

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-58258; File No. SR-OCC-2008-12)

July 30, 2008

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval of a Proposed Rule Change Relating to Cross-Margining

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934,<sup>1</sup> notice is hereby given that on June 10, 2008, 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 and order to solicit comments on the proposed rule change from interested persons and to grant accelerated approval of the proposal.

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

The proposed rule change would amend OCC Rule 705 to add shares of money market funds as a form of collateral that may be deposited and recognized with respect to cross-margin (“XM”) accounts. In addition, the proposed rule change revises the cross-margining agreement between OCC and the Chicago Mercantile Exchange, Inc., (“CME”) to reflect the allowance of money market fund shares as acceptable collateral.

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

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. OCC has prepared summaries, set forth in sections A, B, and C below, of the most

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

significant aspects of such statements.

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

OCC Rule 705 specifies the forms of collateral that may be deposited with respect to cross-margin ("XM") accounts to meet required margin. Such forms of collateral currently include cash, government securities, government sponsored debt securities, letters of credit, and, if mutually acceptable to the XM clearing organizations, common stock. OCC staff regularly reviews these forms of collateral with an approach of determining a suitable balance between its clearing members' desire for a diverse combination of readily-available and cost-effective financial instruments and OCC's interest to access financial instruments that are relatively stable in value and easily converted to cash. Based on such a review, OCC is proposing to expand the forms of margin collateral acceptable for XM accounts to include shares in money market funds ("MMF Shares").

MMF Shares have been increasingly used to collateralize accounts at futures clearinghouses following the December 2000 amendments to Commodity Futures Trading Commission Regulation 1.25, which allow a futures commission merchant or a derivatives clearing organization to invest segregated funds in money market funds.<sup>2</sup> OCC has accepted MMF Shares as collateral for several years.<sup>3</sup> XM participants therefore desire to hypothecate shares in such funds as margin for their XM accounts as well.

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<sup>2</sup> Rules Relating to Intermediaries of Commodity Interest Transactions, 65 FR 77993 (Dec. 13, 2000). OCC estimates that MMF shares account for approximately 30% of the performance bond deposits at the two largest futures clearinghouses, CME and the New York Mercantile Exchange.

<sup>3</sup> Securities Exchange Act Release No. 47599 (Mar. 31, 2003), 68 FR 16849 (Apr. 7, 2003).

Under the rule change, the underlying money market funds will be required to continuously meet the qualification standards of both OCC and the participating Commodity Clearing Organization (“CCO”) and will be valued at the lowest value given to MMF Shares under OCC’s or the CCO’s rules. Initially, OCC proposes to permit MMF Shares to be deposited as collateral in connection with its XM program with CME.<sup>4</sup> Operationally, the shares will be transferred into an account held with the fund issuer that will be jointly controlled by OCC and CME for purposes of perfecting their security interest in deposited shares.

Clearing members will request the purchase of money market mutual fund shares from either OCC or CME. The shares will be jointly purchased by the clearinghouses using the funds of the requesting clearing member(s) that have been drafted from the bank account established in respect of the applicable cross-margining account (i.e., proprietary or segregated funds account). These shares will then be deposited in an account jointly controlled by OCC and the CME, and the clearing member(s) will receive margin credit for the collateral value less the applicable haircut of the shares purchased. Shares will be redeemed for cash from the fund issuer upon the instruction of either (i) the clearing member(s), with the proceeds being returned to the appropriate bank account, or (ii) the clearing organizations, upon the suspension of the clearing

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<sup>4</sup> Presently, OCC maintains XM programs with the CME, The Clearing Corporation (“CCorp”) and ICE Clear U.S., Inc. (“ICE Clear”). However, there is currently no clearing member participating in the OCC/CCorp XM program. If that XM program becomes active again in the future and there is interest in MMF Shares as a form of margin collateral, OCC would then file with the Commission a proposed rule change to amend the OCC/CCorp XM agreement to include MMF Shares. OCC and ICE Clear have determined to defer including MMF Shares in their XM program until the clearing organizations have determined that there is clearing member interest in using such collateral. Because MMF Shares will not be an allowable form of collateral in all OCC XM programs, Rule 705 has been amended to provide that forms of margin collateral must be mutually acceptable to OCC and each participating CCO. This requirement is currently applied to deposits of common stock.

member(s) with proceeds being deposited into the appropriate liquidating settlement account for distribution in accordance with the XM agreement between OCC and CME.

To permit the use of MMF Shares as a form of margin once all necessary regulatory approvals are obtained, OCC and CME have amended and restated their Cross-Margining Agreement (“Original Agreement”), which also has been updated to reflect the withdrawal in 2004 of the New York Clearing Corporation (“NYCC”) as a party thereto.<sup>5</sup> With the elimination of NYCC as a party to the Original Agreement, the New Agreement accommodates the current OCC/CME bilateral cross-margining program but no longer provides for a trilateral cross-margining program. Other significant differences between the Original Agreement and the New Agreement are as follows.

