntary payments in the amount of such voluntary payments and only to the extent that such losses, costs and fees can reasonably be determined by the Corporation. If the remaining amount of any such recovery is less than the amount of losses, costs and fees incurred by non-defaulting Clearing Members and non-defaulting customers participated in the Voluntary Tear-Up, then each such non-defaulting Clearing Member and non-defaulting customer shall be compensated pro rata according to the relative size of its incurred losses, costs and fees from the Voluntary Tear-Ups.

(b) If Clearing Member or customer positions of a defaulted Clearing Member remain open ("**Remaining Open Positions**") after the Corporation has attempted one or more auctions pursuant to Rule 1104 or Rule 1106 and after the Corporation has accounted for any positions voluntary extinguished in accordance with subparagraph (a), and the Corporation determines

that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1009, 1104 through 1107, 2210 and 2211, the Corporation may~~does~~ not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Board of Directors of the Corporation may elect to extinguish (i) the Remaining Open Positions, and/or (ii) any related open positions deemed necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions ("**Related Open Positions**"), through a partial tear-up process ("**Partial Tear-Up**"). The Corporation will notify the staff of the SEC and the CFTC of a determination that Partial Tear-Up will apply.

(c) The Risk Committee shall determine the appropriate scope of each Voluntary Tear-Up under subpart (a) of this Rule and Partial Tear-Up under subpart (b) of this Rule. Each determination of the Risk Committee made for purposes of this Rule 1111 shall (i) be based upon then-existing facts and circumstances, (ii) be in furtherance of the integrity of the Corporation and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

(d) For a Partial Tear-Up under subpart (b) of this Rule, the Corporation will issue a notice (a "**Partial Tear-Up Notice**") identifying:

(i) The Remaining Open Positions and any Related Open Positions;

(ii) With respect to each other Clearing Member, the open positions of such Clearing Member and its customers (if any) that will be subject to Partial Tear-Up (the "**Tear-Up Positions**");

(iii) The termination price (the "**Partial Tear-Up Price**") for each Tear-Up Position; and

(iv) The date and time as of which Partial Tear-Up will occur, as determined by the Risk Committee (the "**Partial Tear-Up Time**").

(e) For a Partial Tear-Up under subpart (b) of this Rule, the Corporation will determine and designate the Tear-Up Positions pursuant to the following methodology:

(i) With respect to Remaining Open Positions, the Corporation will designate Tear-Up Positions in the identical Cleared Contracts and Cleared Securities (on the opposite side of the market) and in an aggregate amount equal to that of the Remaining Open Positions. The Corporation will designate Tear-Up Positions in a particular Cleared Contract or Cleared Security only for non-defaulted Clearing Members that have an open position in such Cleared Contract or Cleared Security, whether for their Clearing Member accounts and/or customer accounts~~, and for non-defaulted customers of a defaulted Clearing Member~~, as follows: the Corporation shall designate Tear-Up Positions in the non-defaulted Clearing Member accounts and their~~non-defaulted~~ customer accounts with open positions in the relevant Cleared Contracts and Cleared Securities in such accounts, on a pro rata basis (provided that solely to the extent such pro rata determination would result in creation of a Tear-Up Position which is a fraction of a Cleared Contract or Cleared Security, the Corporation will reallocate such fractional position among non-defaulted Clearing Members on a random basis to avoid such

result). With respect to a Tear-Up Position designated in a ~~non-defaulted~~ customer account of a Clearing Member ~~(including, without limitation, a non-defaulted customer account of a defaulted Clearing Member)~~, the Tear-Up Position shall be allocated on a pro rata basisby the Clearing Member across any customers that have open positions in such Cleared Contract or Cleared Security in such account (for any listed option positions being extinguished, allocation across customer accounts should occur in accordance with such Clearing Member's procedures for allocating exercises and assignments). ~~Where the Corporation has in effect one or more hedging transactions related to the Remaining Open Positions which hedging transactions will not themselves be subject to Partial Tear-Up, the Corporation may offer to assign or transfer such hedging transactions with related Tear-Up Positions, on such basis as the Corporation may reasonably determine.~~

(ii) With respect to Related Open Positions, a Partial Tear-Up would involve extinguishment of all open positions in those Cleared Contracts and Cleared Securities identified by the Risk Committee as within the appropriate scope of the Partial Tear-Up pursuant to this Rule 1111.

