

August 30, 2012

VIA ELECTRONIC MAIL

David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Rule Filing SR-OCC-2012-14 Rule Certification

Dear Secretary Stawick:

Pursuant to Section 5c(c)(1) of the Commodity Exchange Act, as amended (“Act”), and Commodity Futures Trading Commission Regulation (“CFTC”) 40.6, enclosed is a copy of the above-referenced rule filing submitted by The Options Clearing Corporation (“OCC”). The date of implementation of the rule is the later of 10 business days following receipt of the rule filing by the CFTC hereof or the date the proposed rule is approved by the Securities and Exchange Commission (the “SEC”) or otherwise becomes effective under the Securities Exchange Act of 1934 (the “Exchange Act”). This rule filing has been, or is concurrently being, submitted to the Securities and Exchange Commission (the “SEC”) under the Securities Exchange Act of 1934 (the “Exchange Act”). The text of the rule is set forth at Item 1 of the enclosed 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 and advance notice is to allow OCC to provide central clearing of OTC index options on the S&P 500 Index. The proposed rule change replaces a previously proposed rule change which was withdrawn by OCC.¹ OCC will clear the proposed OTC options in a manner that is highly similar to the manner in which it clears listed options, with only such modifications as are appropriate to reflect the unique characteristics of OTC options.

¹ Securities Exchange Act Release No. 34-66090 (January 3, 2012), 77 FR 1107 (January 9, 2012) (SR-OCC-2011-19).

OTC Options

OCC has entered into a license agreement with Standard & Poor's Financial Services LLC ("S&P") that allows OCC to clear OTC options on three equity indices published by the S&P: the S&P 500 Index, the S&P MidCap 400 Index and the S&P Small Cap 600 Index. The initial OTC options to be cleared by OCC will consist of options on the S&P 500 Index. OCC may clear OTC options on other indices and on individual equity securities in the future, subject to Commission approval of one or more additional rule filings. The current rule filing defines "OTC option" and "OTC index option" generically in order to simplify future amendments to provide for additional underlying interests. OTC options will have predominantly common terms and characteristics, but also include unique terms negotiated by the parties. Transactions in OTC options will not be executed through the facilities of any exchange, but will instead be entered into bilaterally and submitted to OCC for clearance through one or more providers of trade affirmation services.²

OTC options will be similar to exchange-traded standardized equity index options called "FLEX Options" that are currently traded on certain options exchanges.³ FLEX Options are exchange-traded put and call options that allow for customization of certain terms. For example, FLEX index Options traded on the Chicago Board Options Exchange have six customizable terms: (1) underlying index, (2) put or call, (3) expiration date, (4) exercise price, (5) American or European exercise style, and (6) method of calculating settlement value. OCC is the issuer and guarantor of FLEX Options and clears FLEX Options traded on multiple exchanges.

Similar to FLEX Options, OTC options will allow for customization of a limited number of variable terms with a specified range of values that may be assigned to each as agreed between the buyer and seller. Parties submitting transactions in OTC options for clearing by OCC will be able to customize six discrete terms: (1) underlying index;⁴ (2) put or call; (3) exercise price; (4) expiration date; (5) American or European exercise style; and (6) method of calculating exercise settlement value on the expiration date.⁵

² The initial provider of the trade affirmation services in connection with the OTC options will be MarkitSERV.

³ Note that FINRA Rule 2360(a)(16) refers to FLEX Options as "FLEX Equity Options," which it defines as "any options contract issued, or subject to issuance by, The Options Clearing Corporation whereby the parties to the transaction have the ability to negotiate the terms of the contract consistent with the rules of the exchange on which the options contract is traded." OCC does not believe this definition would capture OTC options as they are not traded on any exchange. Nevertheless, as discussed below, OCC is working with FINRA to amend certain of FINRA's rules to clarify the proper application of such rules to OTC options.

⁴ Initially, however, the S&P 500 Index will be the only permitted underlying index.

⁵ The expiration date of an OTC option must fall on a business day. The method of determining the exercise settlement value of an OTC option on its expiration date may be either the opening settlement value or the closing settlement value of the underlying index (calculated by S&P using the opening or

The variable terms and permitted values will be specified in the proposed Section 6 of Article XVII of the By-Laws. With respect to future OTC options accepted for clearing, OCC intends that such future OTC options will conform to the general variable terms and limits on the variable terms set forth in proposed Section 6 of the By-Laws, and will either amend the Interpretations and Policies thereunder to specify additional requirements for specific OTC options or publish such requirements on OCC's website.

Clearing of OTC Options

OCC proposes to clear OTC options subject to the same basic rules and procedures used for the clearance of listed index options. The proposed rules require that the counterparties to the OTC options must be eligible contract participants ("ECPs"), as defined in Section 3a(65) of the Securities Exchange Act of 1934,⁶ as amended (the "Exchange Act") and Section 1a(18) of the Commodity Exchange Act,⁷ as amended (the "CEA"). Because an OTC option will be a "security" as defined in the Exchange Act, the proposed rules also require that the transactions be cleared through a clearing member of OCC that is registered with the Commission as a broker-dealer or one of the small number of clearing members that are "non-U.S. securities firms" as defined in OCC's By-Laws. OCC is not proposing to require clearing members to meet any different financial standards for clearing OTC options. However, clearing members must be specifically approved by OCC to clear OTC options pursuant to new Interpretation and Policy .11 to Section 1 of Article V in order to assure the operational readiness of such clearing members to clear OTC options. Clearing members seeking to clear OTC options will be required to submit a business expansion request and complete an operational review. The operational review consists of an initial meeting with the clearing member's staff to evaluate the staff's experience, confirm the staff's familiarity with current OCC systems and procedures, complete an operational questionnaire, perform a high level review of the clearing member's systems and processing capabilities, and review other pertinent operational information. Successful testing of messaging capability between the clearing member, MarkitSERV and OCC is also necessary. These procedures will determine whether the firm is operationally ready to clear OTC Index Options.

Exercise of an OTC option will be settled by payment of cash by the assigned writer and to the exercising holder through OCC's cash settlement system on the business day following exercise in exactly the same manner as is the case with exercise settlement of listed index options. As in the case of listed index options, the exercise-settlement amount will be equal to the difference between the current value of the underlying interest and the exercise price of the OTC option, times the multiplier that determines the size of the OTC option. In the case of OTC index options on the S&P 500, the multiplier will be fixed at 1. The multipliers for additional OTC index options that OCC may in the

closing price, as applicable, in the primary market of each component security of the underlying index on the specified expiration date), in each case as reported to OCC by CBOE.

⁶ 15 U.S.C. 78c(a)(65),

⁷ 7 U.S.C. 1a(18),

future clear may be fixed at such value as OCC determines and provides for in its By-Laws and Rules.

OCC will calculate clearing margin for the OTC options using its STANS margin system on the same basis as for listed index options and will otherwise apply the same risk management practices to both OTC options and listed index options, including new risk modeling enhancements for longer-tenor options discussed below under "Risk Management Enhancement for Longer-Tenor Options." Because OCC currently clears listed options on all three of the underlying indexes on which OCC is currently licensed to clear OTC options, and because the customizable terms of these OTC options are relatively limited and the range of values that customizable terms may be given is limited, OCC does not believe that valuation and risk management for these OTC options present challenges that are different from those faced in the listed options market. Nevertheless, as discussed further below, OCC is proposing special OTC Options Auctions to be used in the unlikely event that OCC would be unable to close out positions in OTC options of a failed clearing member through other means.

OTC options may be carried in a clearing member's firm account, in market-maker accounts or in its securities customers' account, as applicable. Although customer positions in OTC options will be carried in the securities customers' account (an omnibus account), OCC will use a "customer ID" to identify positions of individual customers based on information provided by clearing members.⁸ However, positions are not presently intended to be carried in individual customer sub-accounts, and positions in OTC options will be margined at OCC in the omnibus customers' account on the same basis as listed options. If a clearing member takes the other side of a transaction with its customer in an OTC option, the transaction will result in the creation of a long or short position (as applicable) in the clearing member's customers' account and the opposite short or long position in the clearing member's firm account. The positions could also be includable in the internal cross-margining account, subject to any necessary regulatory approvals.

The trade data for an OTC option trade will be entered into the system of MarkitSERV or another trade confirmation/affirmation vendor approved by OCC for this purpose (the "OTC Trade Source").⁹ While MarkitSERV will be the only OTC Trade

⁸ Such customer IDs are necessary in order to allow OCC to comply with certain terms of OCC's license agreement with S&P. As described further below, customer IDs will be used for other purposes as well.

⁹ MarkitSERV, LLC is owned by Markit Group Limited, Markit Group Holdings Limited and The Depository Trust & Clearing Corporation. MarkitSERV Limited is a wholly-owned U.K. subsidiary of MarkitSERV, LLC. MarkitSERV, LLC and MarkitSERV Limited (collectively, "MarkitSERV") provide derivatives transaction processing, electronic confirmation, portfolio reconciliation services, and other related services for firms that conduct business in the over-the-counter derivatives markets through a variety of electronic systems, including the MarkitWire system. MarkitWire, owned by MarkitSERV Limited, is an OTC derivatives electronic confirmation/affirmation service offered by MarkitSERV as part of its post-trade processing suite of products. The role of MarkitSERV and MarkitWire in OCC's clearing of OTC options is described in further detail below.

Source at launch, OCC will permit additional OTC Trade Sources in the future in response to sufficient market demand from OCC's clearing members and subject to the ability of any such OTC Trade Source to meet OCC's requirements for operational readiness and interoperability with OCC's systems, as well as requirements with respect to relevant business experience and reputation, adequate personnel and expertise, financial qualification and such other factors as OCC deems relevant. OCC will receive confirmed trades from the OTC Trade Source. It will be permissible for parties to submit trades for clearance that were entered into bilaterally at any time in the past, provided that the eligibility for clearance will be determined as of the date the trade is submitted to OCC for clearance.¹⁰ The OTC Trade Source will process the trade and submit it as a confirmed trade to OCC for clearing. If the trade meets OCC's validation requirements, OCC will so notify the OTC Trade Source, which will notify the submitting parties. Customers of clearing members may have direct access to the OTC Trade Source for purposes of entering or affirming trade data and receiving communications regarding the status of transactions, in which case mechanisms will be put in place for a clearing member to authorize a customer to enter a trade for the clearing member's customers' account or for the clearing member to affirm a trade once entered.

In order for a clearing member to be approved for clearing OTC options, the clearing member must enter into a standard agreement with MarkitSERV (or another OTC Trade Source with which the clearing member intends to enter trade data, if and when OCC enters into arrangements with other OTC Trade Sources). At launch, OTC options will not be subject to the same clearing member trade assignment rules and procedures through which exchange-traded options can be cleared by a clearing member other than the executing clearing member. This functionality may be added at a later date. OCC and MarkitSERV will adopt procedures to permit a customer that has an account with Clearing Member A ("CM A") to enter into an OTC option transaction with Clearing Member B ("CM B") and have the position included in its account at CM A and cleared in CM A's customers' account at OCC.

OTC options will be fungible with each other to the extent that there are OTC options in the system with identical terms. However, OCC will not treat OTC options as fungible with index options listed on any exchange, even if an OTC option has terms identical to the terms of the exchange-listed option.

Clearing members that carry customer positions in cleared OTC options will be subject to all OCC rules governing OCC-cleared options generally, as well as all applicable rules of the Commission and of any self-regulatory organization, including the Financial Industry Regulatory Authority ("FINRA"), of which they are a member. Section 8 of Article III of OCC's By-Laws provides that, subject to the By-Laws and Rules, "the Board of Directors may suspend Clearing Members and may prescribe and

¹⁰ OCC's license agreement with S&P imposes certain requirements relating to minimum time remaining to expiration of an OTC option.

impose penalties for the violation of the By-Laws or the Rules of the Corporation, and it may, by Rule or otherwise, establish all disciplinary procedures applicable to Clearing Members and their partners, officers, directors and employees.” As a condition to admission, Section 3(c) of Article V of the By-Laws provides that a clearing member must agree, among other things, to “pay such fines as may be imposed on it in accordance with the By-Laws and Rules.” Rule 305 permits OCC to impose restrictions on the clearing activities of a clearing member if it finds that the financial or operational condition of the clearing member makes it necessary or advisable to do so for the protection of OCC, other clearing members, or the general public. Rule 1201(a) provides that OCC “may censure, suspend, expel or limit the activities, functions or operations of any Clearing Member for any violation of the By-Laws and Rules or its agreements with the Corporation.” In addition to, or in lieu of, such actions, OCC is permitted under the same paragraph to impose fines. Rule 1202(b) establishes procedures for taking any such disciplinary actions. The foregoing provisions are sufficient to permit OCC to fine or otherwise discipline a clearing member that fails to abide by OCC’s By-Laws and Rules applicable to OTC options, or to prohibit such clearing member from continuing to clear such options.

Regulatory Status of the OTC Options

An OTC option will be a “security” as defined in both the Securities Act of 1933, as amended (the “Securities Act”) and, as noted above, the Exchange Act. OCC will be the “issuer” of the OTC options. The OTC options will be neither “swaps” nor “security-based swaps” for purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”),¹¹

Most of OCC’s clearing members are members of FINRA and subject to FINRA’s rules, which have different provisions for “listed” and “OTC options” and contain various definitions distinguishing between the two. In some cases, OTC options would fall into neither category under FINRA’s definitions and in other cases, they would fall within what OCC perceives to be the wrong category. FINRA and OCC are working together to implement appropriate amendments to FINRA rules to clarify the proper application of such rules to cleared OTC options.

MarkitSERV Trade Submission Mechanics

MarkitSERV provides an interface to OCC that allows OCC to receive messages containing details of transactions in OTC options submitted for clearing by clearing

¹¹ Section 1a(47)(A)(i) of CEA, 7 U.S.C. 1a(47)(A)(i), as added by Section 721(a)(21) of Dodd-Frank, defines “swaps” broadly to include options on indices. However, Section 1a(47)(B)(iii) of the CEA, 7 U.S.C. 1a(47)(B)(iii), excludes from the “swap” definition any option on any index of securities that is subject to the Securities Act and the Exchange Act. A contract that is excluded from the definition of a “swap” under Section 1a(47)(B) of the CEA, 7 U.S.C. 1a(47)(B) (other than Section 1a(47)(B)(x), 7 U.S.C. 1a(47)(B)(x)) is not a “security-based swap” for purposes of Section 3a(68) of the Exchange Act, 15 U.S.C. 78c(a)(68).

members with access to MarketWire and also allows OCC to transmit messages to MarketWire participants identifying the status of submitted transactions. MarketWire applications use product-specific templates to simplify deal entry and negotiations. The templates specify the data required for a given product and also the business validation rules for each field. MarkitSERV has included OCC's validation requirements for OTC options in its trade templates.

The trade data for each OTC option transaction must be entered into MarketWire. MarkitSERV will use a "confirmation/affirmation" procedure in which one party to the trade enters the trade data to the MarketWire platform, which issues a confirmation to the counterparty to be affirmed, rejected or requested to be revised. If the trade details are confirmed, the trade will then be submitted to OCC for clearance and MarkitSERV will affirm such submission to both parties. OCC then validates the trade information for compliance with applicable requirements, such as the identification of an account of an eligible clearing member in which each side of the trade will be cleared, that the variable terms are within permissible ranges, and that minimum size requirements under OCC's license agreement with S&P are met. This validation will be completed by OCC immediately upon submission. OCC's clearing system will automatically accept the trade if it passes the validation process and will otherwise reject it.¹² A trade that is rejected by OCC may be corrected and submitted as a new transaction. Clearing members and customers with access to MarkitSERV will be able to determine whether a trade has been accepted or rejected both through MarkitSERV and, in the case of clearing members, through their interface with OCC's clearing system.

MarkitSERV's Regulatory Status¹³

MarkitSERV is not registered as a clearing agency under the Exchange Act, and the Commission staff has asked OCC to consider whether MarkitSERV would be required to so register in order to provide the proposed services to the OTC options market. OCC believes that no such registration is necessary based upon relevant interpretive guidance issued by the Commission.

Section 3(a)(23)(A) of the Exchange Act¹⁴ defines a "clearing agency" broadly. The definition includes, in relevant part, "any person who . . . provides facilities for comparison of data respecting the terms of settlement of securities transactions[.]" In 1998, the Commission issued a release entitled "Confirmation and Affirmation of

¹² Once accepted, a trade is guaranteed by OCC. Note, however, that OTC options for which the premium payment date communicated by MarkitSERV to OCC is prior to the business day on which the OTC option is submitted to OCC for clearing (referred to as a "Backloaded OTC Option") will not be accepted and guaranteed until the selling clearing member has met its initial morning cash settlement obligations to OCC on the following business day.

¹³ MarkitSERV offers different services in different markets, and this discussion is addressed only to the "confirmation/affirmation" procedure to be used in submitting trades to OCC.

¹⁴ 15 U.S.C. 78c(a)(23)(A).

Securities Trades; Matching” (the “Matching Release”).¹⁵ In the Matching Release, the Commission published “its interpretation that a ‘matching’ service that compares securities trade information from a broker-dealer and the broker-dealer’s customer is a clearing agency function.” The Matching Release distinguishes between such a matching service and a “confirmation/affirmation service” where the “vendor intermediary will only transmit information between the parties to a trade, and the parties will confirm and affirm the accuracy of the information.” The Commission noted that “matching” constitutes the “comparison of data respecting the terms of settlement of securities transactions” and that such services therefore trigger status as a clearing agency, while confirmation/affirmation services would not, by themselves, constitute such a data comparison. The Commission concluded in the Matching Release that “an intermediary that captures trade information from a buyer and a seller of securities and performs an independent reconciliation or matching of that information is providing facilities for the comparison of data within the scope of Exchange Act Section 3(a)(23).” The Commission stated that “matching” is “so closely tied to the clearance and settlement process that it is different not only in degree but also different in kind from the . . . confirmation and affirmation process.” The Matching Release goes on to state: “a vendor that provides confirmation/affirmation services only will exchange messages between a broker-dealer and its institutional customer. The broker-dealer and its institutional customer will compare the trade information contained in those messages, and the institution itself will issue the affirmed confirmation.” This is precisely what occurs when a counterparty to a trade affirms the trade data through MarkitSERV and requests submission to OCC for clearance. MarkitSERV transmits messages only; it does not “compare” or “match” trade data submitted by two parties.

The “confirmation/affirmation” functionality (as described above) to be provided by MarkitSERV (through MarkitWire) with respect to OTC options is functionally identical to the confirmation/affirmation service described in the Matching Release and OCC believes such service would not be a “matching” service within the meaning of the release. OCC believes that MarkitSERV will not be a “clearing agency” with respect to the services to be provided in connection with OTC options. The confirmation/affirmation service described in the Matching Release referred “to the transmission of messages among broker-dealers, institutional investors, and custodian banks regarding the terms of a trade executed for the institutional investor.” MarkitWire’s confirmation/affirmation process will allow for the transmission of messages among OCC’s clearing members (most of which are registered broker-dealers), their customers (all of whom will be ECPs and will therefore be large and financially sophisticated market participants) and OCC, which is itself registered and subject to the Commission’s oversight as a clearing agency.