Section 1 of the New Agreement contains definitional terms. Section 1 has been modified to add a definitional term for MMF Shares (Section 1(q)) and to revise other definitions to reflect the bilateral nature of the OCC/CME XM program. As defined, MMF Shares refer to shares in a money market fund that meet the requirements established under OCC’s and CME’s rules.<sup>6</sup> References to NYCC have been eliminated from all the definition provisions and throughout the cross-margining agreement. The term “Carrying Clearing Organization” has been

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<sup>5</sup> The Amended and Restated Cross-Margining Agreement (“New Agreement”) is attached to OCC’s rule filing as Exhibit 5A. From 1997 to 2004, NYCC (now known as ICE Clear, U.S., Inc.) participated in a trilateral XM program with OCC and CME. See Securities Exchange Act Release No. 38584 (May 8, 1997), 62 FR 26602 (May 14, 1997) (order approving a cross-margining agreement among OCC, CME, and the Commodity Clearing Corporation). The agreement governing this trilateral XM also sets forth the terms and conditions governing the current bilateral program between OCC and CME.

<sup>6</sup> OCC’s criteria for accepting deposits of MMF shares as margin are set forth in OCC Rule 604(b)(3). This rule, among other things, establishes concentration, control, and valuation standards governing money market fund shares.

eliminated as unnecessary. The terms “Pair of Non-Proprietary X-M Accounts” and “Pair of X-M Accounts,” respectively, have replaced the terms “Sets of Non-Proprietary X-M Accounts” and “Sets of Proprietary X-M Accounts” (Sections 1(s) and (w)) in order to reflect the bilateral nature of the OCC/CME XM program. Changes reflecting the deletion of the terms “Carrying Clearing Organization,” “Sets of Non-Proprietary X-M Accounts,” and “Sets of Proprietary X-M Accounts” have been made throughout the New Agreement. The definition of “Market Professional” (Section 1(p)) has been revised to eliminate references to NYFE members, which is the former name of the market for which NYCC provides clearing services. Other than referencing pairs of XM accounts, as applicable, no substantive changes have been made to Sections 2, 3, and 4. Section 5, which relates to the calculation of margin, is also substantively unchanged other than the deletion of an unnecessary provision regarding NYCC’s election to use the margin calculation produced by the designated clearing organization’s margin system.

Section 6 relates to the forms and method of holding initial margin. As revised, Section 6 permits the deposit of MMF Shares as a form of initial margin and requires such shares to be held for the joint benefit of the clearing organizations on the books of the issuing fund or its agent or in such other manner as mutually agreed upon by the clearing organizations.<sup>7</sup> Unnecessary references to the CME acting as NYCC’s agent for the purpose of executing instructions to release forms of collateral from deposit have been deleted.<sup>8</sup>

Section 7 describes daily settlement procedures, which are subject to joint coordination and authorization. References to the CME acting as NYCC’s agent for purposes of authorizing

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<sup>7</sup> Proposed Section 6(a) and (b).

<sup>8</sup> Id.

fund transfers and other provisions relating to trilateral cross-margining have been deleted.<sup>9</sup> The time at which the Clearing Organizations are to share position and other related information to the XM accounts has been advanced to 1:00 a.m. (Central Time) from 3:00 a.m. (Central Time).<sup>10</sup>

Section 8 concerns the suspension and liquidation of one or more XM clearing members. Section 8 has been modified to eliminate the loss or surplus sharing provisions that were effective in the event NYCC was a Carrying Clearing Organization in respect of an XM account, leaving in place terms that provide for equal loss or surplus sharing subject to the limitation that sharing in a surplus by a clearing organization for purposes of covering its other losses experienced is capped at an amount equal to such other losses.<sup>11</sup> In addition, Section 8 has been amended to provide that OCC and CME would demand immediate payment of any letter of credit deposited as margin unless both agreed not to take such action. Provisions that permitted the clearing organizations to defer drawing on a letter of credit on receipt of satisfactory written assurances from the issuing bank extending its irrevocable commitment under the letter have been deleted in favor of the formulation described in the preceding sentence.<sup>12</sup> No substantive changes have been made to Sections 9 through 12.

Section 13 concerns the termination of the New Agreement. Provisions that specifically

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<sup>9</sup> Proposed Section 7(a) and (b).

<sup>10</sup> Proposed Section 7(d).

<sup>11</sup> Proposed Section 8(d) and (f).

<sup>12</sup> Proposed Section 8(c).

related to termination by NYCC have been deleted.<sup>13</sup> Proposed Section 13, paragraph (d), which concerns the treatment of collateral deposited as margin on termination, has been modified to provide for the return of deposited MMF Shares to the depositing clearing member. No substantive changes have been made to Section 14. Section 15, which addresses information sharing, has been modified to reflect the OCC/ICE Clear XM Agreement other than as it relates to use of a recorded phone line for providing notices pursuant to Section 15.<sup>14</sup> No substantive changes have been made to Sections 16 and 17. OCC states that any other changes made to the XM Agreement not specifically described above are not material in nature and therefore were not described in this narrative of the proposed rule change.