(iii) Upon and with effect from the Partial Tear-Up Time, every Tear-Up Position shall be automatically terminated at the Partial Tear-Up Price, without the need for any further step by any party to such Cleared Contract or Cleared Security. Upon such termination, either the Corporation or the relevant Clearing Member, as the case may be, shall be obligated to pay to the other the applicable Partial Tear-Up Price; provided however, that if the Corporation, in its discretion, determines that the resources referenced in subpart (b) of this Rule are inadequate to pay the applicable Partial Tear-Up Price for each position being extinguished in the Partial Tear-Up, the Corporation shall be obligated to pay each relevant Clearing Member a pro rata amount of the applicable Partial Tear-Up Price based on the amount of such resources remaining, and notwithstanding subpart (h) of this Rule the relevant Clearing Member shall have a claim against the Corporation for the value of the difference between the pro rata amount received and the Partial Tear-Up Price. Upon the termination of a Tear-Up Position, the corresponding open position shall be deemed terminated at the Partial Tear-Up Price. Such claim against the Corporation shall be unsecured. With regard to amounts recovered from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) Rules 1011(b) and 1111(a)(ii) shall continue to apply.

(f) For a Partial Tear-Up under subpart (b) of this Rule, in determining the Partial Tear-Up Price for each Tear-Up Position, the Corporation shall exercise its discretion, acting in good faith and in a commercially reasonable manner, in adopting methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models to determine a value for a cleared contract based on the market price of the underlying interest or the market prices of its components. In determining a Partial Tear-Up Price, the Corporation may consider the same information set forth in subpart (c) of Section 27, Article VI of the By-Laws

for determining a close-out amount.

(g) Notwithstanding any provision of this Rule 1111, to the extent that the losses, costs and fees imposed upon non-defaulting Clearing Members and their customers directly resulting from a Partial Tear-Up reasonably can be determined by the Corporation, the Board of Directors may elect to re-allocate such losses, costs and fees among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.

(h) No action or omission by the Corporation pursuant to and in accordance with this Rule 1111 shall constitute a default by the Corporation.

EXHIBIT 5A

By-Laws

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THE OPTIONS CLEARING CORPORATION

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BY-LAWS

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Article VIII - Clearing Fund

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By-Laws, Article VIII – Purpose and Use of Clearing Fund

Maintenance and Purpose of the Clearing Fund
SECTION 1. (a) The Corporation shall maintain a Clearing Fund to which each Clearing Member shall contribute, as provided in this Article VIII, to make good losses suffered by the Corporation, or losses suffered by the Clearing Fund resulting from borrowings pursuant to the authority in Section 5(e) of this Article, (i) as a result of the failure of any Clearing Member to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation, (ii) as a result of the failure of any Clearing Member (including any Appointed Clearing Member) or of CDS to perform its obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued, undertaken, or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable, (iii) as a result of the failure of any Clearing Member to perform any of its obligations to the Corporation in respect of the stock loan and borrow positions of such Clearing Member, (iv) in connection with any liquidation of a Clearing Member's open positions, (v) in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, (vi) as a result of the failure of any Clearing Member to make any other required payment or render any other required performance, or (vii) as a result of the failure of any bank or securities or commodities clearing organization to perform its obligations to the Corporation for reasons specified in Section 5 of this Article, or (viii) as a result of a borrowing by the Corporation for liquidity needs for same day settlement pursuant to the authority in Section 5(e) of this Article. Notwithstanding the foregoing, in the event that the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rule 1111, the Clearing Fund may be used to provide compensation to non-defaulting Clearing Members and their customers as a means of re-allocating the losses, costs and fees imposed upon them as a result of such Voluntary Tear-Up or Partial Tear-Up, but only to the extent that such losses, costs and fees can be reasonably determined by the Corporation.