By contrast, the “matching” services contemplated in the Matching Release would involve “the process whereby an intermediary compares the broker dealer’s trade data

¹⁵ Securities Exchange Act Release No. 34-39829 (April 13, 1998), 63 FR 17943 (April 13, 1998).

submission . . . with the institution's allocation instructions . . . to determine whether the two descriptions of the trade agree." MarkitWire performs no such comparison. Under the confirmation/affirmation procedure, trade data is entered into MarkitWire by one party and such data is made available to the counterparty to be affirmed, rejected or requested to be revised. MarkitWire merely facilitates the transfer of information between the parties sufficient to allow the comparison to be made. A binding transaction (*i.e.*, an "affirmed confirmation" in the language of the Matching Release) is not produced through any action of MarkitSERV, but is instead created by the completion, by the counterparty, of an affirmation of the trade data entered by the first party. MarkitWire provides no "independent reconciliation or matching" of trade data. Rather MarkitWire is providing essentially a messaging service among OCC and the parties to trades in OTC Options. The Matching Release is clear as to the distinction between a matching service and a confirmation/affirmation service, and OCC believes that there is no ambiguity that the services to be provided by MarkitWire with respect to OTC options fall into the latter, rather than the former, category.

Risk Management Enhancements for Longer-Tenor Options

Although OCC's license agreement with S&P allows OCC to clear OTC options with tenors of up to fifteen years, OCC has elected at this time to clear only OTC options on the S&P 500 index with tenors of up to five years. However, OCC currently clears FLEX Options on the S&P 500 with tenors of up to 15 years. While OCC believes that its current risk management practices are adequate for current clearing activity, OCC is in the process of implementing risk modeling enhancements with respect to longer-tenor options, including OTC options. The enhancements are part of OCC's ongoing efforts to test and improve its risk management operations with respect to all longer-tenor options that OCC currently clears. These procedures will be submitted for review in a separate "advance notice" filing and OCC will not commence clearing of OTC options until such procedures have been approved and implemented.

The proposed enhancements are as follows:

- First, OCC will introduce indicative over-the-counter quotations into the daily dataset of prices used to risk manage OCC-cleared products. These quotations will be obtained from a service provider that will collect OTC dealer polling information on a daily basis and provide such data to OCC.
- Second, OCC will introduce variations in the implied volatilities used in the modeling of all cleared options whose residual tenors are at least three years. To date, OCC's margin methodology has assumed that implied volatilities of option contracts are static over the two-day risk horizon. While OCC's backtesting has identified few exceedences related to implied volatility shocks, such shocks could occur and taking them into account in OCC's margin model will allow more

robust risk management. OCC proposes to achieve this result by incorporating into the risk factors included in OCC's models time series of proportional changes in implied volatilities for a range of representative volatilities.

- Third, OCC will introduce a valuation adjustment into its calculation of portfolio net asset value. This adjustment will be based on the aggregate sensitivity of the longer-tenor options in a portfolio to the overall level of implied volatilities at three and five years, and to the implied volatility skew.

A review of individual S&P 500 Index put and call options positions that are in the money by varying amounts and have expiration dates between four and nine years out indicates that the inclusion of modeled implied volatilities tends to result in less margin being held against short call positions and more being held against short put positions. These results are consistent with what would be expected given the strong negative correlation that exists between changes in implied volatility and market returns. On average, OCC observed a decrease in the margin requirement of approximately 24% on the nine call options tested and a 63% increase associated with the nine put options.

Proposed By-Law and Rule Changes

The specific proposed changes to OCC's By-Laws and Rules to provide for the clearing of OTC options relate primarily to: (i) specification of customizable terms; (ii) procedures for submission and acceptance of trades for clearance; and (iii) specification of criteria for eligibility of clearing members to clear transactions in OTC options and limitation of the types of customers for whom clearing members may effect transactions in OTC options. Otherwise, the currently proposed OTC options will be cleared and settled under the same provisions applicable to clearance of listed index options. Many of the proposed amendments are self-explanatory, and OCC has therefore attempted to confine the following discussion to a broad overview with specific explanation only where the reasons for the change may be less obvious.

Article I of the By-Laws contains defined terms used throughout the By-Laws and Rules. OCC proposes to modify certain existing definitions and include certain new definitions in order to incorporate OTC options into existing rules and facilitate the creation of new provisions unique to OTC options. Throughout the By-Laws and Rules, OCC proposes to replace the term "Exchange transaction," which is currently defined in Article I, in relevant part, as "a transaction on or through the facilities of an Exchange for the purchase, writing or sale of a cleared contract" with the term "confirmed trade" so as to make the relevant portions of the By-Laws and Rules applicable to transactions in OTC options as well as listed options, without causing confusion about the role of the OTC Trade Source in OCC's clearing of OTC options. "Confirmed trade" is proposed to be defined in Article I to include transactions "effected on or through the facilities of an exchange" or "affirmed through the facilities of an OTC Trade Source" in order to

include transactions in both listed options and OTC options. The current definition of “confirmed trade” in Rule 101 is proposed to be deleted as unnecessary given the new definition. Much of the length of this rule filing is attributable to the fact that the term “Exchange transaction” is used so many places in the rules. OCC has entered into agreements in the past which reference the term “Exchange transaction” or “exchange transaction.” OCC is also proposing to add an Interpretation and Policy to the new definition of “confirmed trade” in order to avoid any ambiguity concerning how such terms should be interpreted in any such agreement.

OCC proposes to add a new Interpretation and Policy .11 to Section 1 of Article V of the By-Laws, providing the additional criteria that must be met by a clearing member in order to clear OTC index options. Among these new criteria are that clearing members seeking to clear OTC index options on underlying indices published by Standard & Poor’s Financial Services LLC (“S&P”) must execute and maintain in effect a short-form license agreement in such form as specified from time to time by S&P. The current form of S&P short-form index license agreement is attached to the rule filing as Exhibit 3.

The Interpretations and Policies under Section 1, Article VI allow clearing members to adjust their positions with OCC for certain enumerated reasons. OCC proposes to amend the Interpretations and Policies to clarify that adjustment of positions in OTC options will be effected through a manual process (as opposed to the electronic process available to post-trade adjustments in listed options), to the extent permitted by OCC. For the same reason, OCC is proposing to amend Rule 403 to prohibit clearing member trade assignment (“CMTA”) transactions in OTC options. Trade “give-ups” that are effected through the CMTA process in the case of listed options will, in the case of OTC options, be effected through MarkitSERV before the trades are submitted to OCC for clearing.

Article XVII of the By-Laws governs index options in general and OCC is proposing amendments to Article XVII in order to set forth the terms applicable to the initial OTC options proposed to be cleared by OCC — options on the S&P 500 Index — and to differentiate OTC index options from other index options cleared by OCC. For example, certain amendments to the definitions are necessary because OTC options will be permitted to have a much wider range of expiration dates than exchange-traded options (other than FLEX Options). Additional definitional amendments ensure that OTC index options will constitute a separate class of options from other cash-settled index options even if both index options have the same terms and cover the same underlying interest.

Section 3 of Article XVII provides for adjustment of the terms of outstanding index options as necessary to reflect possible changes in the underlying index — such as those creating a discontinuity in the level of the index — that could theoretically make an adjustment necessary to protect the legitimate expectations of holders and writers of options on the index. Pursuant to paragraph (g) of Section 3, most but not all such

adjustments would be made, in the case of listed index options, by an adjustment panel consisting of representatives of the exchanges on which the options are traded. In the case of OTC options, any such adjustments will be made by OCC in its sole discretion. However, in exercising that discretion, OCC may take into consideration adjustment made by the adjustment panel with respect to exchange-traded options covering the same underlying index.¹⁶

OCC proposes to add a new Section 6 to Article XVII to set forth certain provisions unique to OTC index options, including the variable terms allowed for OTC index options and the general limitations on such variable terms. In general, all OTC index options must conform to the terms and limitations set forth in Section 6, and additional specific requirements applicable to specific OTC index options will either be set forth in the Interpretations and Policies under Section 6 or published separately on OCC's website. Section 6 also makes clear that although OTC index options are not fungible with exchange-traded index options, OTC index options of the same series (*i.e.*, options having identical terms) will be fungible with each other. In addition to the terms and limitations applicable to OTC index options, Section 6 will establish that clearing members will be deemed to have made a number of representations and warranties in connection with their activities in OTC options each time they affirm a confirmed trade entered into an OTC Trade Source.

OCC has submitted a rulemaking petition to the Commission¹⁷ seeking an amendment to Commission Rule 238¹⁸ that would exempt the OTC Options from most provisions of the Securities Act. Unless another exemption from the registration requirements of the Securities Act is available, OCC intends to rely upon Rule 506 of Regulation D¹⁹ under the Securities Act, which is a safe harbor under the Securities Act exemption in Section 4(a)(2)²⁰ for offerings by an issuer not involving a public offering. OCC intends to satisfy the conditions of Rule 506 of Regulation D as in effect at the time OCC relies upon the safe harbor. Participants in the existing markets for OTC equity options offered and sold in the United States commonly rely on the private offering exemption under these provisions and such reliance is therefore consistent with existing practice. OTC Options will be available for purchase only by highly sophisticated investors that are both "eligible contract participants," as defined in Section 3a(65) of the Exchange Act,²¹ and "accredited investors," as defined in Rule 501(a) under Regulation D.²² Section 6(f) of Article XVII includes representations of clearing members necessary

¹⁶Because index options, unlike options on individual stocks, rarely, if ever, require adjustments, allocation of the adjustment authority may have little practical significance.

¹⁷ See SEC File No. 4-644 (Submitted January 13, 2012), available at <http://www.sec.gov/rules/petitions/2012/petn4-644.pdf>.

¹⁸ 17 CFR 230.238.

¹⁹ 17 CFR 230.506.

²⁰ 15 U.S.C. 77d(a)(2).

²¹ 15 U.S.C. 77c(a)(65).

²² 17 CFR 230.501.

to ensure that there is no general solicitation or general advertising in connection with the offer or sale of the OTC Options until such time as OCC notifies clearing members that such restriction no longer applies.

Chapter IV of the Rules sets forth the requirements for reporting of confirmed trades to OCC, and Rule 401 thereunder governs reporting of transactions in listed options by participant Exchanges. OCC is proposing to add new Rule 404 to govern the details of reporting of confirmed trades in OTC options by an OTC Trade Source.

As discussed above, positions in OTC options will generally be margined in the same manner as positions in listed options using STANS and pursuant to Chapter VI of the Rules. However, OCC proposes to amend Rule 611 to establish different procedures for the segregation of long positions in OTC options for margining purposes. Long positions in listed options are held in a clearing member's customers' account or firm non-lien account and by default are deemed to be "segregated," meaning that they are not subject to OCC's lien and are given no collateral value when determining the margin requirement in the account. Such positions may be unsegregated only when a clearing member instructs OCC to unsegregate a long position and represents to OCC that the long position is part of a spread transaction carried for a single customer whose margin requirement on the corresponding short position has been reduced in recognition of the spread. OCC will then unsegregate the long position and so reduce OCC's margin requirement. However, in case of long positions in OTC options that are carried in a clearing member's customers' account and for which OCC has received a customer ID, OCC proposes that it will automatically unsegregate such long positions if OCC identifies a qualifying short position in OTC options carried under the same customer ID. Clearing members will not be required to give an affirmative instruction to OCC to unsegregate a long position in OTC options or make a separate representation regarding the spread transaction. Instead, by carrying a qualifying spread position in a customer account, clearing members are deemed to have represented to OCC that the customer's margin has been reduced in recognition of the spread. Based on discussion with the clearing members, it is OCC's understanding that, in practice, broker-dealers reduce customers' margin requirements to reflect spread positions. Therefore, OCC believes that automatic recognition of such spreads by OCC together with the deemed representation will greatly increase operational efficiency while providing equal assurance that long positions in OTC options will be unsegregated only if an identified customer will receive the benefit of the reduced margin required for spread transactions.

Rule 1001 sets forth the amount of the contribution that each clearing member is required to make to the clearing fund. OCC proposes to amend Rule 1001(c) so that, for purposes of calculating the daily average number of cleared contracts held by a clearing member in open positions with OCC during a calendar month (which number is used in turn to determine the clearing member's contribution to the clearing fund), open positions in OTC options will be adjusted as needed to account for any differences between the multiplier or unit of trading with respect to OTC options relative to non-OTC options

covering the same underlying index or interest so that OTC options and non-OTC options are given comparable weight in the computation.²³

In general, the rules in Chapter XI governing the suspension of a clearing member will apply equally to clearing members that transact in OTC options. Rule 1104 provides broad authority for OCC to liquidate a suspended clearing member's margin and clearing fund deposits "in the most orderly manner practicable." Rule 1106 provides similarly worded authority to close out open positions in options and certain other cleared contacts carried by a suspended clearing member. In 2011, the Commission approved an OCC rule change providing OCC the express authority to use a private auction as one of the means by which OCC may close out open positions and liquidate margin and clearing fund deposits of a suspended clearing member.²⁴ OCC anticipates it will use this auction process for OTC options as well. As an additional tool to ensure its ability to close out positions in OTC options promptly, OCC is proposing to amend Rule 1106 to provide for an alternative auction procedure specifically applicable only to OTC index options and related positions hedging, or hedged by, OTC index options (an "OTC Options Auction"). An OTC Options Auction would be used only in unusual circumstances where OCC determines it is not feasible to close out open positions in OTC index options through the other means provided for in OCC's Rules and By-Laws.²⁵ The amendments to Rule 1106 summarize the OTC Options Auction procedures and incorporate by reference the detailed procedures contained in a document entitled "OTC Options Auction Procedures," which will be posted on the Corporation's website and otherwise made available to clearing members upon request of OCC. A copy of the OTC Options Auction Procedures is attached to the rule filing as Exhibit 5.

Rule 1106(e)(2)(C) clarifies that, in the event that the liquidation of a clearing member results in a deficiency that would otherwise result in a proportionate charge against the clearing fund contributions of other clearing members, each OTC Index Option Member (as defined below) that failed to purchase or assume its share of an auction portfolio will be the first to absorb the deficiency, through a "Priority Charge" against such clearing members' clearing fund contributions. The Priority Charge is a "first loss" mechanism, and is not intended to increase a clearing member's total maximum exposure to OCC.

²³ For example, the index multiplier applicable to OTC index options on the S&P 500 Index will be fixed at 1. In comparison, the index multiplier applicable to listed index options is 100.

²⁴ See Securities Exchange Act Release No. 34-65654 (October 28, 2011), 76 FR 68238 (November 3, 2011) (SR-OCC-2011-08). OCC subsequently filed a rule change, currently pending Commission approval, providing detailed procedures for the conduct of such an auction. See Securities Exchange Act Release No. 34-67443 (July 16, 2012), 77 FR 42784 (July 20, 2012) (SR-OCC-2012-11).

²⁵ OCC anticipates that these procedures would be applicable to other OTC derivatives that may be cleared by OCC in the future. However, OCC has limited the currently proposed rule to OTC index options, and will amend it as and if appropriate to apply to other over-the-counter products that OCC may propose to clear in the future.

Under the OTC Options Auction procedures, all clearing members authorized to clear transactions in OTC index options (“OTC Index Option Members”), other than the defaulting clearing member, will be required to participate in the OTC Options Auction by submitting competitive bids for all or a portion of the defaulting clearing member’s OTC index option portfolio. Each such participant will be subject to a minimum participation level based on the participant’s proportionate share of the total “risk margin” requirement posted by all OTC Index Options Members in the previous month for all positions (not limited to OTC option positions) held in accounts eligible to hold OTC options positions (“OTC Eligible Accounts”), after removing the defaulting clearing member.²⁶ This method of calculating the minimum participation level in the OTC Options Auction results in all OTC Index Option Members being required to participate in the OTC Options Auction based on their clearing activity related to all positions in OTC Eligible Accounts. Required participation ensures that the OTC Options Auction will have sufficient participants authorized to clear transactions in OTC index options and that the most active clearing members in OTC index options will submit bids for the largest percentage of the auction portfolio, increasing the likelihood of the acquisition of OTC options positions by clearing members with appropriate financial strength, risk management capabilities and trading expertise. Each participant may submit bids at varying quantities and varying prices, so long as the participant’s bids equal or exceed its minimum participation level. A participant may use bids from non-OTC Index Options Members and non-clearing members in order to meet its minimum participation level, subject to certain Corporation requirements including that it guarantee the performance of such third parties. Each bid will indicate what percentage of the auction portfolio the participant is bidding on and the amount of the bid. Bids will be stated in terms of a price for the entire auction portfolio, and may be either positive or negative. (Negative bids imply an auction portfolio that has a negative net asset value and indicate how much the Corporation would be required to pay the participant to assume the relevant percentage of the auction portfolio.) The Corporation will rank the submitted bids from best to worst and the auction portfolio will be allocated among the bidding participants accordingly until the auction portfolio is exhausted. The bid price that is sufficient to clear the entire auction portfolio will become the single price to be used for all winning bids, even if a participant’s stated bid was better.

In order to provide a strong incentive to ensure competitive bidding by the OTC Index Option Members required to participate in an OTC Options Auction, OTC Index Options Members who fail to win their minimum participation in the auction will be subject to a potential priority charge against its clearing fund contribution. If the cost of liquidating a suspended clearing member’s positions exhausts the clearing member’s margin and clearing fund contribution and any other assets of the suspended clearing member available to OCC, then OCC, pursuant to Section 5 of Article VIII of the By-Laws, would ordinarily withdraw the amount of the deficiency from the clearing fund and

²⁶ This minimum participation level will be multiplied by 1.15 to calculate each participant’s minimum bid size, such that the sum of all participants’ bids will equal 115% of the auction portfolio, in order to increase the likelihood that the entire auction portfolio will be allocated to participants.

charge it on a proportionate basis against all other clearing members' computed contributions as fixed at the time. When an OTC Options Auction has been held in respect of a suspended OTC Index Options Member, however, some or all of any such remaining loss would be assessed first against the clearing fund contributions of any OTC Options Auction participant(s) whose bids are insufficiently competitive to be allocated a portion of the auction portfolio equal to such participant's minimum required participation. This priority charge would be made regardless of the reason for the shortfall—*i.e.*, whether or not the loss resulted from the closing out of OTC options positions. The priority charge would be calculated based on an "assessment ratio," which is formulated to provide incentive to all OTC Options Auction participants to participate to their full minimum participation level in the auction. The method of calculating the assessment ratio is such that if the net asset value of the auction portfolio is zero the assessment ratio will also be zero and no priority charge will be made. As the absolute net asset value of the auction portfolio (whether positive or negative) increases, the assessment ratio also increases, all other factors being equal. If all OTC Options Auction participants submit bids such that each receives an allocation of OTC options positions equal to its minimum participation level, no priority charge will be made regardless of whether or not there is a liquidation shortfall. If a liquidation shortfall remains after any priority charges, or if no priority charges were required, the Corporation will then make a proportionate charge against the clearing fund contributions of all clearing members, including those that participated in the OTC Options Auction, in the usual manner pursuant to Section 5 of Article VIII of OCC's By-Laws.

In order to protect the estate of the suspended clearing member, OCC reserves some discretion in supervising the auction. In the event that the bid price that clears the entire auction portfolio is determined by OCC to be an outlier bid, OCC may choose as the winning bid a price that clears at least 80% of the auction portfolio. The remaining auction portfolio will then be re-auctioned as described above.

