SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-58586; File No. SR-OCC-2008-16)

September 18, 2008

Self-Regulatory Organizations; The Options Clearing Corporation; Order Granting Approval of a Proposed Rule Change Relating to the Cash Dividend Threshold

I. Introduction

On July 24, 2008, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-OCC-2008-16 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").[1] Notice of the proposal was published in the Federal Register on August 19, 2008.[2] No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description

The purpose of the proposed rule change is to mitigate inconsistencies that may result under the current policy for adjusting stock option contracts. In February 2007, the Commission approved rule change SR-OCC-2006-01, which amended Section 11A of Article VI of the OCC By-Laws governing adjustments to options as a result of cash dividends or distributions.[3] Under the new adjustment policy, cash dividends paid by a company other than pursuant to a policy or practice of paying dividends on a quarterly or other regular basis would be deemed "special" and would normally trigger a contract adjustment provided the value of the adjustment is at least $12.50 per option contract. This new adjustment policy will become effective for cash dividends announced on or after February 1, 2009.

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

2 Securities Exchange Act Release No. 58353 (August 13, 2008), 73 FR 48423.

3 Securities Exchange Act Release No. 55258 (February 8, 2007), 72 FR 7701 (February 16, 2007).

However, certain inconsistencies may result when the threshold of "$12.50 per option contract" is applied to all options on the affected underlying security. For example, if a $.10 special cash dividend is declared, the standard-size 100 share option would not be adjusted (because the value is less than $12.50). However, a previously adjusted 150 share option (reflecting a 3 for 2 split) would be adjusted (because the value is $15 per contract). Adjusting some but not all options of the same class in response to the same dividend event, especially if the 100 share option is not adjusted, could be confusing to investors. OCC's Securities Committee (consisting of representatives of each of the options exchanges and OCC) determined that this potential confusion should be avoided.

OCC considered modifying the threshold to specify $.125 per share instead of $12.50 per contract. This approach would address all standard-size (100 share) contracts that currently exist plus adjusted contracts that come into existence in response to splits, etc. However, exchanges have proposed to introduce "maxi" size contracts. Applying the same per share threshold to a 1,000 and 100 share option could sometimes result in significant value being left on the table in the case of the 1,000 share option. Taking the same example of a $.10 per share special dividend, neither option would be adjusted if the threshold were $.125 per share. This would result in a loss of only $10 per contract for the 100 share option, but the loss would be $100 per contract for the 1,000 share option. For this reason, a per share threshold is not being proposed.

Greater consistency across contracts of varying sizes can be achieved by retaining the $12.50 per contract threshold in all cases but adding a qualification specifying that if a corresponding standard-size contract exists on the underlying security, previously adjusted contracts will be adjusted only if the corresponding standard-size contract is also adjusted. For example, if a 100 share option and a 150 share option (previously adjusted for a 3 for 2 split) exist, the 150 share option would be adjusted for a special cash dividend only if the 100 share standard option would also be adjusted for that dividend. Stated differently, OCC will refer back to the preadjustment standard-size option (if any exist) in deciding whether or not to adjust a previously adjusted option. Thus a 150 share option that was derived from a 100 share option as a result of a 3 for 2 split will be referred back to the 100 share option. A 1,500 share option (previously adjusted for a 3 for 2 split) will be referred back to the 1,000 share option (the "standard" size option for a “maxi” contract). Thus, the qualification specifies “only if the corresponding standard-size option contract is also adjusted.”

This qualification achieves greater consistency because in most cases all contracts on the same underlying security would be adjusted if the 100 share contract is adjusted. The qualification also would allow a 1,000 share “standard” contract to be adjusted independently of a 100 share contract. Also, it could happen that an adjusted contract exists but *not* the corresponding standard contract, or a contract calling for delivery of fewer than 100 shares may exist (e.g., as a result of a spinoff adjustment). In these cases, the qualification would be inapplicable and a straightforward application of the $12.50 threshold would determine whether an adjustment would be made. The following are examples of the qualification to the $12.50 per contract threshold.

(A) If a corresponding standard size contract exists:

Shares	Contract	$.09 Dividend ($Value)	Adjust?	$.13 Dividend ($Value)	Adjust?
100	Standard	9.00	NO	13.00	YES
133	4/3 split	11.97	NO	17.29	YES
150	3/2 split	13.50	NO	19.50	YES
10	Spinoff	0.90	NO	1.30	NO
177	Merger	15.93	NO	23.01	YES
1000	Standard	90.00	YES	130.00	YES
1500	3/2 split	135.00	YES	195	YES

Shares	Contract	$.02 Dividend ($Value)	Adjust?	$.01 Dividend ($Value)	Adjust?
100	Standard	2.00	NO	1.00	NO
133	4/3 split	2.66	NO	1.33	NO
150	3/2 split	3.00	NO	1.50	NO
10	Spinoff	0.20	NO	0.10	NO
177	Merger	3.54	NO	1.77	NO
1000	Standard	20.00	YES	10.00	NO
1500	3/2 split	30.00	YES	15.00	NO

(B) If the 100 share standard size contract does not exist:

Shares	Option	$.09 Dividend ($Value)	Adjust?	$.13 Dividend ($Value)	Adjust?
133	4/3 split	11.97	NO	17.29	YES
150	3/2 split	13.50	YES	19.50	YES
10	Spinoff	0.90	NO	1.30	NO
177	Merger	15.93	YES	23.01	YES
1000	Standard	90.00	YES	130.00	YES
1500	3/2 split	135.00	YES	195	YES

The new adjustment policy approved in File No. SR-OCC-2006-01 will take effect beginning with dividends announced on and after February 1, 2009. OCC intends this proposed rule change to take effect at the same time, but these changes will not be implemented until the exchanges have conducted appropriate educational efforts and definitive copies of an appropriate supplement to the options disclosure document, Characteristics and Risks of Standardized Options, are available for distribution.

III. Discussion

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securiteis transactions.[4] The Commission finds the proposed rule change to be consistent with this requirement because it should reduce inconsistencies in the adjustment of stock option contracts. As a result, OCC's proposed rule change should promote the prompt and accurate clearance and settlement of securities transactions.

IV. 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 and the rules and regulations thereunder.

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4 15 U.S.C. 78q-1(b)(3)(F).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-OCC-2008-16) be and hereby is approved.[5]

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.[6]

J. Lynn Talyor
Assistant Secretary

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[5] 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).

[6] 17 CFR 200.30-3(a)(12).