* * *

Application of the Clearing Fund
SECTION 5. (a) If:

(i) any Clearing Member shall fail to discharge duly any obligation on or arising from any confirmed trade accepted by the Corporation,
(ii) any Clearing Member, (including any Appointed Clearing Member) or of CDS shall fail to perform any obligations (including its obligations to the correspondent clearing corporation) under or arising from any exercised or assigned option contract or any other contract or obligation issued or guaranteed by the Corporation or in respect of which the Corporation is otherwise liable,
(iii) any Clearing Member shall fail to perform any obligation to the Corporation in respect of the stock loan and borrow positions of such Clearing Member,
(iv) the Corporation shall suffer any loss or expense upon any liquidation of a Clearing Member's open positions,
(v) the Corporation shall suffer any loss or expense in connection with protective transactions effected for the account of the Corporation pursuant to Chapter XI of the Rules, or
(vi) any Clearing Member shall fail to make any other payment or render any other performance required under the By-Laws or the Rules,

then the Corporation shall (after appropriate application of other funds in the accounts of the Clearing Member) apply the Clearing Member's Clearing Fund contribution to the discharge of such obligation, the reimbursement of such loss or expense, or the making of such payment or the funding of such performance. If the sum of all such obligations, losses or expenses, and payments exceeds the sum of the amount of the Clearing Member's total Clearing Fund contribution and the amount of the other funds of the Clearing Member available to the Corporation, and if the Clearing Member fails to pay the Corporation the amount of any such deficiency on demand, the amount of the deficiency shall be paid out of the Clearing Fund and charged on a proportionate basis against all other Clearing Members' computed contributions as fixed at the time, but the Clearing Member who failed to pay the deficiency shall remain liable to the Corporation for the full amount of such deficiency until repayment thereof by such Clearing Member, or

(vii) the Corporation performs a Voluntary Tear-Up or a Partial Tear-Up pursuant to Rue 1111,

then, the Corporation may elect to proportionately charge the Clearing Fund in the amount(s) the Corporation reasonably determines necessary to compensate non-defaulting Clearing Members and their customers for the losses, costs or fees imposed upon them as a direct result of such Voluntary Tear-Up or Partial Tear-Up, but only to the extent that such losses, costs and fees can be reasonably determined by the

Corporation.

* * *

Making Good of Charges to the Clearing Fund
SECTION 6.

* * *

(a) *Making Good of Charges to the Clearing Fund.* Whenever an amount is paid out of the Clearing Fund contribution of a Clearing Member, whether by proportionate charge or otherwise, such Clearing Member shall be liable to promptly make good the deficiency in its required contribution resulting from such payment by replenishment of the Clearing Fund. ~~Notwithstanding the foregoing and except as provided for below, if the payment is made as a result of a proportionate charge, a Clearing Member will not be liable to make good more than an additional 100% of the amount of its then required contribution if (i) within five business days following such proportionate charge the Clearing Member notifies the Corporation in writing that it is terminating its status as a Clearing Member, (ii) no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case as promptly as practicable after the giving of such notice; provided that a Clearing Member which so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with the preceding sentence, and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.~~ Each Clearing Member shall have and shall at all times maintain the ability to ~~make good~~ replenish any deficiency described in this Section 6(a) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(b) *Cooling-Off Period; Assessments.* Notwithstanding anything in Section 6 and except as provided for below, if an amount is paid out of the Clearing Fund as a result of a proportionate charge resulting from any of the events described in clauses (i) through (iv) of Section 5(a), then starting on the date of such proportionate charge there shall automatically commence a cooling-off period during which a Clearing Member will not be liable to make good more than an additional 200% of the amount of its then required contribution (for definitional purposes, amounts in excess of a Clearing Member's then required contribution shall be "assessments").