OCC anticipates that the likelihood of having to use this alternative auction is small. Nevertheless, in view of the fact that positions in OTC index options are expected to be large and that there may be no active trading market in options with terms precisely identical to the terms of the OTC index options in question, OCC believes that this is an appropriate failsafe provision. It should be noted that the Chicago Mercantile Exchange Inc. ("CME") has rules allowing its clearing house and certain CME committees to administer an auction process to liquidate positions in interest rate swaps ("IRS") in the event of a default of a CME clearing member authorized to submit IRS for clearing (an "IRS Member").²⁷ Although the financial safeguards supporting IRS clearing, including its "guaranty fund," and the IRS auction process are different from OCC's clearing fund and OTC Options Auction in that, among other things, there is a separate guaranty fund for IRS, the IRS auction shares certain similarities with the OTC Options Auction. In

²⁷ See CME Rules 8G14, 8G25 and 8G802.B. See also Commodity Futures Trading Commission Rule Change Submission No. 12-061RR of CME, the Board of Trade of the City of Chicago Inc. and the New York Mercantile Exchange, available at: <http://www.cmegroup.com/market-regulation/files/12-061rr.pdf>

particular, the IRS auction process requires mandatory participation of IRS clearing members with open interest in a position being auctioned and, in order to provide incentive for IRS Members to submit quality bids in an IRS auction, provides that in the event there is a loss to CME's clearing house associated with an IRS Member's default, IRS Members that do not submit quality bids in an IRS auction are subject to having their IRS guaranty fund deposit assessed before assessments are made against other IRS clearing members' guaranty fund deposits. In its original rule filing, OCC had proposed a different failsafe solution whereby OCC could terminate open positions of a suspended clearing member by setting a close-out value that non-defaulting clearing members holding the opposite side of the suspended clearing member's positions would be required to accept or pay in settlement of the terminated positions. However, clearing members objected to that proposed method and have advocated the auction procedures proposed here in lieu of the early termination proposal.²⁸ Clearing members in an OTC advisory group were active in designing the OTC Options Auction procedures, including the priority charges.

Impact of Clearing OTC Options on Other OCC-Cleared Products

Cleared OTC options will not be fungible with listed options. However, an OTC option may have economic characteristics that are substantially similar or identical to the characteristics of options in series of listed options that OCC clears. While it is possible that in any given instance a market participant may elect to enter into an OTC option in lieu of an economically similar listed product, OCC does not believe that its clearing of OTC options will adversely affect the efficiency or liquidity of the listed markets. The OTC options markets currently exist to accommodate a variety of commercial and other needs of market participants, including the ability to customize the terms of transactions. While the availability of an OCC guarantee for OTC transactions in which the parties would otherwise be exposed to each others' creditworthiness may cause transactions that currently occur in the non-cleared OTC markets to migrate to the cleared-OTC markets, OCC does not believe it will cause significant migration from the listed markets to the cleared OTC markets. The limitation of the OTC options markets to ECPs as well as the significant minimum transaction size and tenor requirements that are applicable to certain transactions in the currently proposed OTC options under the S&P License Agreement will limit the use of cleared OTC options and should help to ensure that there is no substantial migration from the listed markets to the OTC markets for this product. The existing bilateral OTC options markets have existed for years alongside the listed options markets, and OCC believes that dealers in such bilateral options often use the listed markets to hedge positions taken in such bilateral options and other OTC derivatives.

²⁸ See comment letter from Alessandro Cocco, Managing Director of J.P. Morgan Clearing Corporation and J.P. Morgan Securities LLC, to Ms. Elizabeth M. Murphy, Secretary, Securities and Exchange Commission (January 30, 2012), available at <http://www.sec.gov/comments/sr-occ-2011-19/occ201119-2.pdf>.

Notice of Launch Date

Following approval of this rule change by the Commission, OCC expects to provide notice to its clearing members of the date on which it intends to implement this rule change and begin clearing OTC options.

Opposing Views

No opposing views were expressed related to the rule amendments.

Notice of Pending Rule Certification

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

Certification

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

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

Sincerely,


Stephen Szarmack

Enclosure

cc: CFTC Central Region (w/ enclosure)
525 West Monroe Street, Suite 1100
Chicago, IL 60661

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 19b-4

Proposed Rule Change and Advance Notice

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 advance notice and rule change is filed by The Options Clearing Corporation (“OCC” or the “Corporation”) in connection with proposed amendments to its By-Laws and Rules as set forth below to provide for the clearance and settlement of index options that are negotiated bilaterally in the over-the-counter market and submitted to OCC for clearance (“OTC options”).¹ In this rule filing, OCC seeks approval to clear *only* OTC options on the S&P 500 Index. OCC expects to clear OTC options on other indices and on individual equity securities in the future, and it will be necessary to file further rule changes for Commission approval of those additional products.

Material proposed to be added to OCC’s By-Laws and Rules as currently in effect is underlined and material proposed to be deleted is enclosed in bold brackets. Double underlining and double bold brackets indicate either (a) material proposed to be added or deleted in a separate pending rule filing or (b) material approved by the Commission, but not yet implemented by OCC, as indicated in the footnotes accompanying such material.

THE OPTIONS CLEARING CORPORATION

BY-LAWS

* * *

ARTICLE I

DEFINITIONS

* * *

Definitions

¹ This rule filing replaces SR-OCC-2011-19, which was filed with the Commission on December 20, 2011, amended January 3, 2011 at the staff’s request, and withdrawn on March 9, 2012.

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

A. [no change]

B.

Backloaded OTC Option

(1) The term “Backloaded OTC option” means an OTC option for which the premium payment date communicated to the Corporation by the OTC Trade Source is prior to the business day on which such OTC option is submitted to the Corporation for clearing.

(1) – (5) [renumbered as (2) – (6); otherwise no change]

Buyer

[(6)] (7) The term “buyer” used in relation to a future means, as the context requires, a person with a long position in the future or a person purchasing a future in a confirmed trade [an Exchange transaction].

(7) [renumbered as (8); otherwise no change]

C.

(1) – (3) [no change]

Carrying Clearing Member

(4) The term “Carrying Clearing Member” means a Clearing Member that has authorized an Executing Clearing Member to direct the transfer of a confirmed trade [an Exchange transaction] to a designated account of such Carrying Clearing Member pursuant to a CMTA arrangement.

(5) – (8) [no change]

Class

(9) The term “class” means, when applied to options, all option contracts of the same type and style covering the same underlying interest; provided, however, that OTC options and listed options that would otherwise constitute a single class of options shall constitute separate classes. [and w]When applied to futures, the term “class” means all futures covering the same underlying interest.

(10) – (12) [no change]

Clearing Member

(13) The term “Clearing Member” means a person or organization that has been admitted to membership in the Corporation pursuant to the provisions of the By-Laws and Rules.

References in the By-Laws or Rules to the term “Clearing Member” preceded by a capitalized reference to an underlying interest or a cleared contract, e.g., a “Stock Clearing Member,” or a “Security Futures Clearing Member,” shall be deemed to be to a Clearing Member approved in accordance with Article V of the By-Laws to clear transactions in options on the specified underlying interest, or in the cleared contract, as applicable, provided that the term “Stock Clearing Member” shall be deemed to include a Clearing Member approved to clear transactions in BOUNDS as well as stock options, the term “Treasury Securities Clearing Member” shall mean a Clearing Member approved to clear transactions in Treasury Securities options excluding yield-based Treasury options and the term “Index Clearing Member” shall mean a Clearing Member approved to clear transactions in cash-settled options other than OTC options. The term “OTC Index Option Clearing Member” means a person that has been approved to clear OTC index options.

(14) – (15) [no change]

Closing Purchase Transaction

(16) The term “closing purchase transaction” means a confirmed trade [an Exchange transaction] in which the purchaser’s intention is to reduce or eliminate his short position in a series of cleared security.

Closing (Sale) Transaction

(17) The term “closing sale transaction” or “closing writing transaction” means a confirmed trade [an Exchange transaction] in which the seller’s intention is to reduce or eliminate a long position in a series of cleared security.

CMTA

(18) The term “CMTA” (Clearing Member Trade Assignment) means the process by which an Executing Clearing Member, acting on its own behalf or as the Clearing Member of an Introducing Broker, directs the transfer of a confirmed trade [an Exchange transaction] to a designated account of a Carrying Clearing Member for clearance and settlement.

(19) [no change]

CMTA Customer; CMTA Customer Identifier; Customer CMTA Indicator

(20) The term “CMTA Customer” means a customer of a Carrying Clearing Member who has been assigned a CMTA Customer Identifier by such Carrying Clearing Member to designate that confirmed trades [Exchange transactions] executed and cleared on such customer’s behalf are pursuant to a CMTA arrangement. The term “CMTA Customer Identifier” means a string of characters (as may be modified from time to time) assigned by a Carrying Clearing Member to identify a CMTA Customer. The term “Customer CMTA Indicator” means an indicator included with the [matching] confirmed trade information to designate that a confirmed trade [an Exchange transaction] was effected on behalf of a CMTA Customer.

(21) – (22) [no change]

Commencement Time

(23) The term “commencement time” [means the time at which Exchange transactions are accepted for clearing by the Corporation as specified] has the meaning given in Section 5 of Article VI.

(24) – (26) [no change]

Confirmed Trade

(27) The term “confirmed trade” means a transaction for the purchase, writing, or sale of a cleared contract, or for the closing out of a long or short position in a cleared contract, that is (i) effected on or through the facilities of an Exchange and submitted to the Corporation for clearance or (ii) affirmed through the facilities of an OTC Trade Source and submitted to the Corporation for clearance.

...Interpretations and Policies:

.01 The term “Exchange transaction” was removed from the By-Laws and Rules and replaced with the term “confirmed trade” to reflect the expansion of the Corporation’s clearing activities into OTC options. “Confirmed trade” is a successor term to the term “Exchange transaction.” Any reference to the term “Exchange transaction” or “exchange transaction” in any agreement to which the Corporation is a party should be interpreted to refer instead to the term “confirmed trade.”

(27) – (36) [renumbered as (28) – (37); otherwise no change]

Customers’ Account

[(37)](38) The term “customers’ account” in respect of a Clearing Member means an account of the Clearing Member on the records of the Corporation which is confined to confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member on behalf of its securities customers, other than those transactions of Market-Makers which are cleared through a Market-Maker’s account. The term “customers’ account” does not include a segregated futures account or customers’ lien account.

(38) [renumbered as (39); otherwise no change]

D. [no change]

E.

(1) – (10) [no change]

Exchange Rules

(11) The term “Exchange Rules,” when used in respect of any Exchange, means the constitution, certificate of incorporation, by-laws, rules and stated policies, and all written

interpretations thereof, or instruments corresponding to the foregoing, as the same may be in effect from time to time, of that Exchange. The term “Exchange Rules” in respect of [an Exchange transaction] a confirmed trade effected on or through the facilities of an Exchange means the constitution, certificate of incorporation, by-laws, rules and stated policies, and all written interpretations thereof, or instruments corresponding to the foregoing, as the same may be in effect from time to time, of that Exchange [the Exchange on which such transaction was effected]. The term “Exchange Rules” in respect of a cleared contract means the constitution, certificate of incorporation, by-laws, rules and stated policies, and all written interpretations thereof, as the same may be in effect from time to time, of each Exchange on which such cleared contract is traded.

[Exchange Transaction

(12) The term “Exchange transaction” as used in respect of an Exchange other than an international market means a transaction on or through the facilities of an Exchange for the purchase, writing, or sale of a cleared contract or for the closing out of a long or short position in a cleared contract. As used in respect of an international market, such term means a transaction on or through the facilities of such market for the purchase, writing, or sale of a cleared contract, or for the closing out of a long or short position in a cleared contract, for which the Corporation acts as clearing agent pursuant to an international market agreement.]

Executing Clearing Member

(12) [(13)] The term “Executing Clearing Member” means a Clearing Member, on its own behalf or as the Clearing Member of an Introducing Broker, that has been authorized by a Carrying Clearing Member to direct confirmed trades [Exchange transactions] to be transferred to a designated account of the Carrying Clearing Member pursuant to such Clearing Members’ CMTA arrangement.

Execution-Only Clearing Member

(13) [(14)] The term “Execution-Only Clearing Member” shall mean a Clearing Member approved to act only as a Clearing Member that transfers confirmed trades [Exchange transactions] or allocates positions to other Clearing Members, and not to carry positions in its accounts with the Corporation on a routine basis.

(15) – (20) [renumbered as (14) – (19); otherwise no change]

Expiration Exercise Report

(20) [(21)] The term “Expiration Exercise Report” shall mean information [a report] made available online by the Corporation to a Clearing Member on an expiration date identifying [listing], by account, each expiring option contract in each of the Clearing Member’s accounts with the Corporation. Such term shall also include updated versions of any such information [report] made available to a Clearing Member prior to such time on the expiration date as the Corporation shall from time to time specify. [An Expiration Exercise Report shall indicate the closing price (as defined in Rule 805) of the underlying interest for each series of

options listed therein and shall include such further information as the Corporation shall deem appropriate.]

(22) – (23) [renumbered as (21) – (22); otherwise no change]

F.

(1) – (2) [no change]

Firm Account

(3) The term “firm account” in respect of a Clearing Member means an account established by the Clearing Member which is confined to confirmed trades [Exchange transactions] cleared and positions carried on behalf of non-customers of the Clearing Member. The term “firm lien account” means a firm account as to which the Corporation shall have a lien on all long positions in the account pursuant to Sections 3(a), (b)(iv), (c)(v), and (k) of Article VI of the By-Laws, and the term “firm non-lien account” means a firm account as to which the Corporation shall have a lien only on unsegregated long positions therein.

(4) – (12) [no change]

G. – H. [no change]

I.

(1) – (3) [no change]

Index Multiplier

(4) The term “index multiplier” (i) as used in reference to an index option contract other than an OTC index option contract, means the dollar amount (as specified by the Exchange on which such contract is traded) by which the current index value is to be multiplied to obtain the aggregate current index value, [and] (ii) as used in reference to an OTC index option contract, means the dollar amount (as agreed upon by the parties to such transaction) by which the current index value is to be multiplied to obtain the aggregate current index value, and (iii) as used in reference to index futures of any series, means the dollar amount (as specified by the Exchange on which such series is traded) by which the final settlement price in respect of such futures is to be multiplied to obtain the final variation payment. Such term replaces the term “unit of trading,” used in reference to other kinds of options.

Index Value Determinant

(5) The term “index value determinant,” used in respect of settlement of flexibly structured index option contracts and futures and OTC options, means the method for determining the current index value on the expiration date or maturity date as that method is reported to the Corporation by the applicable Exchange [on which the option or future was purchased] or OTC Trade Source.

(6) – (10) [no change]

International Option

(11) The term “international option” means an option contract issued by the Corporation as the result of an international transaction pursuant to an international market agreement. In addition, the Corporation may designate other options belonging to the same class as such options as international options, and may designate confirmed trades [Exchange transactions] in such options as international transactions, for the purposes of some or all of the provisions of the By-Laws and Rules applicable to international options and international transactions, respectively.

International Transaction

(12) The term “international transaction” means a confirmed trade [an Exchange transaction] effected under the provisions of an international market agreement and shall include such other confirmed trades [Exchange transactions] as the Corporation may designate as international transactions in accordance with the definition of “international option.”

Introducing Broker; IB Identifier

(13) The term “Introducing Broker” means a broker-dealer or futures commission merchant that takes an order for [an Exchange] a transaction in a cleared contract from a CMTA Customer, executes or arranges for [an Exchange member] another broker-dealer or futures commission merchant to execute such transaction and, in the case of an Introducing Broker that is not a Clearing Member, arranges for its Clearing Member or the executing [Exchange member's] broker-dealer's or futures commission merchant's Clearing Member to direct the resulting confirmed trade [Exchange transaction] to be transferred to a designated account of a Carrying Clearing Member. The term “IB Identifier” means a string of characters (as may be modified from time to time) assigned by the Executing Clearing Member to (i) itself or (ii) an Introducing Broker that is not a Clearing Member to identify an Introducing Broker that has executed or arranged for the execution of any [Exchange] transaction in a cleared contract on behalf of a CMTA Customer.

J.**JBO Participant**

(1) The term “JBO Participant” means a broker-dealer registered with the Securities and Exchange Commission that: (i) maintains a joint back office arrangement with a Clearing Member pursuant to the requirements of Regulation T promulgated by the Board of Governors of the Federal Reserve System; (ii) meets the requirements applicable to JBO Participants as specified in Exchange Rules; and (iii) consents to having his confirmed trades [Exchange transactions] cleared and positions carried in a JBO Participants' account. A JBO Participant shall be considered a “Market-Maker” for purposes of these By-Laws and Rules, except for purposes of Chapter IV of the Rules, or where the context otherwise requires.

JBO Participants' Account

(2) The terms “JBO Participants' account” in respect of a Clearing Member means an account established by the Clearing Member which is confined to confirmed trades

[Exchange transactions] cleared and positions carried by the Clearing Member on behalf of JBO Participants.

(3) [no change]

K. – L. [no change]

M.

(1) – (3) [no change]

Market-Maker Account

(4) The term “Market-Maker account” or “Market-Maker’s account” in respect of a Clearing Member means an account established by the Clearing Member which is confined to confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member in an account that is not required to be segregated under Section 4d of the Commodity Exchange Act on behalf of a Market-Maker; and, unless the context otherwise requires, such term includes (i) a combined Market-Makers’ account, and (ii) a JBO Participants’ account.

(5) – (11) [no change]

Maturity Date

(12) The term “maturity date” means (i) in respect of a series of futures other than flexibly structured security futures, the date designated by the Exchange(s) on which such series is traded as the date on or as of which the final settlement price for such series is determined, and (ii) in respect of a flexibly structured future, the date agreed upon by the Purchasing Clearing Member and Selling Clearing Member in a confirmed trade [an Exchange transaction] as the date on or as of which the final settlement price for such future is determined, as such date is reported to the Corporation by the Exchange.

(13) – (15) [no change]

N. [no change]

O.

OCC Proprietary X-M Account; OCC Non-Proprietary X-M Account; CCO Proprietary X-M Account; CCO Non-Proprietary X-M Account; Set of X-M Accounts

(1) The term “OCC cross-margin account” or “OCC X-M account” means an account carried by a Joint Clearing Member or the OCC Clearing Member of a Pair of Affiliated Clearing Members at the Corporation in which options positions subject to cross-margining treatment are maintained. The term “CCO cross-margin account” or “CCO X-M account” means an account carried by a Joint Clearing Member or the CCO Clearing Member of a Pair of Affiliated Clearing Members at a Carrying CCO in which futures options, commodity options and futures contracts subject to such cross-margining treatment are maintained. A “proprietary X-M account” means an X-M account that is confined to the confirmed trades [Exchange

transactions] and positions of non-customers of the carrying Clearing Member and other proprietary Market Professionals. A “non-proprietary X-M account” means an X-M account that is confined to the confirmed trades [Exchange transactions] and positions of Market Professionals that are neither non-customers of the carrying Clearing Member nor other proprietary Market Professionals. The term “set of X-M accounts,” which may consist of two X-M accounts (“paired accounts”) or three or more X-M accounts, means the OCC X-M account (proprietary or non-proprietary) and each corresponding CCO X-M account of a Joint Clearing Member or a Pair of Affiliated Clearing Members carried at the Carrying CCO(s).

Opening Purchase Transaction

(2) The term “opening purchase transaction” means a confirmed trade [an Exchange transaction] in which the purchaser’s intention is to create or increase a long position in a series of cleared contracts.

Opening Sale (Writing) Transaction

(3) The term “opening sale transaction” or “opening writing transaction” means a confirmed trade [an Exchange transaction] in which the seller’s intention is to create or increase a short position in a series of cleared contracts.