In addition to Exhibit 5A, the following are attached as exhibits to the proposed rule change filing:

<b>EXHIBIT</b>	<b>NAME</b>
EXHIBIT 5B	Proprietary Cross-Margin Account Agreement and Security Agreement (Joint Clearing Member)
EXHIBIT 5C	Proprietary Cross-Margin Account Agreement and Security Agreement (Affiliated Clearing Members)
EXHIBIT 5D	Non-Proprietary Cross-Margin Account Agreement and Security Agreement (Joint Clearing Member)
EXHIBIT 5E	Non-Proprietary Cross-Margin Account Agreement and Security Agreement (Affiliated Clearing Members)

<sup>13</sup> Proposed Section 13(a), (b), and (c).

<sup>14</sup> See Securities Exchange Act Release No. 57118 (Jan. 9, 2008), 73 FR 2970 (Jan. 16, 2008) (order approving the cross-margining agreement between OCC and ICE Clear U.S., Inc.).

EXHIBIT 5F	Market Professional's Agreement for Cross-Margining (Joint Clearing Member)
EXHIBIT 5G	Market Professional's Agreement for Cross-Margining (Affiliated Clearing Members)

These forms of agreements have been slightly modified from the forms currently used in OCC/CME cross-margining. Modifications include: (i) deleting provisions and terminology (e.g., "Carrying Clearing Organization") that were applicable to trilateral cross-margining, (ii) reflecting the definition of "market professional" as used in the New Agreement, and (iii) eliminating the requirement that clearing members and market professionals furnish the clearing organizations with financing statements relating to positions, collateral and property maintained with respect to accounts subject to cross-margining. The adoption by all 50 states of revisions to Articles 8 and 9 of the Uniform Commercial Code ("UCC") has eliminated the need to obtain financing statements that were required to perfect security interests in futures and options under earlier versions of those Articles.

OCC states that the proposed rule change is consistent with the purposes and requirements of Section 17A of the Act<sup>15</sup> because it updates the (i) forms of collateral that are currently permitted to be deposited with respect to XM accounts under the OCC/CME cross-margining program to include MMF Shares, a form of collateral currently permitted by both clearing organizations to be deposited with respect to accounts other than cross-margin accounts; and (ii) documents used in connection with OCC/CME cross-margining. Cross-margining enhances the safety of the clearing system while providing lower clearing margin costs to

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



participants. Expanding acceptable collateral for cross-margin accounts should encourage their use and is therefore beneficial to the clearing system and its participants. Updating the documents governing the OCC/CME cross-margining program provides greater clarity and certainty with respect to the program's operation. Moreover, OCC states that the proposed rule change is not inconsistent with OCC's by-laws and rules, including any proposed to be amended.

B. Self-Regulatory Organization's Statement on Burden on Competition

OCC does not believe that the proposed rule change would impose any burden on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments were not and are not intended to be solicited with respect to the proposed rule change and none have been received.

III. Commission's Findings and Order Granted Accelerated Approval of the Proposed Rule Change

Section 17A(b)(3)(F) of the Act<sup>16</sup> requires the rules of a clearing agency to assure the safeguarding of securities and funds that are in the custody or control of the clearing agency or for which it is responsible. The Commission believes the proposal is consistent with this requirements because money market fund shares are already an acceptable form of margin asset that may be deposited at OCC and are subject to OCC's prudent controls. Moreover, the use of money market fund shares for cross-margining purposes should further diversify the portfolio of assets that may be deposited to collateralize cross-margin accounts thereby enhancing OCC's ability to access financial instruments that are relatively liquid and stable in value. Accordingly,

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<sup>16</sup> 15 U.S.C. 78q-1(b)(3)(F).

the proposed rule change should not affect OCC's ability to assure the safeguarding of securities and funds in its custody or control or for which it is responsible.

Pursuant to Section 19(b)(2) of the Act,<sup>17</sup> OCC has requested the Commission to approve the proposed rule change prior to the thirtieth day after the date of publication of notice of the filing. The Commission finds good cause for approving because the new OCC/CME cross-margining program is based on and is substantially similar to other cross-margining programs that the Commission has approved and because such approval will allow OCC to implement the new program in late July pursuant to its implementation schedule.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to [rule-comment@sec.gov](mailto:rule-comment@sec.gov). Please include File No. SR-OCC-2008-12 on the subject line.

##### Paper Comments:

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

All submissions should refer to File No. SR-OCC-2008-12. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments

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<sup>17</sup> 15 U.S.C. 78s(b)(2).

more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. to 3:00 p.m. Copies of such filing also will be available for inspection and copying at OCC's principal office and on OCC's Web site at [http://www.theocc.com/publications/rules/proposed\\_changes/proposed\\_changes.jsp](http://www.theocc.com/publications/rules/proposed_changes/proposed_changes.jsp). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. OCC-2008-12 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

#### V. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular Section 17A of the Act<sup>18</sup> and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>19</sup> that the

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<sup>18</sup> 15 U.S.C. 78q-1.

<sup>19</sup> 15 U.S.C. 19s(b)(2).

proposed rule change (SR-OCC-2008-12) be, and it hereby is, approved on an accelerated basis.<sup>20</sup>

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.<sup>21</sup>

Florence E. Harmon  
Acting Secretary

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<sup>20</sup> In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>21</sup> 17 CFR 200.30-3(a)(12).