The cooling-off period shall be fifteen consecutive calendar days from the date of such proportionate charge; provided however, that if one or more subsequent events described in clauses (i) through (iv) of Section 5(a) occur during the fifteen-day period and result in one or more proportionate charges against the Clearing Fund, the cooling-off period shall be extended through (i) the fifteenth calendar day from the date of the most recent proportionate charge resulting from the subsequent event, or (ii) the twentieth calendar day from the date of the initial proportionate charge, whichever is sooner. After the cooling-off period ends, Clearing Members shall not be liable for any deficiency arising from losses or expenses suffered by the Corporation as a result of any event described in clauses (i) through (iv) of Section 5(a) that occurred during the cooling-off period. Each Clearing Member shall have and shall at all times maintain the ability to make good any deficiency described in this Section 6(b) by 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the first business day following the day on which the Corporation notifies the Clearing Member of such deficiency.

(c) *Termination During Cooling-Off Period.* After the expiration of the cooling-off period, a Clearing Member will not be liable for replenishment of the Clearing Fund as required by Section 6(a) or assessments as contemplated by Section 6(b), if (i) not later than the last day of the cooling-off period the Clearing Member notifies the Secretary of the Corporation in writing that it is terminating its status as a Clearing Member, (ii) after giving such notice no opening purchase transaction or opening writing transaction is submitted for clearance through any of the Clearing Member's accounts and (if the Clearing Member is a Market Loan Clearing Member or a Hedge Clearing Member) no Stock Loan is initiated through any of the Clearing Member's accounts after the giving of such notice, and (iii) the Clearing Member closes out or transfers all of its open positions with the Corporation, in each case not later than the last day of the cooling off period. A Clearing Member that so terminates its status as a Clearing Member shall be ineligible to be readmitted to such membership unless the Clearing Member agrees to such reimbursement of the persons who were Clearing Members at the time of such termination as the Board of Directors deems fair and equitable in the circumstances. In the event a Clearing Member notifies the Corporation of its intent to terminate its status as a Clearing Member in accordance with this Section 6(c), and such Clearing Member's computed contribution is less than its minimum required contribution, then the Clearing Member shall also make good 100% of the amount equal to its minimum required contribution less its computed contribution to the Clearing Fund.

EXHIBIT 5B

OCC RULES

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THE OPTIONS CLEARING CORPORATION

RULES

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CHAPTER X
Clearing Fund Contributions

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[RESERVED: RULES 1005 – 1010]

RULE 1011 – Voluntary Payments

(a) Where, after the default of a Clearing Member, the Corporation determines that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1104 through 1107, 2210 and 2211, the Corporation may not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Corporation will issue a notice (a "**Voluntary Payment Notice**") inviting all non-defaulting Clearing Members to make a payment to the Clearing Fund in addition to amounts required under Rule 1001 (a "Voluntary Payment") to make up for the relevant shortfall. Terms for Voluntary Payments shall be set forth in the Voluntary Payment Notice and shall include, without limitation, the following:

(i) no Clearing Member shall be obliged to make a Voluntary Payment;

(ii) no Voluntary Payment may be withdrawn once made; and

(iii) the Corporation shall have full discretion whether or not to accept a particular Voluntary Payment.

(b) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member), the Corporation shall seek to compensate first from any such recovery the non-defaulting Clearing Members that made voluntary payments, in the amount of each such Clearing Member's voluntary payment. If the amount of any such recovery is less than the amount the Corporation received in voluntary payments, then each non-defaulting Clearing Member shall be compensated from the recovery pro rata according to the relative size of its voluntary payment.