Option Contract

(4) The term “option contract” or “option” means a put option, a call option, a binary option, a range option or a packaged spread option (as defined in Article XXVI of the By-Laws) issued by the Corporation pursuant to the By-Laws and Rules. The term “stock option contract” means a put or a call, as defined in this Article I for which the underlying security is an equity security, including fund shares, or an index-linked security. The term “Treasury securities option contract” means a put or a call, as defined in Article XIII of the By-Laws. The term “yield-based Treasury option contract” means a put or a call, as defined in Article XVI of the By-Laws. The term “debt securities option contract” means a Treasury securities option contract. The term “foreign currency option contract” means a put or a call, as defined in Article XV of the By-Laws. The term “cross-rate foreign currency option contract” means a put or a call, as defined in Article XX of the By-Laws. The term “cash-settled foreign currency option contract” means a put or a call, as defined in Article XXII of the By-Laws. The term “index option contract” means [a put or a call, as defined in Article XVII of the By-Laws] any option contract the underlying interest of which is a securities index or commodities index. The term “cash-settled option contract” means any option contract that is settled upon exercise by payment of cash rather than delivery of, and payment for, the underlying interest. The term “non-equity securities option contract” means a debt securities option contract (other than an option on an index-linked security), a foreign currency option contract, a cross-rate foreign currency option contract, a cash-settled option contract, or a futures option. The term “futures option” means any option to buy or sell any commodity futures contract traded on, through the facilities of, or subject to the rules of a futures market.

Origination Date

(5) The term “origination date” means the date when the bilateral option was entered into by the parties to such bilateral option, as communicated to the Corporation by the OTC Trade Source.

OTC Index Option

(6) The term “OTC index option” means an “OTC option,” as defined in this Article I, that is an index option.

OTC Option

(7) The term “OTC option” means an “option contract,” as defined in this Article I, with variable terms that are negotiated bilaterally between the parties to such transaction (subject to any specific requirements applicable to such products as set forth in the By-Laws and Rules), and that is affirmed through the facilities of an OTC Trade Source and submitted to the Corporation for clearing as a confirmed trade.

OTC Trade Source

(8) The term “OTC Trade Source” means any electronic messaging system approved by the Corporation through which transactions in OTC options may be affirmed by the parties to such transactions and submitted to the Corporation for clearance.

OTC Trade Source Rules

(9) The term “OTC Trade Source Rule,” when used in respect of any OTC Trade Source, means the rules, agreements, policies and procedures of the OTC Trade Source applicable to users or participants of the OTC Trade Source.

P.

(1) – (8) [no change]

Premium

(9) The term “premium” in respect of any confirmed trade [Exchange transaction] in option contracts means the aggregate price of such option contracts agreed upon between the purchaser and seller in such transaction. In the case of a transaction in stock options, the premium is equal to the agreed upon premium per unit multiplied by the unit of trading for the series of options multiplied by the number of contracts subject to the confirmed trade [Exchange transaction]. As used in respect of any confirmed trade in [Exchange transaction] BOUNDS, the word “premium” means the trade price.

(9) – (11) [no change]

Proprietary Futures Professional Account

(12) The term “proprietary futures professional account” in respect of a Clearing Member means an account of the Clearing Member on the records of the Corporation which is

confined to confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member on behalf of futures professionals who are not futures customers.

Proprietary Market-Maker; Proprietary Market-Maker Account

(13) The term “proprietary Market-Maker” in respect of a Clearing Member carrying an account that is not required to be segregated under Section 4d of the Commodity Exchange Act means a Market-Maker that is (A) a non-customer of such Clearing Member or (B) a Related Person of such Clearing Member that (i) is not a customer of such Clearing Member for purposes of Rule 15c3-3 of the Securities and Exchange Commission, (ii) does not carry the accounts of persons who are customers of such Market-Maker for purposes of Rule 15c3-3, and (iii) has consented to be treated as a proprietary Market-Maker for purposes of the By-Laws and Rules. The term “proprietary Market-Maker” shall include any participant, as such, in an account that is not required to be segregated under Section 4d of the Commodity Exchange Act of which 10% or more is owned by a proprietary Market-Maker. The term “proprietary Market-Maker account” means an account established by a Clearing Member which is confined to the confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member on behalf of a proprietary Market-Maker.

(14) – (15) [no change]

Purchasing Clearing Member

(16) The term “Purchasing Clearing Member” means the Clearing Member acting as, or on behalf of, the purchaser of a cleared contract [in an Exchange transaction].

(17) [no change]

Q. [no change]

R.

(1) – (4) [no change]

Reporting Authority

(5) When used in respect of any cash-settled contract, the term “reporting authority” shall mean the source [, designated by the Exchange or other market on which such contracts are traded,] that is relied upon by the Corporation as the official source for the current price or value of the underlying interest.

(6) [no change]

Restricted Lien

(7) The term “restricted lien” means a security interest of the Corporation in specified assets (including any proceeds thereof) in an account of a Clearing Member with the Corporation as security for the Clearing Member’s obligations to the Corporation arising from such account or, to the extent so provided in the By-Laws or Rules, a specified group of accounts that includes such account including, without limitation, obligations in respect of all confirmed

trades [Exchange transactions] effected through such account or group of accounts, short positions maintained in such account or group of accounts, and exercise notices assigned to such account or group of accounts.

(8) [no change]

Return

(9) The term “Return” means the process by which a Carrying Clearing Member transfers back to an Executing Clearing Member, for one or more reasons specified in the CMTA Agreement between the Clearing Members, a position resulting from a confirmed trade [an Exchange transaction] transferred by the Executing Clearing Member to an account of the Carrying Clearing Member.

(10) [no change]

S.

(1) – (4) [no change]

Segregated Futures Account

(5) The term “segregated futures account” in respect of a Clearing Member means an account of the Clearing Member on the records of the Corporation which is confined to confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member on behalf of futures customers.

Segregated Futures Professional Account

(6) The term “segregated futures professional account” in respect of a Clearing Member means an account of the Clearing Member on the records of the Corporation which is confined to confirmed trades [Exchange transactions] cleared and positions carried by the Clearing Member on behalf of futures professionals who are futures customers. A segregated futures professional account is a type of segregated futures account.

(7) [no change]

Seller

(8) The term “seller” means, as the context requires, a person with a short position in a future or a person selling a future in a confirmed trade [an Exchange transaction].

Selling Clearing Member

(9) The term “Selling Clearing Member,” in respect of a confirmed trade [an Exchange transaction] in options or BOUNDS, means the Writing Clearing Member and, in respect of a confirmed trade [an Exchange Transaction] in futures, means the Clearing Member acting as, or on behalf of, the seller.

(10) – (11) [no change]

Settlement Day

(12) The term “settlement day”, when used in respect of amounts owed by Clearing Members to the Corporation or by the Corporation to Clearing Members to settle [Exchange] confirmed trades and/or stock loan transactions, means: (i) the first business day following the Corporation’s receipt of a report of [matching] confirmed trade information from the Exchange on which the transaction was effected or a report of a completed stock loan from the Depository, or (ii) with respect to transactions in cleared contracts effected in trading sessions beginning on one calendar day and ending on the next calendar day, the business day after the day on which trading ends, as applicable, unless a different settlement day is specified in the Corporation’s By-Laws, Rules or procedures.

(13) [no change]

Settlement Time

(14) The term “settlement time”, when used in respect of a Clearing Member’s obligation to pay the Corporation amounts owed to settle [Exchange] confirmed trades and/or stock loan transactions or any other obligations to the Corporation, other than such transactions settling outside the United States, means 9:00 A.M. Central Time (10:00 A.M. Eastern Time) on the settlement day for such [Exchange] confirmed trades and/or stock loan transaction or other obligation.

The term “settlement time”, when used in respect of the Corporation’s obligation to pay a Clearing Member amounts owed to settle [Exchange] confirmed trades and/or stock loan transactions or any other obligations to a Clearing Member, other than such transactions settling outside the United States, means 1:00 P.M. Central Time (2:00 P.M. Eastern Time) on the settlement day for such [Exchange] confirmed trades and/or stock loan transaction or other obligation. For [Exchange] confirmed trades and/or stock loan transactions or other obligations settling outside the United States, the settlement time therefor shall be as specified in the By-Laws, Rules or procedures of the Corporation.

(15) – (28) [no change]

T.**Trade Date**

(1) The term “trade date” in respect of any confirmed trade effected on or through the facilities of an Exchange [Exchange transaction] means the day on which such transaction occurred except that: (i) in the case of classes of options that are cleared through ICS, the trade date in respect of transactions in such options that are effected in trading sessions conducted after 3:00 P.M. Central Time (4:00 P.M. Eastern Time) shall be deemed to be the business day following, and (ii) the trade date in respect of confirmed trades [Exchange transactions] in cleared contracts that are effected in trading sessions beginning on one calendar day and ending on the next calendar day shall be deemed to be the calendar day on which such trading ends. The term “trade date” in respect of any confirmed trade in OTC options means the day on which such transaction is accepted by the Corporation for clearance.

Trade Price

(2) The term “trade price” in respect of a confirmed trade [an Exchange transaction] in market baskets of a particular class means the price of such market baskets agreed upon in such transaction. The term “trade price” in respect of a confirmed trade [an Exchange transaction] in BOUNDS means the price of such BOUNDS agreed upon in such transaction.

(3) – (8) [no change]

U. [no change]

V.

Variable Terms

(1) The term “variable terms” in respect of a series of option contracts other than OTC options means the name of the underlying interest, the exercise price (or, in respect of a series of delayed start options that does not yet have a set exercise price, the exercise price setting formula and exercise price setting date), the index value determinant and the index multiplier (in the case of a flexibly structured index option), the cap interval (in the case of a capped option) and the expiration date of such option contract. The term “variable terms” in respect of a series of OTC options means the terms of such options that are permitted to be negotiated bilaterally between the parties within the range of values specified by the Corporation therefor as set forth in the By-Laws and Rules. “Variable terms,” when used in respect of a series of futures means the name of the underlying interest, the maturity date, the method of determining the final settlement price, and the series marker, if any, and in the case of a flexibly structured index future, the index value determinant and the index multiplier.

(2) – (3) [no change]

W.

(1) – (2) [no change]

Writing Clearing Member

(3) The term “Writing Clearing Member” means the Clearing Member acting as, or on behalf of, the writer (as defined, in the case of, in this Article I, and in the case of BOUNDS, in Article XXIV of the By-Laws) of a cleared contract [in an Exchange transaction].

X – Z. [no change]

* * *

ARTICLE V

CLEARING MEMBERS

* * *

Qualifications

SECTION 1. (a) – (d) [no change]

...Interpretations and Policies

.01 [no change]

.02 Operational Capability

a. [no change]

b. the applicant, if an Exchange member or otherwise authorized to compare trades executed on an Exchange, has demonstrated the ability to reconcile [unmatched] unconfirmed and advisory trades on a timely and efficient basis, in accordance with applicable Exchange rules and procedures;

.03 – .05 [no change]

.06 Additional Membership Criteria

If the Membership/Risk Committee determines that the applicant's financial or operational condition, in relation to the business that the applicant is expected to transact with the Corporation, makes it necessary or advisable, for the protection of the Corporation, Clearing Members, or the general public, the Membership/Risk Committee may recommend to the Board of Directors that (i) additional financial requirements be imposed on an applicant for clearing membership, including, but not limited to, requiring such applicant to increase its net capital or to make and maintain an initial margin deposit, or (ii) restrictions be imposed on the applicant's clearance of confirmed trades [Exchange transactions]. The Board of Directors shall independently review such recommendation and shall determine in its discretion whether to impose such requirements or restrictions. Additional requirements or restrictions imposed pursuant to this Section shall remain in force for the period determined by the Board of Directors, but in any event not later than the end of the first three calendar months commencing after the applicant's admission to clearing membership. The imposition of additional requirements or restrictions pursuant to this Section shall not preclude the Corporation from imposing contemporaneous requirements or restrictions pursuant to other provisions of the By-Laws and Rules, including without limitation, Rule 305.

.06 - .09 [no change]

.11 Designation as an OTC Index Option Clearing Member

In order to be designated as an OTC Index Option Clearing Member, a Clearing Member must (i) be a broker-dealer registered under Section 15(b)(1) or (2) of the Securities Exchange Act of 1934 or a Non-U.S. Securities Firm; (ii) execute and maintain in effect such agreements and other documents as the Corporation may prescribe (including, for purposes of clearing OTC index options on indices published by the Standard & Poor's Financial Services LLC ("S&P"), a short-form index license agreement in the form specified from time to time by S&P); (iii) be a user of or participant in an OTC Trade Source for the purpose of affirming and submitting confirmed trades to the Corporation for clearance; and (iv) meet such other requirements as the Corporation may specify. An OTC Index Option Clearing Member shall continue to comply

with all conditions described above until the Clearing Member has closed out all open positions in OTC index options.

Conditions to Admission²

SECTION 3. No applicant shall be admitted as a Clearing Member until the applicant has deposited with the Corporation its initial contribution to the Clearing Fund in the amount required by Article VIII of the By-Laws and has signed and delivered to the Corporation an agreement in such form as the [[Board of Directors]] Corporation shall require, including applicant's agreements (a) to clear through the Corporation, either directly or through another Clearing Member, all of its confirmed trades [Exchange transactions] and all other transactions which the By-Laws or the Rules may require to be cleared through the Corporation, (b) to abide by all provisions of the By-Laws and the Rules and by all procedures adopted pursuant thereto, (c) that the By-Laws and the Rules shall be a part of the terms and conditions of every confirmed trade [Exchange transaction] or other contract or transaction which the applicant, while a Clearing Member, may make or have with the Corporation, or with other Clearing Members in respect of cleared contracts, or which may be cleared or required to be cleared through the Corporation, (d) to grant the Corporation all liens, rights and remedies set forth in the By-Laws and the Rules, (e) to pay to the Corporation all fees and other compensation provided by or pursuant to the By-Laws and the Rules for clearance and for all other services rendered by the Corporation to the applicant while a Clearing Member, (f) to pay such fines as may be imposed on it in accordance with the By-Laws and the Rules, (g) to permit inspection of its books and records at all times by the representatives of the Corporation and to furnish the Corporation with all information in respect of the applicant's business and transactions as the Corporation or its officers may require, (h) to make such payments to or in respect of the Clearing Fund as may be required from time to time, (i) to comply, in the case of Non-U.S. Securities Firms, with the guidelines and restrictions imposed on domestic broker-dealers regarding the extension of credit, as provided by Section 7 of the Securities Exchange Act of 1934 and Regulation T promulgated thereunder by the Board of Governors of the Federal Reserve System, with respect to any customer account that includes cleared contracts issued by the Corporation, (j) to comply, in the case of Non-U.S. Securities Firms, with the Rules of the National Association of Securities Dealers governing maintenance margin and cut-off times for the submission of exercise notices by customers, and (k) to consent, in the case of Non-U.S. Securities Firms, to the jurisdiction of Illinois courts and to the application of United States law in connection with any dispute with the Corporation arising from membership.

...Interpretations and Policies [no change]

* * *

ARTICLE VI

² The text of Section 3 of Article V as presented in this rule change reflects material that is proposed to be added or deleted, but is not yet approved by the Commission. See SR-OCC-2012-12.

CLEARANCE OF CONFIRMED TRADES [EXCHANGE TRANSACTIONS]

* * *

General Clearance Rule

SECTION 1. All confirmed trades [Exchange transactions] shall be cleared through the Corporation, and no other transaction shall be cleared through the Corporation without its consent.

...Interpretations and Policies

.01 (a) Subject to paragraph (c) below, it is the policy of the Corporation to permit a Clearing Member to submit adjustments to its positions with the Corporation to (1) effect a transfer of accounts between Clearing Members; (2) effect a Return, (3) effect a CMTA Retransfer; (4) correct a bona fide error or omission regarding a confirmed trade [an Exchange transaction] previously submitted to the Corporation by the Exchange, security futures market, futures market, futures market, [or] international market or OTC Trade Source on which such confirmed trade [Exchange transaction] occurred or was affirmed; (5) grant a request for offset pursuant to Rule 1306; and (6) effect a retender in connection with the settlement of a physically-settled commodity future pursuant to Rule 1307. Such data shall be submitted in such form and within such times as the Corporation shall prescribe. Such adjustments shall be treated as confirmed trades [Exchange transactions] for the purposes of Sections 15 and 16 of Article VI of the By-Laws and for the purposes of other sections of Article VI except where the context otherwise requires. Notwithstanding the foregoing, adjustment of positions in OTC Options shall be a manual process and subject to such procedures as the Corporation may specify from time to time.

(b) – (c) [no change]

.02 On an expiration date, a Clearing Member may submit adjustments to its positions only to correct bona fide errors or omissions with respect to confirmed trades [Exchange transactions] in expiring options series. Such adjustments shall be submitted in such form and at such times as may be prescribed by the Corporation but no later than the deadline for submitting exercise instructions prescribed pursuant to Rule 805(b).

Responsibility of Clearing Members for Confirmed Trades [Exchange Transactions]

SECTION 2. Every Clearing Member shall be responsible for the clearance of the confirmed trades [Exchange transactions] of the Clearing Member and of the confirmed trades [Exchange transactions] transferred to one of its accounts pursuant to a registered CMTA arrangement as further specified in Rule 403.

Maintenance of Accounts

SECTION 3. Every Clearing Member may establish and maintain with the Corporation one or more of the following accounts:

(a) A firm account, which shall be confined to (i) the confirmed trades [Exchange transactions] in cleared securities other than security futures of such Clearing Member's non-customers, (ii) the confirmed trades [Exchange transactions] in (x) futures other than security futures and (y) futures options and commodity options of persons whose transactions are not required to be treated as the transactions of futures customers, and (iii) the confirmed trades [Exchange transactions] in security futures of persons whose transactions are not required to be treated as the transactions either of securities customers or of futures customers. The Clearing Member, on behalf of itself and each other non-customer on whose behalf positions may be maintained in the firm account, agrees that the Corporation shall have a general lien on all positions and on all other securities, margin and other funds and property in such account, the Corporation shall have the right to net all writing transactions against all purchase transactions effected in such account in accordance with the Rules, and the Corporation may close out the positions in the account and apply the proceeds thereof at any time without prior notice to the Clearing Member or any other non-customer. Such firm account shall be a "firm lien account." The Corporation may also permit each Clearing Member to establish a "firm non-lien account," which shall be confined to those confirmed trades [Exchange transactions] of non-customers of the Clearing Member in respect of which the Clearing Member does not intend to give the Corporation a lien on the segregated long positions in the account (although the Corporation shall have a restricted lien on the unsegregated long positions in securities options and on other securities (including security futures) therein and the proceeds thereof and a general lien on all other property (other than segregated long positions) in such account. The firm non-lien account shall be subject to the same margin requirements as the Clearing Member's customers' account.

(b) A separate Market-Maker's account, which shall be confined to the confirmed trades [Exchange transactions] of the Market-Maker for which it is established. In addition, a Clearing Member who is registered with a Securities Exchange or security futures market as a Market-Maker may maintain a separate Market-Maker's account, which shall be confined to such Clearing Member's confirmed trades [Exchange transactions] as such Market-Maker (including the confirmed trades [Exchange transactions] of a specialist unit in which such Clearing Member is a participant). The Clearing Member agrees, and represents to the Corporation that it has obtained the agreement of each Market-Maker on whose behalf positions may be maintained in a Market-Maker's account, that (i) the Corporation shall have a restricted lien on long positions in securities options and on other securities (including security futures) in such Market-Maker's account and the proceeds thereof and a general lien on all other funds and property in such Market-Maker's account, (ii) the Corporation shall have the right to net all writing transactions against all purchase transactions effected in such account in accordance with the Rules, and (iii) the Corporation may close out the positions in the account, and apply the proceeds thereof, at any time without prior notice to the Clearing Member or Market-Maker, and (iv) notwithstanding the provisions of clause (i) hereof, if the Market-Maker is the Clearing Member or a proprietary Market-Maker, the Corporation shall have a general lien on all positions and on all other securities, margin, and other funds and property in such account, and the account shall be a "firm lien account."