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CHAPTER XI
Suspension of a Clearing Member

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RULE 1111 – Voluntary Tear-Ups and Partial Tear-Ups

(a) (i) The Corporation may notify Clearing Members and provide an opportunity for Clearing Members to voluntarily agree to have positions of a Clearing Member or, with the consent of customers of such Clearing Member, to agree to have each such customer's position, extinguished by the Corporation (a "**Voluntary Tear-Up**") at any time following the suspension or default of a Clearing Member and after the Corporation has attempted one or more auctions pursuant to Rule 1104 or Rule 1106, and after the Corporation has determined that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1011, 1104 through 1107, 2210 and 2211, the Corporation may not have sufficient resources to satisfy its obligations and liabilities as a result of such default. The Corporation will issue a notice (a "**Voluntary Tear-Up Notice**") informing all non-defaulting Clearing Members of the opportunity to participate in a Voluntary Tear-Up. Terms for Voluntary Tear-Ups shall be set forth in the Voluntary Tear-Up Notice and shall include, without limitation, the following:

(x) no Clearing Member, or customers of a Clearing Member, shall be obliged to participate in a Voluntary Tear-Up; and

(y) the Corporation shall have full discretion whether or not to accept a particular Voluntary Tear-Up offer.

(ii) If the Corporation successfully recovers from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) and the amount of such recovery exceeds the amount the Corporation received in voluntary payments, the Corporation shall compensate from such remaining amounts of the recovery the non-defaulting Clearing Members and non-defaulting customers that voluntarily extinguished open positions in the amount of losses, costs or fees directly resulting from the Voluntary Tear-Up, but only after the Corporation has fully compensated non-defaulting Clearing Members that made voluntary payments in the amount of such voluntary payments and only to the extent that such losses, costs and fees can reasonably be determined by the Corporation. If the remaining amount of any such recovery is less than the amount of losses, costs and fees incurred by non-defaulting Clearing Members and non-defaulting customers participated in the Voluntary Tear-Up, then each such non-defaulting Clearing Member and non-defaulting customer shall be compensated pro rata according to the relative size of its incurred losses, costs and fees from the Voluntary Tear-Ups.

(b) If Clearing Member or customer positions of a defaulted Clearing Member remain open ("**Remaining Open Positions**") after the Corporation has attempted one or more auctions pursuant to Rule 1104 or Rule 1106 and after the Corporation has accounted for any positions voluntary extinguished in accordance with subparagraph (a), and the Corporation determines that, notwithstanding the availability of any resources remaining under Rules 707, 1001, 1009, 1104 through 1107, 2210 and 2211, the Corporation may not have sufficient resources to satisfy its obligations and liabilities as a result of such default, the Board of Directors of the Corporation

may elect to extinguish (i) the Remaining Open Positions, and/or (ii) any related open positions deemed necessary to mitigate further disruptions to the markets affected by the Remaining Open Positions ("**Related Open Positions**"), through a partial tear-up process ("**Partial Tear-Up**"). The Corporation will notify the staff of the SEC and the CFTC of a determination that Partial Tear-Up will apply.

(c) The Risk Committee shall determine the appropriate scope of each Voluntary Tear-Up under subpart (a) of this Rule and Partial Tear-Up under subpart (b) of this Rule. Each determination of the Risk Committee made for purposes of this Rule 1111 shall (i) be based upon then-existing facts and circumstances, (ii) be in furtherance of the integrity of the Corporation and the stability of the financial system, and (iii) take into consideration the legitimate interests of Clearing Members and market participants.

(d) For a Partial Tear-Up under subpart (b) of this Rule, the Corporation will issue a notice (a "**Partial Tear-Up Notice**") identifying:

(i) The Remaining Open Positions and any Related Open Positions;

(ii) With respect to each other Clearing Member, the open positions of such Clearing Member and its customers (if any) that will be subject to Partial Tear-Up (the "**Tear-Up Positions**");

(iii) The termination price (the "**Partial Tear-Up Price**") for each Tear-Up Position; and

(iv) The date and time as of which Partial Tear-Up will occur, as determined by the Risk Committee (the "**Partial Tear-Up Time**").