(c) A combined Market-Makers' account, which shall be confined to the confirmed trades [Exchange transactions] of the Market-Makers for which it is established. No confirmed trades [Exchange transactions] of the Clearing Member or proprietary Market-Makers shall be included

in a combined Market-Makers' account that is used for the confirmed trades [Exchange transactions] of Market-Makers that are not proprietary Market-Makers. Likewise, no confirmed trades [Exchange transactions] of associated Market-Makers shall be included in a combined Market-Makers' account that is used for the confirmed trades [Exchange transactions] of Market-Makers that are not associated Market-Makers. The Clearing Member agrees, and represents to the Corporation that it has obtained the agreement of each Market-Maker on whose behalf positions may be maintained in a combined Market-Makers' account, that (i) the positions of such Market-Maker may be commingled in a combined Market-Makers' account with the positions of the Clearing Member acting as Market-Maker or of other proprietary Market-Makers if such Market-Maker is a proprietary Market-Maker; with the positions of other associated Market-Makers if such Market-Maker is an associated Market Maker, or with other Market-Makers that are not proprietary or associated Market-Makers if such Market-Maker is not a proprietary or associated Market-Maker; (ii) the Corporation shall have a restricted lien on all long positions in securities options and on other securities (including security futures) in such combined Market-Makers' account and the proceeds thereof and a general lien on all other funds and property in such combined Market-Makers' account, (iii) the Corporation shall have the right to net all writing transactions against all purchase transactions effected in such account in accordance with the Rules, (iv) the Corporation may close out the positions in the account, and apply the proceeds thereof, at any time without prior notice to the Clearing Member or Market-Maker, and (v) notwithstanding the provisions of clause (i) hereof, if a combined Market-Makers' account is confined to the confirmed trades [Exchange transactions] of the Clearing Member and proprietary Market-Makers, the Corporation shall have a general lien on all positions and on all other securities, margin, and other funds and property in such account, and the account shall be a "firm lien account."

(d) [no change]

(e) Every Clearing Member conducting a public business in which it effects confirmed trades [Exchange transactions] for securities customers shall also establish and maintain a customers' account, which shall be confined to the confirmed trades [Exchange transactions] of such Clearing Member's securities customers. The Clearing Member, on behalf of itself and each securities customer on whose behalf positions may be maintained in the customers' account, agrees that the Corporation shall have a restricted lien on all unsegregated long positions in securities options and on all other securities (other than segregated long positions) (including security futures) in such account and the proceeds thereof, and on all other funds and property in such account (other than segregated long positions).

(f) Every Clearing Member conducting a public business in which it effects confirmed trades [Exchange transactions] for futures customers shall also establish and maintain a segregated futures account, which shall be confined to the confirmed trades [Exchange transactions] in futures, futures options and commodity options of such Clearing Member's futures customers. Notwithstanding the preceding sentence, in the case of those futures customers for which a Clearing Member effects transactions that are futures professionals, the Clearing Member is not required to maintain a segregated futures account under this paragraph (f), but instead may maintain a segregated futures professional account, as provided in paragraph (j) below. The Clearing Member, on behalf of itself and each futures customer on whose behalf positions may be maintained in the segregated futures account, agrees that the Corporation shall have a

restricted lien on all positions, margin and other funds and property in such account as security for the Clearing Member's obligations to the Corporation for the positions in that account and in any segregated futures professional account maintained by the Clearing Member pursuant to paragraph (j) below. The Corporation shall comply with applicable regulations of the Commodity Futures Trading Commission pertaining to the holding of segregated funds by clearing organizations of contract markets.

(g) [no change]

(h) A JBO Participants' account, which shall be confined to the confirmed trades [Exchange transactions] of the JBO Participants for which it is established. The Clearing Member agrees, and represents to the Corporation that it has obtained the agreement of each JBO Participant on whose behalf positions may be maintained in the JBO Participants' account, that (i) the positions of such JBO Participant may be commingled with the positions of other JBO Participants, (ii) the Corporation shall have a restricted lien on all long positions in securities options and on all other securities (including security futures), in such JBO Participants' account and a general lien on all other funds and property in such JBO Participants' account with the Clearing Member (iii) the Corporation shall have the right to net all writing transactions against all purchase transactions effected in such accounts in accordance with the Rules, and (iv) the Corporation may close out positions in the account, and apply the proceeds thereof, at any time without prior notice to the Clearing Member or JBO Participant. Except for purposes of Chapter IV of the Rules, or where the context requires otherwise, all provisions in the By-Laws and the Rules which apply to Market-Makers or a Market-Maker account with the Corporation shall be deemed to apply with equal force to JBO Participants and to a JBO Participants' account with the Corporation, and all references in the By-Laws and the Rules to Market-Makers shall be deemed to also refer to JBO Participants.

(i) [no change]

(j) A segregated futures professional account, which shall be confined to the confirmed trades [Exchange transactions] in futures, futures options and commodity options of the Clearing Member's futures customers who are futures professionals. The Clearing Member, on behalf of itself and each futures professional on whose behalf positions may be maintained in the segregated futures professional account, agrees that the Corporation shall have a restricted lien on all positions, margin and other funds in such account as security for the Clearing Member's obligations to the Corporation arising from that account and any segregated futures account maintained by the Clearing Member pursuant to paragraph (f) above and that the Corporation may close out the positions in the account and apply the proceeds thereof at any time without prior notice to the Clearing Member or any futures professional. The Corporation shall comply with applicable regulations of the Commodity Futures Trading Commission pertaining to the holding of segregated funds by clearing organizations of contract markets.

(k) A proprietary futures professional account, which shall be confined to the confirmed trades [Exchange transactions] of futures professionals whose transactions are not required to be treated as the transactions of securities customers or of futures customers. The Clearing Member, on behalf of itself and each other futures professional on whose behalf positions may be maintained in the proprietary futures professional account, agrees that the Corporation shall have a general lien on all positions and on all other securities, margin and other funds in such account, and the

Corporation may close out the positions in the account and apply the proceeds thereof at any time without prior notice to the Clearing Member or any futures professional. Such account shall be a “firm lien account.”

...Interpretations and Policies:

.01 [no change]

.02 In any “proprietary account” a Clearing Member is permitted to carry both cleared contracts that are “securities” as defined in Section 3(a)(10) of the Securities Exchange Act of 1934 and cleared contracts that are commodity futures, futures options or commodity options subject to regulation under the Commodity Exchange Act, and the margin requirements applicable to any such proprietary account shall be determined under Rule 601 based upon the net liquidating value of all positions carried in the account. Accordingly, all such proprietary accounts are deemed to be held subject to a “cross-margining agreement or similar arrangement” for purposes of Section 561(b)(3)(A) of the United States Bankruptcy Code (11 U.S.C. § 561(b)(3)(A)) and any netting performed between cleared contracts that are securities, on the one hand, and cleared contracts that are commodity futures, futures options or commodity options, on the other, including any close-out netting that is performed in accordance with Section 27 of Article VI of the By-Laws or Chapter XI of the Rules, shall be deemed to occur pursuant to such cross-margining agreement or similar arrangement. For purposes of this interpretation, a “proprietary account” includes (i) a firm account, (ii) a separate Market-Maker’s account for which the Market-Maker is a Clearing Member or a proprietary Market-Maker trading for his own account, (iii) a combined Market-Maker’s account confined to the confirmed trades [Exchange transactions] of Market-Makers who are Clearing Members or proprietary Market-Makers trading for their own accounts, (iv) an OCC proprietary X-M account (together with the corresponding proprietary X-M account at a participating futures clearing organization), or (v) a proprietary futures professional account and any other account that does not contain positions or other property of any person who is a “customer” within the meaning of the Commodity Exchange Act and regulations thereunder.

.03 – .07 [no change]

.08 As used in this Section 3: (i) the phrase “all long positions, securities, margin and other funds” is deemed to include any “investment property” as that term is defined in Article 9 of the Uniform Commercial Code (including long and short positions in security futures) and any other asset in the applicable account;[:] (ii) the phrase “obligations to the Corporation in respect of all confirmed trades [Exchange transactions]” includes any and all obligations arising directly or indirectly from a confirmed trade [an Exchange transaction], including, without limitation, (a) obligations relating to any long or short position in any cleared contract that is created in a confirmed trade [an Exchange transaction], (b) any obligation to make a cash payment, or physical delivery of an underlying interest, resulting from the exercise of, assignment of an exercise notice to, or maturity of such a cleared contract, and (c) any fees or charges imposed by the Corporation with respect to such confirmed trades [Exchange transactions]; and (iii) references to securities or other property “in” an account includes any securities or other property that are identified as deposited as margin in respect of such account.

.09 Notwithstanding anything to the contrary in this Section 3, confirmed trades in OTC options shall be effected, and positions in OTC options shall be maintained, only in a Clearing Member's firm account, separate Market-Maker's account, combined Market-Makers' account or securities customers' account, as applicable. Confirmed trades in certain classes of OTC options, as specified by the Corporation from time to time, for which resulting positions are to be carried in a securities customers' account must be submitted to the Corporation with a customer ID assigned by the OTC Trade Source for the limited purpose of identifying whether a transaction in an OTC Option was an opening transaction or a closing transaction.

Obligation of Purchasing Clearing Members

SECTION 4. The Purchasing Clearing Member in a confirmed trade [an Exchange transaction] in respect of a cleared contract other than a future shall be obligated to pay the Corporation the amount of the premium agreed upon in such [Exchange] transaction. In the event that the Corporation fails to receive such payment at or before the settlement time, the Corporation shall have the right to apply any funds credited to accounts of the Clearing Member with the Corporation or that are otherwise in the possession or at the disposal of the Corporation to the payment of such premium; provided, however, that the Corporation shall not apply funds in a customers' account, segregated futures account (including a segregated futures professional account), customers' lien account, Market-Maker's account (if the Market-Maker is a customer) or in a combined Market-Makers' account (if the Market-Makers are customers) for the payment of premiums on transactions in any account other than such account. Notwithstanding any other provision of the By-Laws or Rules, if the Corporation accepts an opening purchase transaction in an account at a time when the Corporation has not received payment of all amounts due from the Purchasing Clearing Member in respect of such account, the long position resulting from the acceptance of such transaction by the Corporation shall be deemed to be an unsegregated long position, and the Corporation shall have the right to close out or, in the case of options, to exercise such long position and to apply the proceeds in accordance with Chapter XI of the Rules.

Obligations of the Corporation

SECTION 5. Upon the acceptance of a confirmed trade [an Exchange transaction] by the Corporation, the Corporation shall be substituted through novation as the buyer to the seller and the seller to the buyer, the rights of the parties to such transaction shall be solely against the Corporation and the Corporation shall be obligated to the parties in accordance with the provisions of the By-Laws and the Rules. Subject to Sections 7 and 8 of this Article VI, a confirmed trade [an Exchange transaction] shall be deemed to have been accepted by the Corporation at the commencement time specified in this Section 5 for such confirmed trade [Exchange transaction]. Except as provided (i) in Section 7 of Article XII in respect of futures issued in exchange-for-physical transactions, block trades, or other trades designated by a futures market or security futures market reporting the trades as non-competitively executed trades, (ii) in Section 1 of Article XX in respect of cross-rate foreign currency options, [and] (iii) in Section 1 of Article XXIII in respect of foreign currency index options, and (iv) in this Section 5 in

respect of OTC options, the commencement time for a cleared contract is the time at which the Corporation makes available to the Purchasing Clearing Member and the Selling Clearing Member Daily Position Reports reflecting the **confirmed trade** [Exchange transaction] in which such cleared contract was purchased, provided that the commencement time for a cleared contract in respect of which the Corporation receives [matching] **confirmed** trade information on the expiration date or maturity date for such contract, or if such date is not a business day, on the immediately preceding business day, means the close of trading on the Exchange on which such transaction was effected on such expiration or maturity date or immediately preceding business day, as the case may be. **The acceptance of confirmed trades in, and the commencement time for, an OTC option shall be the time at which the Corporation's report of its acceptance of the confirmed trade relating to such OTC option is made available to the Clearing Member within the Corporation's clearing system; provided, however, that in the case of a confirmed trade in a Backloaded OTC option, such a confirmed trade shall not be deemed accepted, and may be rejected, by the Corporation until the Selling Clearing Member has met its regular morning cash settlement obligations to the Corporation on the following business day. A Backloaded OTC option will not be accepted for clearing by the Corporation if the Corporation receives such Backloaded OTC option from the relevant OTC Trade Source after 4:00 P.M. Central Time (5:00 P.M. Eastern Time on the business day that is four business days prior to the expiration date of the Backloaded OTC option.**

Upon the acceptance of a confirmed trade [an Exchange transaction] in respect of cleared contracts, the Corporation shall be obligated as follows:

- (a) In an opening purchase transaction, the Corporation shall be obligated to issue to the Purchasing Clearing Member the number of cleared contracts purchased in such [Exchange] transaction.
- (b) In a closing purchase transaction, the Corporation shall be obligated to reduce the Purchasing Clearing Member's short position in the cleared security in which the [Exchange] transaction was effected by the number of contracts purchased in such [Exchange] transaction.
- (c) In an opening or closing writing transaction, the Corporation shall be obligated to pay, at the time and in the manner specified by the Rules, the Writing Clearing Member the amount of the premium agreed upon in such [Exchange] transaction.

...Interpretations and Policies:

.01 The Corporation will accept for clearing [matched]**confirmed** trades in flexibly structured options and flexibly structured security futures, provided that the variable terms of the contract comply with any limitations on such variable terms published by the Corporation from time to time by notice to the Exchanges that have clearing agreements with the Corporation.

Issuance of Cleared Contracts

SECTION 6. The Corporation shall be the issuer of all cleared contracts purchased in confirmed trades [Exchange transactions]. Subject to the provisions of Sections 7 and 8 of this Article VI, a cleared contract shall be issued by the Corporation in every opening purchase transaction at the commencement time for such transaction. Any such cleared contract shall carry the rights and

obligations set forth in the By-Laws and Rules applicable to the particular cleared contract and shall contain the variable terms as agreed upon by the Purchasing Clearing Member and Selling Clearing Member (or by Exchange Members authorized to give up the names of such Clearing Members), as shown on the trade information filed by them with the Exchange on which such opening purchase transaction occurred or the OTC Trade Source through which such transaction was affirmed and which is transmitted to the Corporation in a report of [matched] confirmed trades submitted by such Exchange or OTC Trade Source. (In the event of a discrepancy between the trade information filed with the Exchange or OTC Trade Source and the information reported to the Corporation, the latter shall govern as between the Clearing Member and the Corporation.) Unless and until a cleared contract is issued as provided by the By-Laws, the Corporation shall have no obligation in respect thereof.

...Interpretations and Policies [no change]

Reporting of [Matched] Confirmed Trades

SECTION 7. (a) The acceptance of every confirmed trade [Exchange transaction] and the issuance of every cleared contract by the Corporation as provided in Sections 5 and 6 of this Article VI shall be subject to the condition that the Exchange or OTC Trade Source on which such [Exchange] transaction occurred or was affirmed [occurs] shall have reported to the Corporation, during such times as the Corporation shall prescribe, [matching] confirmed trade information with respect to such transaction showing that the trade information submitted by the Purchasing Clearing Member and the Selling Clearing Member agree:

(i) in the case of option contracts or BOUNDS, as to (1) the identity of the other party to the transaction, (2) in the case of option contracts, the type of option contract, (3) the ticker symbol for the option contract or BOUND, (4) the variable terms of the option contract or BOUND (5) the amount of the premium, (6) the number of contracts or BOUNDS, and (7) the description of the parties as purchaser and writer; and

(ii) in the case of futures, as to (1) the identity of the other party to the transaction, (2) the variable terms, (3) the number of contracts, and (4) the description of the parties as buyer and seller.

(b) The Corporation shall have no obligation to any purchaser, writer, buyer, or seller for any loss resulting from the untimely reporting by an Exchange, [or] market, or OTC Trade Source of any [matching] confirmed trade information or from any error in [matching] confirmed trade information furnished to the Corporation.

(c) An Exchange or OTC Trade Source may instruct the Corporation to disregard a transaction previously reported by such Exchange or OTC Trade Source as a [matched] confirmed trade because of a subsequent determination that (i) the trade information submitted by the Purchasing Clearing Member and Selling Clearing Member did not agree, (ii) the trade information did not contain all the information required by the Corporation as set forth in the By-Laws and Rules, or (iii) new or revised trade information was required to properly clear the transaction. In accordance with such instruction, the Corporation shall disregard the previously reported transaction and such transaction shall be deemed null and void and given no effect for purposes

of the By-Laws and Rules. The Corporation shall have no obligation to any purchaser, writer, buyer, or seller in acting pursuant to an Exchange's of OTC Trade Source's instruction to disregard a previously reported transaction.

Payments to Corporation

SECTION 8. Except as provided (i) in Section 7 of Article XII in respect of futures issued in exchange-for-physical transactions, block trades, or other trades designated by a futures market or security futures market reporting the trades as non-competitively executed trades, (ii) in Section 5 of Article XX in respect of cross-rate foreign currency options, [and] (iii) in Section 7 of Article XXIII in respect of foreign currency index options, and (iv) in this Section 8 with respect to certain OTC options, the Corporation shall have no right to reject any confirmed trade [Exchange transaction] or to refuse to issue any cleared contract as a consequence of the failure of the Purchasing Clearing Member to pay any amount due to the Corporation at or before the settlement time for such [Exchange] transaction. In the case of any confirmed trade for any Backloaded OTC option, the Corporation may reject such confirmed trade if the Selling Clearing Member fails to meet its initial margin obligations to the Corporation in respect of such Backloaded OTC option when due.

General Rights and Obligations of Holders and Writers

SECTION 9. (a) *Call Option Contracts.* Subject to the provisions of the By-Laws and Rules of the Corporation, the holder of a single American-style call option contract has the right, beginning at the time such option contract is issued pursuant to this Article VI and expiring at the expiration time therefor on the expiration date [the Saturday immediately following the third Friday of the expiration month] of such option contract, to purchase from the Corporation at the aggregate exercise price the number of units of the underlying security represented by such option contract, all in accordance with Exchange Rules and the By-Laws and Rules. Subject to the provisions of the By-Laws and Rules of the Corporation, the holder of a single European-style call option contract has the right on (and only on) the expiration date, expiring at the expiration time therefor on such date, to purchase from the Corporation at the aggregate exercise price the number of units of the underlying security represented by such option contract, all in accordance with Exchange Rules and the By-Laws and Rules. The writer of a single call option contract is obligated, upon the assignment to him of an exercise notice in respect of such option contract, to deliver the number of units of the underlying security represented by such option contract against payment of the aggregate exercise price, all in accordance with Exchange Rules and the By-Laws and Rules.

(b) *Put Option Contracts.* Subject to the provisions of the By-Laws and Rules of the Corporation, the holder of a single American-style put option contract has the right, beginning at the time such option contract is issued pursuant to this Article VI and expiring at the expiration time therefor on the expiration date [the Saturday immediately following the third Friday of the expiration month] of such option contract, to sell to the Corporation at the aggregate exercise price the number of units of the underlying security represented by such option contract, all in

accordance with Exchange Rules and the By-Laws and Rules. Subject to the provisions of the By-Laws and Rules of the Corporation, the holder of a single European-style put option contract has the right on (and only on) the expiration date, expiring at the expiration time therefor on such date, to sell to the Corporation at the aggregate exercise price the number of units of the underlying security represented by such option contract, all in accordance with Exchange Rules and the By-Laws and Rules. The writer of a single put option contract is obligated upon the assignment to him of an exercise notice in respect of such option contract, to pay the aggregate exercise price against delivery of the number of units of the underlying security represented by such option contract, all in accordance with Exchange Rules and the By-Laws and Rules.

(c) [no change]

...Interpretations and Policies [no change]

Terms of Cleared Contracts

SECTION 10. (a) [no change]

(b) Except to the extent provided otherwise in the next sentence with respect to delayed start options and except to the extent provided otherwise in the By-Laws and Rules with respect to transactions in flexibly structured options or OTC options, the expiration date and exercise price and, (i) in the case of capped option contracts, the cap interval (as defined, in the case of capped cash-settled option contracts, in Article XVII of the By-Laws), and (ii) in the case of packaged spread options, the base exercise price and spread interval (as defined in Article XXVI of the By-Laws), of option contracts of each series of options shall be determined by each Exchange at the time such series of options is first opened for trading on that Exchange. In the case of delayed start options, the exercise price setting date and the exercise price setting formula of option contracts of each series shall be determined by the Exchange at or before the time such series of options is first opened for trading on that Exchange. The unit of trading of option contracts of each series of options shall be designated by the Corporation prior to the time such series of options is first opened for trading, and in the absence of such designation for a series of options in which the underlying security is a common stock, the unit of trading shall be 100 shares. The unit of trading and exercise price established for an option contract are subject to adjustment in accordance with the By-Laws.

(c) – (f) [no change]

(g) New series of cleared contracts may generally be opened on a same day or next day basis; provided, however, that no series of cleared contracts shall be opened for trading without the consent of the Corporation unless the Corporation shall have received prior notice thereof from the Exchange not later than the applicable deadline for new series established from time to time by the Corporation. The Corporation may require a longer notice period for new series of cleared contracts having as a contract month, maturity date or expiration month a calendar month that is not then, or was not during the prior calendar year, in use for any other series of cleared contract. Series of flexibly structured cleared contracts may be subject to different notice periods than those applicable to other cleared contracts. Notwithstanding any other provision of this Section 10, a new series of OTC options may be opened on the date a confirmed trade in OTC options is

accepted by the Corporation for clearing and all OTC options covering the same underlying interest and having identical terms shall be considered to be in the same series.

...Interpretations and Policies [no change]

Closing Sale Transactions

SECTION 15. A Clearing Member shall not effect a closing sale transaction in an account unless, at the time of such transaction, such Clearing Member has a long position in such account for at least the number of cleared contracts involved in such transaction. In the event any [Exchange] transaction of a Clearing Member is recorded as a closing sale transaction in the [matching] confirmed trade information reported in respect of such transaction and the Clearing Member does not have a long position in the applicable account for at least the number of cleared contracts involved in such transaction, then the transaction shall be deemed to be an opening sale transaction to the extent that the number of cleared contracts involved in such transaction exceeds the number of cleared contracts in such long position. A Selling Clearing Member in a closing sale transaction involving a cleared contract agrees that, upon the Corporation's acceptance of such transaction, the Corporation shall reduce the Clearing Member's long position in the account through which the transaction was effected by the number of cleared contracts involved.

Closing Purchase Transactions

SECTION 16. A Clearing Member shall not effect a closing purchase transaction in an account unless, at the time of such transaction, such Clearing Member has a short position in such account for at least the number of cleared securities involved in such transaction. In the event any [Exchange] transaction of a Clearing Member is recorded as a closing purchase transaction in the [matching] confirmed trade information reported in respect of such transaction and the Clearing Member does not have a short position in the applicable account for at least the number of cleared securities involved in such transaction, then the transaction shall be deemed to be an opening purchase transaction to the extent the number of cleared securities involved in such transaction exceeds the number of cleared securities in such short position.

Certain Delays

SECTION 18. (a) Anything in these By-Laws or the Rules notwithstanding, in the event that the Corporation is unable for any reason (i) to make available, pursuant to Chapter VIII of the Rules, any Expiration Exercise Report, or (ii) to receive properly submitted exercise instructions from Clearing Members, prior to 5:00 P.M. Central Time (6:00 P.M. Eastern Time) on any expiration date that is immediately followed by a day that is not a business day, the Corporation shall make available the delayed report or accept such exercise instructions as soon as practicable thereafter, provided that the Corporation may, in its discretion, defer making the delayed report available or accepting such instructions until 7:00 A.M. Central Time (8:00 A.M. Eastern Time) or as soon as

practicable thereafter on the non-business day immediately following such expiration date, or, if such expiration date is followed by more than one consecutive non-business day, on such of those days as the Corporation shall specify. In any such event, Clearing Members shall submit exercise instructions to the Corporation on such non-business day within such times and in such manner as the Corporation shall prescribe. Exercise instructions submitted by a Clearing Member to the Corporation within time limits fixed pursuant to this subsection shall be deemed to have been duly given prior to the expiration of the option contracts to which they relate. Notwithstanding the foregoing, no Expiration Exercise Report shall under any circumstances be made available by the Corporation, nor shall any exercise instructions be accepted by the Corporation, after 11:00 P.M. Central time (12:00 midnight Eastern Time) on the last consecutive non-business day immediately following the expiration date.

(b) In the event that the Corporation (i) fails to make Expiration Exercise Reports available to Clearing Members, or is unable to receive properly submitted exercise instructions from Clearing Members in response to such reports, prior to 11:00 P.M. Central Time (12:00 midnight Eastern Time) on the last consecutive non-business day immediately following the expiration date (in cases to which subsection (a) applies) or on the expiration date (in all other cases), and (ii) has failed to prescribe alternative procedures for exercising expiring options pursuant to Rule 805, or determines in its discretion, and so advises Clearing Members, that procedures so prescribed were inadequate, then each Clearing Member shall be deemed to have properly and irrevocably tendered to the Corporation, on a timely basis, an exercise notice with respect to:

(1) every expiring option contract in each of the Clearing Member's accounts which is deemed to have been exercised pursuant to Rule 805(d)(2) as supplemented, in the case of options contracts other than stock options, by the Rules in the Chapter applicable to such other option contracts, except to the extent that the Clearing Member has given the Corporation written instructions, prior to 11:00 P.M. Central Time (12:00 midnight Eastern Time) on the last consecutive non-business day immediately following the expiration date (in cases to which subsection (a) applies) or on the expiration date (in all other cases) to exercise none, or fewer than all, of the option contracts in such series carried in such account; and

(2) every other expiring option contract in any of the Clearing Member's accounts which the Clearing Member has given the Corporation written instructions to exercise prior to 11:00 P.M. Central Time (12:00 midnight Eastern Time) on the last consecutive non-business day immediately following the expiration date (in cases to which subsection (a) applies) or on the expiration date (in all other cases).

Exercise notices deemed to have been tendered pursuant to this subsection shall be deemed to have been duly filed prior to the expiration of the option contracts to which they relate. No exercise notice shall be deemed to have been tendered to the Corporation in respect of any non-equity securities option contract pursuant to subsection (b)(1) above if the Corporation has not established price intervals applicable to such option contract for the purposes of Rule 805(d)(2).

(c) In the event the Corporation should for any reason be unable to assign an exercise notice prior to any hour prescribed in the Rules, the Corporation shall assign such exercise notice as soon as practicable thereafter and shall fix such date of assignment and exercise settlement date as it, in its discretion, shall deem fair and reasonable in the circumstances.

(d) Any action taken by the Corporation pursuant to this Section 18 shall be reported by the Corporation to the Securities and Exchange Commission within two business days thereafter.

(e) Paragraphs (a) and (b) of this Section 18 shall be inapplicable to options that are subject to automatic exercise. Automatic exercise of such options shall be effected without regard to any delay in making available an Expiration Exercise Report with respect to such options.

Clearance of International Transactions

SECTION 20. International transactions shall be cleared in accordance with the By-Laws and Rules; provided, however, that the times specified in the By-Laws and Rules for the availability of any report, or the payment of any amount, due to or from a Clearing Member in respect of international transactions and positions in international options may be altered as determined by the Corporation from time to time in accordance with an international market agreement. All international transactions, positions in international option contracts, margin requirements arising therefrom, and exercises and assignments of exercise notices in respect of international option contracts may be reported separately from other confirmed trades [Exchange transactions] and option contracts in daily reports, Daily Margin Reports, Exercise Settlement Reports and other reports made available in connection with the By-Laws and Rules and the procedures of the Corporation; and premium, margin and exercise settlements in respect of such international transactions and positions in international option contracts may be conducted in accordance with the By-Laws and Rules.

...Interpretations and Policies [no change]

Classes of Options Cleared Through ICS

SECTION 22. Certain classes of options may from time to time be designated by the Corporation for clearance through ICS. Positions in, and exercises and assignments of exercise notices in respect of, classes of options cleared through ICS may be reported to Clearing Members in reports that are separate from similar reports relating to other classes of options, and reports relating to classes of options cleared through ICS may be distributed to Clearing Members at times other than the times when reports relating to other classes of options are distributed. The deadline for filing of exercise notices in respect of options cleared through ICS may be earlier than the deadline in respect of other classes of options. Except as otherwise expressly provided or where the context clearly requires otherwise, all confirmed trades [Exchange transactions] cleared through ICS that take place in trading sessions conducted after 3:00 P.M. Central Time (4:00 P.M. Eastern Time) shall be deemed for purposes of the By-Laws and Rules to have been effected on the following business day.

...Interpretations and Policies [no change]

Close-Out Netting

SECTION 27. (a) *Default or Insolvency of the Corporation.* If at any time the Corporation: (i) fails to comply with an undisputed obligation to pay money or deliver property to a Clearing Member under the By-Laws or Rules for a period of thirty days from the date that OCC receives notice from the Clearing Member of the past due obligation, (ii) institutes or has instituted against it a proceeding seeking a judgment of insolvency or bankruptcy or any other relief under any bankruptcy or insolvency law or other similar law affecting creditors' rights, or a petition is presented for its winding up or liquidation, and, in the case of any such proceeding or petition presented against it, such proceeding or petition results in a judgment of insolvency or bankruptcy or the entry of an order for relief or the making of an order for the Corporation's winding-up or liquidation, or (iii) takes corporate action to authorize any proceeding or petition described in clause (ii) above, the Corporation or its representative shall promptly notify the Securities and Exchange Commission, the Commodity Futures Trading Commission, all Clearing Members, any clearing organizations with which the Corporation has cross-margining or cross-guarantee arrangements, and all Exchanges, futures markets and security futures markets for which the Corporation clears confirmed trades [Exchange transactions] and all OTC Trade Sources from which OCC accepts confirmed trades for clearance.

(b) *Notice of Termination.* Upon the occurrence of any event described in clause (i) through (iii) of paragraph (a), a Clearing Member that is neither suspended nor in default with respect to any obligation owing to the Corporation may notify the Corporation in writing of its intention to terminate all cleared contracts and stock loan and borrow positions in all accounts of such Clearing Member; provided that a notice based on the Corporation's failure to comply with an obligation described in clause (i) may only be made by the Clearing Member to whom such obligation is owed. The Corporation shall promptly forward any such notice, specifying the date of receipt thereof, to the Securities and Exchange Commission, the Commodity Futures Trading Commission, all Clearing Members, any clearing organizations with which the Corporation has cross-margining or cross-guarantee arrangements, and all Exchanges, futures markets and security futures markets for which the Corporation clears confirmed trades [Exchange transactions] and all OTC Trade Sources from which OCC accepts confirmed trades for clearance. Such notice shall have the effects hereinafter described in this Section with respect to all Clearing Members, without the necessity of a similar notice being sent by any other Clearing Member. As of the close of business on the third business day following the Corporation's receipt of such notice or such other termination time as may be established by the United States Bankruptcy Code in the case of a proceeding governed by such Code (the "Termination Time"), the Corporation shall accept no more confirmed trades [Exchange transactions] for clearing, and all pending transactions, positions in cleared contracts and stock loan and borrow positions remaining in all accounts of all Clearing Members at the Termination Time shall be valued as of the Termination Time and liquidated in accordance with this Section. Such liquidated positions shall be netted to the maximum extent permitted by law and the By-Laws and Rules, and settlement of the net amounts shall be effected in the manner provided by this Section in satisfaction of all obligations owing between the Corporation and Clearing Members in respect of such positions. The provisions of this Section, other than paragraph (l) below, shall not apply to the disposition of assets and liabilities in any X-M account provided for in Article VI, Section 24 of the By-Laws. From and after the Termination Time the rights of Clearing Members against the Corporation shall be limited to those set forth in this Section. In the event that a Clearing Member is suspended by the Corporation pursuant to Chapter 11 of the Rules or the Corporation

suffers a loss from any cause that is chargeable against the Clearing Fund in accordance with the By-Laws and Rules, whether such suspension or loss occurs before or after the Corporation gives a notice under this paragraph (a), the provisions of paragraph (m) below shall apply.

(c) – (m) [no change]

* * *

ARTICLE VIII

CLEARING FUND

* * *

Maintenance and Purposes 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 (i) as a result of the failure of any Clearing Member to discharge duly any obligation on or arising from any confirmed trade [Exchange transaction] 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.

(b) [no change]

Application of Clearing Fund

SECTION 5. (a) If (i) any Clearing Member shall fail to discharge duly any obligation on or arising from any confirmed trade [Exchange transaction] 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.

For the purposes of this paragraph, any amount owed by the Corporation to a Participating CCO pursuant to a Participating CCO Agreement as the result of the liquidation of sets of X-M accounts shall be deemed to be a loss suffered by the Corporation upon the liquidation of positions in non-equity securities options.

(b) – (g) [no change]

...**Interpretations and Policies** [no change]

Contribution Refund

SECTION 7. Whenever a Clearing Member definitively ceases to be such, the amount of its contribution to the Clearing Fund shall be returned to it, but not until all confirmed trades [Exchange transactions] and open positions of the Clearing Member from which losses or payments chargeable to the Clearing Fund might result have been fulfilled or closed, or, with the approval of the Corporation, another Clearing Member has been substituted thereon. All amounts chargeable against a Clearing Member's contribution to the Clearing Fund on account of transactions that occurred while it was a Clearing Member, including proportionate charges and unpaid fees, shall be deducted from the amount returned. For purposes of this Section 7, a Clearing Member will be deemed to have definitively ceased to be a Clearing Member at such time as it has fulfilled all requirements of Sub-Sections (i) through (iii) of Section 6 of this Article and has met all outstanding obligations to the Corporation.

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ARTICLE XII

FUTURES, FUTURES OPTIONS AND COMMODITY OPTIONS

* * *

SECTION 1. — SECTION 6. [no change]

SECTION 7. The acceptance by the Corporation of any futures transaction that is identified as an “exchange-for-physical” or “EFP,” a “block trade,” or any other non-competitively executed trade in [matching] confirmed trade information reported by an Exchange or in any instruction submitted directly to the Corporation by a Clearing Member, as applicable, shall be subject to the condition that the Corporation shall have received any variation payments due in the accounts of the purchasing and selling Clearing Members in which the transaction was effected at the first variation settlement after the transaction was reported to the Corporation. Unless such a transaction is rejected as hereinafter provided, the time of such variation settlement shall be the commencement time of the transaction. In the event that the Corporation fails to receive any such variation payment when due, the Corporation may (either by a general rule or resolution adopted by the Board of Directors or by action of the officers of the Corporation with respect to specific transactions) reject the transaction. In the event that the transaction is rejected as herein provided, the Corporation shall promptly notify, either orally or in writing, the Clearing Members party to the transaction, and such Clearing Members shall have the remedies (if any) provided in the rules of the Exchange on which the transaction was effected.

* * *

ARTICLE XIV

BINARY OPTIONS; RANGE OPTIONS

* * *

Definitions

SECTION 1.

A. – L. [no change]

M.

Multiplier

(1) The term “multiplier” when used in respect of a confirmed trade [an Exchange transaction] in binary options means the fixed number by which the price agreed upon by the purchaser and seller is multiplied in order to calculate the total purchase price per contract.

N. – O. [no change]

P.

Premium

(1) The term “premium” when used in respect of a confirmed trade [an Exchange transaction] in binary options or range options means the price, in dollars and cents, agreed upon by the purchaser and seller in the transaction times the multiplier (if applicable) and the number of contracts subject to the [Exchange] transaction.

Q. – Z. [no change]

* * *

ARTICLE XV

FOREIGN CURRENCY OPTIONS

* * *

Definitions

SECTION 1.

A. – O. [no change]

P.

Premium

(1) The term “premium” in respect of a confirmed trade [an Exchange transaction] in foreign currency options is equal to the price per unit of underlying currency of each such option, multiplied by the unit of trading and by the number of contracts subject to the [Exchange] transaction. Premium may be expressed either in units (including fractions, decimals, or multiples of such units) of the trading currency designated by the Exchange on which such options are traded or as a percentage of the amount of underlying currency covered by the transaction. Premium shall be payable in the currency in which it is expressed.

Q. – R. [no change]

S.

Settlement Time

(1) The term “settlement time” in respect of a confirmed trade [an Exchange transaction] in foreign currency options settling in the United States means 9:00 A.M. Central time (10:00 A.M. Eastern time) on the first business day immediately following the day on which the Corporation receives [matching] confirmed trade information in respect of such transaction from the Exchange on which such transaction [Transaction] was effected. The term “settlement time” in respect of a confirmed trade [an Exchange transaction] in foreign currency options settling outside the United States means 11:00 A.M. local time in the country of origin of the trading currency (*i.e.*, the premium currency), or such other time as the Corporation may specify, on the first foreign business day in that country immediately following the business day

on which the Corporation receives [matching] confirmed trade information in respect of such transaction from the Exchange on which such transaction was effected.

T. – Z. [no change]

* * *

ARTICLE XVI

YIELD BASED TREASURY OPTIONS

* * *

Definitions

SECTION 1.

(a) – (k) [no change]

Premium

(l) The term “premium” in respect of a confirmed trade [an Exchange transaction] in yield-based Treasury options means the “per unit” price of each such option, as agreed upon by the purchaser and seller in such transaction, times the multiplier and the number of options subject to the transaction.

(m) – (n) [no change]

* * *

ARTICLE XVII

INDEX OPTIONS AND CERTAIN OTHER CASH-SETTLED OPTIONS

* * *

Introduction

By-Laws in this Article are applicable only to cash-settled options that are not specifically addressed elsewhere in these By-Laws, including Exchange-listed index options, OTC index options [options where the underlying interests are indexes] and cash-settled commodity options other than binary options or range options (which are governed by the provisions of Article XIV). Section 1 of Article XII is also applicable to cash-settled commodity options. By-Laws in Articles I-XI are also applicable to cash-settled options, in some cases supplemented by one or more By-Laws in this Article, except for By-Laws that have been replaced in respect of such options by one or more By-Laws in this Article and except where the context otherwise requires. Whenever a By-Law in this Article supplements or, for purposes of this Article, replaces one or

more By-Laws in Articles I-XI, that fact is indicated in brackets following the By-Law in this Article.