(e) For a Partial Tear-Up under subpart (b) of this Rule, the Corporation will determine and designate the Tear-Up Positions pursuant to the following methodology:

(i) With respect to Remaining Open Positions, the Corporation will designate Tear-Up Positions in the identical Cleared Contracts and Cleared Securities (on the opposite side of the market) and in an aggregate amount equal to that of the Remaining Open Positions. The Corporation will designate Tear-Up Positions in a particular Cleared Contract or Cleared Security only for non-defaulted Clearing Members that have an open position in such Cleared Contract or Cleared Security, whether for their Clearing Member accounts and/or customer accounts, as follows: the Corporation shall designate Tear-Up Positions in the non-defaulted Clearing Member accounts and their customer accounts with open positions in the relevant Cleared Contracts and Cleared Securities in such accounts, on a pro rata basis (provided that solely to the extent such pro rata determination would result in creation of a Tear-Up Position which is a fraction of a Cleared Contract or Cleared Security, the Corporation will reallocate such fractional position among non-defaulted Clearing Members on a random basis to avoid such result). With respect to a Tear-Up Position designated in a customer account of a Clearing Member, the Tear-Up Position shall be allocated on a pro rata basis by the Clearing Member across any customers that have open positions in such Cleared Contract or Cleared Security in such account (for any listed option positions being

extinguished, allocation across customer accounts should occur in accordance with such Clearing Member's procedures for allocating exercises and assignments).

(ii) With respect to Related Open Positions, a Partial Tear-Up would involve extinguishment of all open positions in those Cleared Contracts and Cleared Securities identified by the Risk Committee as within the appropriate scope of the Partial Tear-Up pursuant to this Rule 1111.

(iii) Upon and with effect from the Partial Tear-Up Time, every Tear-Up Position shall be automatically terminated at the Partial Tear-Up Price, without the need for any further step by any party to such Cleared Contract or Cleared Security. Upon such termination, either the Corporation or the relevant Clearing Member, as the case may be, shall be obligated to pay to the other the applicable Partial Tear-Up Price; provided however, that if the Corporation, in its discretion, determines that the resources referenced in subpart (b) of this Rule are inadequate to pay the applicable Partial Tear-Up Price for each position being extinguished in the Partial Tear-Up, the Corporation shall be obligated to pay each relevant Clearing Member a pro rata amount of the applicable Partial Tear-Up Price based on the amount of such resources remaining, and notwithstanding subpart (h) of this Rule the relevant Clearing Member shall have a claim against the Corporation for the value of the difference between the pro rata amount received and the Partial Tear-Up Price. Upon the termination of a Tear-Up Position, the corresponding open position shall be deemed terminated at the Partial Tear-Up Price. Such claim against the Corporation shall be unsecured. With regard to amounts recovered from a suspended or defaulted Clearing Member (or from the estate of a suspended or defaulted Clearing Member) Rules 1011(b) and 1111(a)(ii) shall continue to apply.

(f) For a Partial Tear-Up under subpart (b) of this Rule, in determining the Partial Tear-Up Price for each Tear-Up Position, the Corporation shall exercise its discretion, acting in good faith and in a commercially reasonable manner, in adopting methods of valuation expected to produce reasonably accurate substitutes for the values that would have been obtained from the relevant market if it were operating normally, including but not limited to the use of pricing models to determine a value for a cleared contract based on the market price of the underlying interest or the market prices of its components. In determining a Partial Tear-Up Price, the Corporation may consider the same information set forth in subpart (c) of Section 27, Article VI of the By-Laws for determining a close-out amount.

(g) Notwithstanding any provision of this Rule 1111, to the extent that the losses, costs and fees imposed upon non-defaulting Clearing Members and their customers directly resulting from a Partial Tear-Up reasonably can be determined by the Corporation, the Board of Directors may elect to re-allocate such losses, costs and fees among all non-defaulting Clearing Members through a special charge to all non-defaulting Clearing Members in an amount corresponding to each such non-defaulting Clearing Member's proportionate share of the variable amount of the Clearing Fund at the time such Partial Tear-Up is conducted.

(h) No action or omission by the Corporation pursuant to and in accordance with this Rule 1111 shall constitute a default by the Corporation.