Definitions

SECTION 1.

A. – B. [no change]

C.

(1) – (3) [no change]

Class of Options

(4) The term “class of options” used in respect of cash-settled options means all such options of the same type and style (and, in addition, in the case of flexibly structured index options and OTC index options, having the same index value determinant) and having the same underlying interest, provided that OTC index options shall constitute a separate class of options from other cash-settled options of the same type and style and having the same underlying interest.

Current Underlying Interest Value; Current Index Value

(5) The term “current underlying interest value” when used in respect of cash-settled options means the current value or level of the underlying interest at a point in time as reported by the reporting authority. The current underlying interest value in respect of an index option is sometimes also referred to as the “current index value.” Subject to the provisions of Section 5 of this Article, the term “current index value,” in respect of any underlying index on a given day, means the level of such index at the close of trading on such day, or if such day is not a trading day, on the immediately preceding trading day, or, in the case of an index option other than an OTC index option, any multiple or fraction thereof specified by the Exchange, as such value is reported by the reporting authority. Notwithstanding the foregoing, but subject to the provisions of Section 4 of this Article, the current index value for an index underlying a flexibly structured index option or an OTC index option on the expiration date shall be determined in accordance with the index value determinant.

D. [no change]

E.

(1) – (2) [no change]

Expiration Date

(3) The term “expiration date” in respect of cash-settled options other than flexibly structured options or OTC index options means the Saturday following the third Friday of the expiration month, except that in respect of an option contract that is identified by an Exchange as having an expiration date different from the Saturday following the third Friday of the expiration month, the term “expiration date” shall mean such date as identified by the Exchange at or prior to the time of inception of trading of the class or series, as applicable. The

expiration date of an OTC index option shall be determined as set forth in Section 6 of this Article.

Expiration Time

(4) The term “expiration time” in respect of an OTC index option contract means 7:00 P.M. Central Time (8:00 P.M. Eastern Time).

F. – H. [no change]

I.

Index Component

(1) [no change]

[Index Value Determinant]³

[(3) The term “index value determinant” used in respect of settlement of flexibly structured index option contracts means the method for determining the current index value on the expiration date as that method is reported to the Corporation by the Exchange on which the option was purchased.]

J. – O. [no change]

P.

Premium

(1) The term “premium” in respect of a confirmed trade [an Exchange transaction] in cash-settled options means the price of each such option (expressed in points), as agreed upon by the purchaser and seller in such transaction, times the multiplier or unit of trading, as applicable, and the number of options subject to the transaction.

Put

(2) [no change]

Q. [no change]

R.

Reference Index

(1) [no change]

Reporting Authority

(2) The term “reporting authority” in respect of cash-settled options other than OTC index options means the institution or reporting service designated by an Exchange as the

³ This definition is proposed to be deleted because it is redundant to the definition of the same term in Article I of the By-Laws.

official source for the current value of a particular underlying interest or reference variable. Unless another reporting authority is identified by the listing Exchange for a class of cash-settled options, the listing Exchange will be the reporting authority. In respect of OTC index options, the reporting authority shall be the institution or reporting service designated by the Corporation as the official source for the current value of a particular underlying interest or reference variable.

S.

Series of Options

(1) The term “series of options” used in respect of cash-settled options other than OTC index options means all such options of the same class with the same exercise price (or, in the case of delayed start options that do not yet have a set exercise price, the same exercise price setting formula and exercise price setting date), cap price (if any), unit of trading (if any), expiration date, and multiplier; provided that if an Exchange shall adopt a rule superseding Section 1 C.(5) of this Article, index options (other than OTC index options) to which such Exchange rule applies shall be deemed to be of a different series than otherwise identical index options to which such rule does not apply. In respect of OTC index options, the term “series of options” means all such options of the same class and having identical variable terms.

T. – Z. [no change]

General Rights and Obligations of Holders and Writers of Cash-Settled [Index] Options

SECTION 2. [no change]

Adjustments

SECTION 3.

(a) – (c) [no change]

(d) If an Exchange shall increase or decrease the index multiplier for any index option contract, or the reporting authority shall change the method of calculation of an underlying index or reference index so as to create a discontinuity or change in the level of the index that does not reflect a change in the prices or values of the index securities, or the Corporation shall substitute one underlying index or reference index for another pursuant to paragraph (e) [(d)] of this Section 3, the Corporation shall make such adjustments in the number of outstanding affected options or the exercise prices of such options or such other adjustments, if any, as the Corporation in its sole discretion deems fair to both the holders and the writers of such options.

(e) – (g) [no change]

(h) Except in the case of OTC index options or any of the events described [as otherwise provided] in paragraphs (f) and (g) of this Section 3, determinations with respect to adjustments pursuant to this Section shall be made by an adjustment panel. The provisions of Article VI,

Section 11 of the By-Laws shall apply equally to adjustment panels convened pursuant to this Article XVII, Section 3(g).

...Interpretations and Policies:

.01 For the elimination of doubt, all adjustments to the terms of outstanding cleared contracts in OTC index options shall be made by the Corporation in its sole discretion, based on its judgment as to what is appropriate for the protection of investors and the public interest, taking into account such factors as fairness to holders and writers (or purchasers and sellers) of the affected contracts, the maintenance of a fair and orderly market in the affected contracts, consistency of interpretation and practice (including consistency with adjustments to Exchange-listed index options on the same underlying interest), and efficiency of exercise settlement procedures.

[Section 3 of this Article replaces Section 11A of Article VI of the By-Laws.]

Unavailability or Inaccuracy of Current Underlying Interest Value

Effective for Series of Options Opened for Trading After September 16, 2000

SECTION 4. (a) If the Corporation shall determine that the primary market(s) (as determined by the Corporation) for one or more index components did not open or remain open for trading (or that any such components did not open or remain open for trading on such market(s)) on a trading day at or before the time when the current index value for that trading day would ordinarily be determined, or that a current index value or other value or price to be used as, or to determine, the exercise settlement amount (a "required value") for a trading day is otherwise unreported, inaccurate, unreliable, unavailable or inappropriate for purposes of calculating the exercise settlement amount, then, in addition to any other actions that the Corporation may be entitled to take under the By-Laws and Rules, the Corporation shall be empowered to do any or all of the following with respect to any series of options on such index ("affected series"):

(1) The Corporation may suspend the settlement obligations of exercising and assigned Clearing Members with respect to cash-settled option contracts of the affected series. At such time as the Corporation determines that the required value is available or the Corporation has fixed the exercise settlement amount pursuant to subparagraph (2) of this Section, the Corporation shall fix a new date for settlement of exercised option contracts.

(2) The Corporation may fix the exercise settlement amount for exercised contracts of an affected series. In the case of cash-settled securities options other than OTC index options [options that are securities], the exercise settlement amount shall be fixed by a panel consisting of two designated representatives of each Exchange on which the affected series is open for trading and the Chairman of the Corporation. In the case of OTC index options or cash-settled commodity options, unless the By-Laws or Rules specifically provide otherwise in respect of a particular class of such options, the exercise settlement amount shall be fixed by the Corporation. The Corporation will consult with the Membership/Risk Committee when appropriate to obtain any additional or supplemental market information or data from the members of such committee that the Corporation believes will be useful in setting such exercise settlement value[unless the By-Laws or Rules specifically provide otherwise in respect of a particular class of commodity options]. The panel (or the Corporation, as the case may be) shall fix the exercise settlement

amount based on its judgment as to what is appropriate for the protection of investors and the public interest, taking into account such factors as fairness to holders and writers of options of the affected series, the maintenance of a fair and orderly market in such affected series of options, consistency of interpretation and practice, and consistency with actions taken in related futures or other markets. Without limiting the generality of the foregoing, the panel (or the Corporation) may fix the exercise settlement amount using: (i) the reported price or value for the relevant security(ies), commodity(ies) or underlying interest at the close of regular trading hours (as determined by the Corporation) on the last preceding trading day for which such a price or value was reported by the reporting authority; (ii) the reported price or value for the relevant security(ies), commodity(ies) or underlying interest at the opening of regular trading hours (as determined by the Corporation) on the next trading day for which such an opening price or value is reported by the reporting authority; or (iii) a price or value for the relevant security(ies), commodity(ies) or underlying interest at such other time, or representing a combination or average of prices or values at such time or times, as the Corporation deems appropriate. The provisions of Article VI, Section 11(c) of the By-Laws with respect to the vote required to constitute the determination of an adjustment panel, the voting rights of members of adjustment panels, the ability of such panels to conduct their business by telephone or other designated means, and the ability of the Chairman of the Corporation and Exchange representatives to designate others to serve in their place on such panels shall apply equally to panels convened pursuant to this Section. Every determination pursuant to this Section shall be within the sole discretion of the Corporation or the panel making such determination, as the case may be, and shall be conclusive and binding on all investors and not subject to review.

(3) [no change]

(b) [no change]

...**Interpretations and Policies** [no change]

Time for Determination of Current Index Value

SECTION 5. (a) An Exchange may provide by rule that the current index value for the index underlying any class of index options traded on such Exchange, either generally or on particular trading days, shall be determined by reference to the reported level of such index at a time or times other than the close of trading. Similarly, the parties to a transaction in OTC index options may elect to base the current index value of the underlying index on a given day on the reported level of the underlying index at either the open or close of trading on such day. Any such Exchange rule or election by the parties to a transaction in OTC index options shall supersede any contrary provision in Section 1 C.(5) of this Article.

(b) [no change]

OTC Index Options

SECTION 6. (a) Variable Terms. The variable terms that are negotiated bilaterally between the parties to a transaction in OTC index options shall include (i) the type of option; (ii) the style of

option; (iii) the underlying index, selected only from among those underlying indices approved by the Corporation and which the By-laws and Rules specifically allow to be selected as an underlying index for an OTC index option; (iv) the expiration date; (v) the exercise price (stated in U.S. dollars and cents); (vi) the index multiplier; and (vii) the index value determinant; subject in each case to the limitations generally applicable to such variable terms as set forth in paragraph (b) below and any additional specific requirements applicable to OTC index options on a particular underlying index as set forth in the interpretations and policies following this Section 6 or as otherwise published by the Corporation on its website.

(b) *General Limitations on Variable Terms.* In respect of an OTC index option contract: (i) the type of option may be either a put or a call; (ii) the style of option may be either American-style or European-style; (iii) the underlying index may be any index identified by the Corporation as a permissible underlying index; (iv) the expiration date shall be a business day that is, at the maximum, no more than fifteen years from the trade date of the contract; (v) the exercise price shall be stated in U.S. dollars and cents; and (vi) the current index value at expiration may be determined based on either the opening index value or closing index value.

(c) *Acceptance of Confirmed Trades in OTC Index Options for Clearing.* If the confirmed trade information in respect of a transaction in OTC index options reported by an OTC Trade Source to the Corporation passes the Corporation's validation process, the Corporation shall accept such confirmed trade for clearing. The Corporation shall reject the transaction if the Corporation determines that: (i) any variable term of the contract does not comply with any applicable limitations established by the Corporation; (ii) the transaction would violate any applicable restrictions imposed on any of the Clearing Members for whose accounts the transaction is submitted to the Corporation for clearing (including, but not limited to, one or both of such Clearing Members are not approved to clear OTC index options); (iii) the information in the confirmed trade report submitted by the OTC Trade Source to the Corporation contains unresolved errors or omissions; or (iv) the information in the confirmed trade does not meet any other applicable criteria set forth in the By-Laws and Rules or procedures of the Corporation. Any transactions in OTC index options submitted to the Corporation for clearing that are rejected by the Corporation shall have no further effect as regards the Corporation and shall be deemed null and void and given no effect for purposes of the By-Laws and Rules.

(d) *The Role of the Corporation.* Commencing at the time at which the Corporation accepts a confirmed trade in OTC index options for clearing, the Corporation shall be substituted through novation as the seller to the Purchasing Clearing Member and the buyer to the Selling Clearing Member, and shall be the obligor to the extent set forth in the By-Laws and Rules with respect to obligations owing to persons having positions in such cleared contract. Each Clearing Member agrees with the Corporation that (i) it shall be bound, in accordance with the By-Laws and Rules, by all transactions in OTC index options submitted for its account through an OTC Trade Source and accepted by the Corporation for clearing; and (ii) it shall be bound by the terms of each transaction as reported by the OTC Trade Source to the Corporation and the Corporation shall not be responsible or liable to the Clearing Member for any error or omission in the variable terms or other information reported by the OTC Trade Source in connection with such transaction or for any acts or omission taken or made by the Corporation in reliance on such information.

(e) Fungibility. OTC index options of the same series shall be fungible. Positions in OTC index options created in a transaction between two counterparties may be closed out through a closing transaction between one of the parties to the original transaction and a different counterparty.

(f) Clearing Members' Representations and Warranties. Upon the submission of a confirmed trade in OTC index options to the Corporation for clearing, each Clearing Member for whose account the transaction is submitted shall be deemed to represent and warrant to the Corporation that: (i) the offer and sale of the OTC index options that are the subject of such transaction are exempt from the registration requirements of the Securities Act of 1933; (ii) such transaction has been effected by the Clearing Member in accordance with, the Clearing Member's participation in such transaction is in compliance with, and the Clearing Member will continue with respect to such transaction to comply with, all applicable laws and regulations including, without limitation, all applicable rules and regulations of the Securities and Exchange Commission, and the rules of the Financial Industry Regulatory Authority, Inc. and any other regulatory or self-regulatory organization to which the Clearing Member is subject; (iii) in respect of OTC index options on any S&P Index, the Clearing Member has read and understands the disclaimer language set forth below in item .03 of the Interpretations and Policies following this Section 6; (iv) in the case where the transaction is effected for the account of a customer, the customer is an "Eligible Contract Participant" as defined in Section 3a(65) of the Securities Exchange Act of 1934, as amended; (v) unless the Corporation notifies Clearing Members that the OTC Options will no longer be offered and sold pursuant to Rule 506 of Regulation D under the Securities Act of 1933, as amended, the Clearing Member has not offered or sold the OTC Options to any person that is not an "accredited investor," as defined in Rule 501(a) under Regulation D and has otherwise complied with applicable conditions to the exemption set forth in Rule 506; and (vi) unless the Corporation notifies Clearing Members that such restriction no longer applies, the Clearing Member has not offered or sold the OTC Options by any form of general solicitation or general advertising that, at the time of such activities, is or may be deemed to constitute general solicitation or general advertising, as described in Rule 502(c) of Regulation D. The Clearing Member shall indemnify and hold the Corporation harmless from any claim, liability or expense, including reasonable attorneys' fees, which may arise or be asserted as a result of any such representation and warranty being false or of any action brought against OCC alleging that any such representation and warranty is false, other than any claim, liability or expense that (a) results primarily from the gross negligence or willful misconduct of the Corporation or (b) results from conduct of the Corporation that causes the offer or sale of the OTC Options to become subject to the registration provisions of Section 5 of the Securities Act of 1933, as amended.

(g) Except as expressly provided in this paragraph or elsewhere in the By-Laws and Rules, and except to the extent inconsistent with the provisions of this Section 6, OTC index options shall be subject to all provisions of the By-Laws and Rules to the extent such provisions are applicable by their terms.

...Interpretations and Policies:

.01 Only the S&P 500 Index has been approved by the Corporation as an underlying index for OTC index options, as described in Section 6(a)(iii) of this Article XVII. In respect of an OTC index option contract on the S&P 500 Index: (i) the index multiplier shall be fixed at 1, (ii) the

expiration date must be within 5 years of the date on which a transaction in such OTC index option is accepted by the Corporation for clearance, and (iii) unless one or the other of the parties to the transaction is entering into the transaction as a closing purchase transaction or a closing sale transaction (provided, in either case, that such closing transaction does not constitute an opening purchase transaction or opening sale transaction for a non-proprietary account of one Clearing Member and a closing sale transaction or closing purchase transaction, respectively, for any proprietary account of the other Clearing Member), the expiration date must be at least 125 days, and no more than 15 years, from the origination date. In addition, unless one or more of the parties to the transaction is entering into the transaction as a closing purchase transaction or a closing sale transaction (provided, in either case, that such closing transaction does not constitute an opening purchase transaction or opening sale transaction for a non-proprietary account of one Clearing Member and a closing sale transaction or closing purchase transaction, respectively, for any proprietary account of the other Clearing Member), the minimum "notional value" of a transaction in OTC index options on the S&P 500 Index submitted to the Corporation for clearing shall be: (x) for options with an expiration date that is 275 or fewer days from its origination date, \$500,000 times the value of the S&P 500 Index at the opening of business in New York on the first business day of the calendar year in which the Corporation accepted the transaction for clearing; or (y) for options with an expiration date that is more than 275 but less than 1,101 days from its origination date, at least \$100,000 times the value of the S&P 500 Index at the opening of business in New York, New York on the first business day of the calendar year in which the Corporation accepted the transaction for clearing. The "notional value" of a transaction in an OTC index option on the S&P 500 Index shall equal the quantity of contracts multiplied by the closing value of the S&P 500 index on the business day prior to the date the transaction is accepted by the Corporation for clearing.

.02 For purposes of paragraph (c) of this Section 6, any transaction in OTC index options submitted to the Corporation for clearing that is rejected by the Corporation shall remain subject to any applicable agreement between the original parties to the transaction which, for the avoidance of doubt, may provide, among other things, that such rejected transaction shall remain a bilateral transaction between the parties subject to such agreement or other documentation as the parties have entered into for that purpose or may be terminated. The offer and sale of any such option or other security entered into bilaterally would not be covered by any exemption from the registration or other requirements of the Securities Act of 1933 that is specifically applicable, and limited, to OTC index options issued by the Corporation, and parties that may be deemed offerors or sellers of any such bilateral option contract or other security should satisfy themselves that the offer and sale would not be in violation of any applicable provision of the Securities Act of 1933.

.03 For purposes of clause (iii) of paragraph (f) of this Section 6, the S&P disclaimer reads as follows:

"S&P SHALL OBTAIN INFORMATION FOR INCLUSION IN OR FOR USE IN THE CALCULATION OF THE S&P INDEXES FROM SOURCES WHICH S&P CONSIDERS RELIABLE, BUT S&P DOES NOT GUARANTEE THE ACCURACY AND/OR THE COMPLETENESS OF THE S&P INDEXES OR ANY DATA INCLUDED THEREIN AND S&P SHALL HAVE NO LIABILITY FOR ANY ERRORS, OMISSIONS, OR INTERRUPTIONS THEREIN. S&P MAKES NO WARRANTY, EXPRESS OR IMPLIED, AS

TO RESULTS TO BE OBTAINED BY ANY PERSON OR ANY ENTITY FROM THE USE OF THE S&P INDEXES OR ANY DATA INCLUDED THEREIN IN CONNECTION WITH THE TRADING OF THE CONTRACTS, OR FOR ANY OTHER USE. S&P MAKES NO EXPRESS OR IMPLIED WARRANTIES, AND EXPRESSLY DISCLAIMS ALL WARRANTIES OR MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE WITH RESPECT TO THE S&P INDEXES OR ANY DATA INCLUDED THEREIN, WITHOUT LIMITING ANY OF THE FOREGOING, IN NO EVENT SHALL S&P HAVE ANY LIABILITY FOR ANY SPECIAL, PUNITIVE, INDIRECT, OR CONSEQUENTIAL DAMAGES (INCLUDING LOST PROFITS), EVEN IF NOTIFIED OF THE POSSIBILITY OF SUCH DAMAGES."

* * *

ARTICLE XX

CROSS RATE FOREIGN CURRENCY OPTIONS

* * *

Definitions

SECTION 1.

A. – B. [no change]

C.

(1) – (2) [no change]

Commencement Time

(3) The term “commencement time” in respect of a cross-rate foreign currency option means the time that is three hours following the settlement time of the confirmed trade [Exchange transaction] in which such cross-rate foreign currency option was purchased.

D. – O. [no change]

P.

Premium

(1) The term “premium” in respect of a confirmed trade [an Exchange transaction] in cross-rate foreign currency options means the price per unit of underlying currency of each such option multiplied by the unit of trading and by the number of contracts subject to the [Exchange] transaction. Premium may be expressed either in units (including fractions, decimals, or multiples of such units) of the trading currency designated by the Exchange on which such options are traded or as a percentage of the underlying currency. Premium shall be payable in the currency in which it is expressed.

(2) [no change]

Q. – R. [no change]

S.

Settlement Time

(1) The term “settlement time” in respect of a confirmed trade [an Exchange transaction] in cross-rate foreign currency options means 11:00 A.M. local time in the country of origin of the trading currency (*i.e.*, the premium currency), or such other time as the Corporation may specify, on the first foreign business day in that country immediately following the business day on which the Corporation receives [matching] confirmed trade information in respect of such transaction from the Exchange on which such transaction was effected.

T. – Z. [no change]

Extraordinary Events

SECTION 3. (a) [no change]

(b) If the Corporation shall in its discretion determine that extraordinary events would prevent the orderly settlement of confirmed trades [Exchange transactions] in, or exercises of, cross-rate foreign currency option contracts in the manner contemplated by the Rules, or impose undue burdens on the Corporation or on Cross-Rate Foreign Currency Clearing Members in connection therewith, then, in addition to any other actions that the Corporation may be entitled to take under the By-Laws and the Rules, the Corporation shall be empowered to make such adjustments in premium and exercise settlement procedures for affected option contracts (including, without limitation, the fixing of United States dollar cash settlement prices deliverable (i) in lieu of the trading currency in settlement of confirmed trades [Exchange transactions] or (ii) in lieu of either the trading currency or the underlying currency (or both) in settlement of exercises) as the Corporation in its sole discretion determines to be fair to the parties to such transactions or exercises.

[Section 3 of this Article replaces Section 19 of Article VI of the By-Laws.]

Payment of Premiums

SECTION 5. The acceptance of every confirmed trade [Exchange transaction] in cross-rate foreign currency options and the issuance of every such option (other than an option contract for which the commencement time is the close of trading on the business day immediately prior to the expiration date) by the Corporation shall be subject to the condition that the Corporation shall have received payment at or before the settlement time of all premiums denominated in the same trading currency due to the Corporation from the Purchasing Clearing Member in the account in which the [Exchange] transaction is effected. In the event the Corporation fails to receive such payment at or before the applicable settlement time, the Corporation may (either by a general rule or resolution adopted by the Board of Directors or by action of the officers of the Corporation with respect to specific transactions) reject any or all unaccepted opening and closing purchase transactions in such account relating to options denominated in the same

trading currency. In the event any transaction is rejected as herein provided, the Corporation shall promptly notify, either orally or in writing, the Purchasing Clearing Member and all Writing Clearing Members involved, and such Writing Clearing Members shall have the remedies, (if any), provided in the Exchange Rules of the Exchange on which such transaction was effected.

[Section 5 of this Article supplements Section 8 of Article VI of the By-Laws.]

* * *

ARTICLE XXII

CASH-SETTLED FOREIGN CURRENCY OPTIONS

* * *

Definitions

SECTION 1.

A. – B. [no change]

C.

Commencement Time

(5) The term “commencement time” in respect of a FX Index Option contract means the time that is three hours following the settlement time of the [Exchange transaction] confirmed trade in which such FX Index Option contract was purchased.

D. – O. [no change]

P.

Premium

(1) The term “premium” in respect of a confirmed trade [an Exchange transaction] in cash-settled foreign currency options other than rate-modified foreign currency options means the price (in the designated currency) of each such option, as agreed upon by the purchaser and seller in such transaction, multiplied by the number of units of underlying currency covered by the option and by the number of options subject to the transaction. The term “premium” in respect of a confirmed trade [an Exchange transaction] in rate-modified foreign currency options means the price (in the designated currency) of each such option, as agreed upon by the purchaser and seller in such transaction, multiplied by the multiplier and by the number of options subject to the transaction.

(2) [no change]

Q. – Z. [no change]

* * *

ARTICLE XXIII

FLEXIBLY STRUCTURED INDEX OPTIONS DENOMINATED IN A FOREIGN CURRENCY

* * *

Definitions

SECTION 1.

A. – B. [no change]

C.

Commencement Time

(5) The term “commencement time” in respect of [a] an FX Index Option contract means the time that is three hours following the settlement time of the confirmed trade [Exchange transaction] in which such FX Index Option contract was purchased.

D – O. [no change]

P.

Premium

(1) The term “premium” in respect of a confirmed trade [an Exchange transaction] in FX Index Options means the price of each such option in the designated currency (expressed in points), as agreed upon by the purchaser and seller in such transaction, times the index multiplier and the number of options subject to the transaction.

(2) [no change]

Q. – R. [no change]

S.

(1) [no change]

Settlement Time

(2) The term “settlement time” in respect of confirmed trade [an Exchange transaction] in FX Index Options means 11:00 A.M. local time in the country of origin of the trading currency, or such other time as the Corporation may specify, on the first foreign business day in that country immediately following the business day on which the Corporation receives [matching] confirmed trade information in respect of such transaction from the Exchange on which such transaction was effected.

Extraordinary Events

SECTION 3. (a) [no change]

(b) If the Corporation shall in its discretion determine that extraordinary events would prevent the orderly settlement of confirmed trades [Exchange transactions] in, or exercises of, FX Index Option contracts in the manner contemplated by the Rules, or impose undue burdens on the Corporation or on FX Index Option Clearing Members in connection therewith, then, in addition to any other actions that the Corporation may be entitled to take under the By-Laws and the Rules, the Corporation shall be empowered to make such adjustments in premium and exercise settlement procedures for affected option contracts (including, without limitation, the fixing of United States dollar amounts payable (i) in lieu of the trading currency in settlement of confirmed trades [Exchange transactions] or (ii) in lieu of the trading currency in settlement of exercises) as the Corporation in its sole discretion determines to be fair to the parties to such transactions or exercises.

Payment of Premiums

SECTION 7. (a) The acceptance of every confirmed trade [Exchange transaction] in FX Index Options and the issuance of every such option (other than an option contract for which the commencement time is the close of trading on the expiration date) by the Corporation shall be subject to the condition that the Corporation shall have received payment at or before the settlement time of all premiums denominated in the same trading currency due to the Corporation from the Purchasing Clearing Member in the account in which the [Exchange] transaction is effected. In the event the Corporation fails to receive such payment at or before the applicable settlement time, the Corporation may (either by a general rule or resolution adopted by the Board of Directors or by action of the officers of the Corporation with respect to specific transactions) reject any or all unaccepted opening and closing purchase transactions in such account relating to options denominated in the same trading currency. In the event any transaction is rejected as herein provided, the Corporation shall promptly notify, either orally or in writing, the Purchasing Clearing Member and all Writing Clearing Members involved, and such Writing Clearing Members shall have the remedies, (if any), provided in the Exchange Rules of the Exchange on which such transaction was effected.

[Section 7 of this Article supplements Section 8 of Article VI of the By-Laws.]

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ARTICLE XXVI

PACKAGED SPREAD OPTIONS

* * *

Definitions

SECTION 1.

A. – O. [no change]

P.

(1) – (5) [no change]

Premium

(6) The term “premium” in respect of a confirmed trade [an Exchange transaction] in packaged spread options means the price of each such option (expressed in points), as agreed upon by the purchaser and seller in such transaction, times the index multiplier and the number of options subject to the transaction.

Q. – Z. [no change]

RULES

* * *

CHAPTER I

DEFINITIONS

* * *

Definitions

RULE 101. Unless the context otherwise requires, for all purposes of these rules, the terms herein shall have the meanings given them in Article I of the By-Laws of the Corporation or as set forth below:

A. – B. [no change]

C.

Clearing Bank

(1) The term “Clearing Bank” means a bank or trust company which has entered into an agreement with the Corporation in respect of settlement of confirmed trades [Exchange transactions] on behalf of Clearing Members.

D. – L. [no change]

M.

[Matched Trade]

(1) Reserved [The term “matched trade” shall mean an Exchange transaction which has been reported to the Corporation as a matched trade in accordance with the Rules.]⁴

N.

Net Daily Premium

(1) The term “net daily premium” when applied to any account of a Clearing Member for any settlement time, means the net amount payable to or by the Corporation at such settlement time in respect of all confirmed trades [Exchange transactions] of the Clearing Member in such account as a Purchasing Clearing Member and a Writing Clearing Member.

O. – Z. [no change]

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CHAPTER II

MISCELLANEOUS REQUIREMENTS

* * *

Designation of Clearing Offices

RULE 204. Every Clearing Member shall designate the office of the Corporation through which it shall clear its Exchange transactions and otherwise conduct business with the Corporation, and each Clearing Member shall clear all of its confirmed trades [Exchange transactions] (no matter on which Exchange such transaction was effected) and otherwise conduct all of its business with the Corporation through the office of the Corporation it so designates. Notwithstanding the foregoing, the Corporation may from time to time permit one or more Clearing Members to utilize services of the Corporation through more than one office of the Corporation and Clearing Members may designate a different office as the one through which they will file exercise notices, receive assignments of exercise notices, deliver or receive certificates for underlying securities, or any one or more of the foregoing.

Records

RULE 207. Every Clearing Member shall keep records showing (a) with respect to each confirmed trade [Exchange transaction] in option contracts, the names of the Clearing Members who are parties to the transaction, the underlying security or future (or, in the case of index options or packaged spread options, the underlying index), the ticker symbol, the type of option, the premium, the trade date, the exercise price (or, in the case of packaged spread options, the

⁴ This definition is proposed to be deleted because it is now proposed to be replaced with the definition of “confirmed trade” in Article I of the By-Laws as set forth above.

base exercise price and spread interval), the expiration month, the name of the customer, whether the transaction was a purchase or writing transaction and whether it was an opening or closing transaction; (b) with respect to each confirmed trade [Exchange transaction] in BOUNDS, the series, the trade price, the trade date, the name of the customer, whether the transaction was a purchase or writing transaction and whether it was an opening or closing transaction; (c) with respect to each confirmed trade [Exchange transaction] in futures, the series, the trade price, the trade date, the name of the customer, whether the transaction was a purchase or sale transaction and whether it was an opening or closing transaction; and (d) with respect to each confirmed trade [Exchange transaction] in options contracts, futures or BOUNDS, such other information as may from time to time be required by law, regulation, the Exchange on which the transaction was effected or the Corporation. Such records, and all other records required by the By-Laws and Rules, shall be retained readily accessible for at least five years in such form as the Corporation may authorize and shall be deemed the joint property of the Corporation and the Clearing Member maintaining them. The Corporation shall be entitled to inspect or take temporary possession of any such records at any time upon demand.

* * *

CHAPTER IV

TRADE REPORTING AND [MATCHING] CONFIRMATION

* * *

Reporting of [Matched] Confirmed Trades Effected on Exchanges

RULE 401. (a) Each business day each Exchange shall report to the Corporation information with respect to each confirmed trade [Exchange transaction] made on such Exchange during said business day (or on a previous day and reconciled on said business day) and as to which [matching] confirmed trade information has been submitted by or on behalf of the Purchasing Clearing Member and the Writing or Selling Clearing Member. Such [matching] confirmed trade information shall also include a Customer CMTA Indicator, a CMTA Customer Identifier, and an IB Identifier to the extent required under applicable Exchange rules. If a give-up service provider reports to the Corporation the information required under this Rule 401 for confirmed trades [Exchange transactions] effected on an affiliated futures market, [matched] confirmed trade information from the give-up service provider shall be deemed to have been submitted to the Corporation by such affiliated futures market for all purposes of the By-Laws and Rules.

(1) - (3) [no change]

(b) Subject to Rule 403, each Clearing Member shall be responsible to the Corporation in respect of each confirmed trade [Exchange transaction] in which such Clearing Member is identified as a Purchasing Clearing Member or Writing or Selling Clearing Member in [matching] confirmed trade information reported to the Corporation by an Exchange, whether or not such [matching] confirmed trade information was correct.

(c) As used in this Rule in respect of a particular Exchange, the term “business day” shall ordinarily mean any day on which such Exchange is open for trading in cleared contracts. Notwithstanding the foregoing, when an international market is open for trading on a day when Exchanges in the United States are closed, the Corporation may agree with such international market that [matching] confirmed trade information regarding confirmed trades [Exchange transactions] effected on such international market on such day shall be reported to the Corporation on the following business day.

(d) The Corporation shall prescribe the times during which [matching] confirmed trade information is to be reported to the Corporation and the format of such reporting.

...Interpretations and Policies

.01 [no change]

.02 A Clearing Member may, through the systems of the Corporation, update certain non-critical trade information with respect to such transaction, provided that such updates are not in contravention of any rule of the Exchange on which a confirmed trade [Exchange transaction] was executed.

Supplementary Report of [Matched] Confirmed Trades

RULE 402. (a) In extraordinary circumstances, the Corporation may in its discretion accept from an Exchange after the Corporation’s cut-off time for receiving [matching] confirmed trade information for a particular business day (the “trade date”) in accordance with Rule 401, supplementary [matching] confirmed trade information reflecting the comparison of additional trades executed on or before the trade date that remained [unmatched] unconfirmed at the Corporation’s cut-off time. This Rule 402 shall have no application to reports of confirmed trades in OTC options submitted through an OTC Trade Source, which are subject to the provisions of Rule 404.

(b) - (f) [no change]

...Interpretations and Policies

.01 The procedure provided for in Rule 402 is intended for use only in extraordinary circumstances involving large numbers of [unmatched] unconfirmed trades. It is generally expected that this procedure will be employed only on a weekend or a holiday, when sufficient time exists to permit an Exchange to conduct additional trade[-matching] confirmation after the Corporation’s cut-off time on a particular trade date. However, continued improvements in trade processing and clearing systems may permit this procedure to be employed on weeknights as well.

Clearing Member Trade Assignment (“CMTA”)

RULE 403. (a) (1) Clearing Members that are parties to a CMTA arrangement shall register their arrangement with the Corporation and provide such information regarding the arrangement as the Corporation shall require. The registration of a CMTA arrangement shall be effective when the Clearing Members have supplied to the Corporation [matching] confirmed information

regarding the arrangement. Such registration shall: (i) constitute notice to the Corporation that the Executing Clearing Member has been authorized by the Carrying Clearing Member to direct the transfer of confirmed trades [Exchange transactions] to a designated account or accounts of the Carrying Clearing Member; (ii) constitute the continuing representation and warranty of each Clearing Member to the Corporation that they have entered into a CMTA Agreement which, if the Corporation has specified an approved form, is in substantially the form approved by the Corporation; and (iii) remain in effect until terminated as specified herein. A Clearing Member that is a party to a CMTA arrangement involving CMTA Customers shall also register with the Corporation each CMTA Customer Identifier and each IB Identifier that has been assigned for purposes of such CMTA arrangement, and shall promptly update such registrations to the extent a CMTA Customer Identifier or an IB Identifier is modified or deleted; provided that the identifiers have been approved by the other Clearing Member to the CMTA arrangement before the identifiers are submitted to the Corporation for registration. Registration of such identifiers, including any modifications or deletions thereto, shall be effective when the Corporation's systems have accepted such registration or updated identifier information. The Corporation may reject the registration a particular CMTA Customer Identifier or IB Identifier in the event an assigned identifier is already registered with the Corporation.

(2) In addition to the foregoing registrations, Clearing Members that are parties to a CMTA arrangement may elect to authorize the Corporation to settle fees and commissions owed by the Carrying Clearing Member to the Executing Clearing Member in respect of transfers effected pursuant to that arrangement. Clearing Members making such election shall specifically register that aspect of their CMTA arrangement with the Corporation. Such registration shall authorize (i) the Executing Clearing Member to enter into the Corporation's systems fee and commission information with respect to transfers effected pursuant to the CMTA arrangement between the Clearing Members, subject to such system checks as may be established by the Corporation from time to time, and (ii) the Corporation to calculate and settle, in accordance with the applicable provisions of Rule 504, the aggregate of such entered amounts on the next following business day without any further authorization or consent of the Carrying Clearing Member. Registration of this aspect of the Clearing Members' CMTA arrangement shall be effective when the Corporation's systems have accepted such registration. Any entries made pursuant to such registration shall be solely for fees and commissions related to transfers effected pursuant to the Clearing Members' CMTA arrangement and for no other purposes.

(b) Before transferring a confirmed trade [an Exchange transaction] to a Carrying Clearing Member as specified in the [matching] confirmed trade information reported to the Corporation, the Corporation shall first determine whether a CMTA registration is in effect between the Executing Clearing Member and the Carrying Clearing Member. If such a registration is in effect, the Corporation shall transfer the confirmed trade [Exchange transaction] to the designated account of the Carrying Clearing Member unless such [matching] confirmed trade information additionally includes a Customer CMTA Indicator. In that event, the Corporation shall further determine whether such [matching] confirmed trade information also includes a CMTA Customer Identifier and IB Identifier. If the [matching] confirmed trade information includes a CMTA Customer Identifier and an IB Identifier and each such identifier matches a CMTA Customer Identifier and an IB Identifier registered for purposes of the CMTA arrangement between the Carrying Clearing Member and the Executing Clearing Member, the

Corporation shall transfer the confirmed trade [Exchange transaction] to the Carrying Clearing Member. If, however, (i) a CMTA registration is not in effect, (ii) the Corporation, in its sole discretion, determines that the information submitted in connection with the CMTA transaction contains an error or omission as provided in paragraph (c) of Interpretation .01 to Article VI, Section 1 of the By-Laws, or (iii) the [matching] confirmed trade information reported in respect of a confirmed trade [an Exchange transaction] includes a Customer CMTA Indicator, but incorrect, incomplete, or missing information as to either identifier, the transaction shall be deemed to be a failed CMTA transaction and shall not be transferred to an account of the Carrying Clearing Member. A failed CMTA transaction will instead be transferred to a designated account of the Executing Clearing Member, which shall be responsible for the clearance and settlement of such transaction. In the absence of such designation, the Corporation shall transfer the failed CMTA transaction to the customers' or segregated futures account, as applicable, of the Executing Clearing Member.

(c) The Carrying Clearing Member shall be responsible for the clearance and settlement of each confirmed trade [Exchange transaction] that has been transferred to one of its accounts pursuant to an effective CMTA registration, subject to such Carrying Clearing Member's right to effect a Return as specified herein.

(d) A Carrying Clearing Member may Return to the Executing Clearing Member a position resulting from the transfer of a confirmed trade [an Exchange transaction], as follows:

(1) – (4) [no change]

(e) The Carrying Clearing Member shall be responsible for the clearance and settlement of any position resulting from a confirmed trade [an Exchange transaction] transferred to it in accordance herewith that (i) has been exercised or assigned, (ii) has matured or (iii) will expire or mature before the Corporation's next business day, notwithstanding the fact that the Carrying Clearing Member has the right to Return such position. To the extent that a Carrying Clearing Member has the right to Return such position, the Carrying Clearing Member shall not effect a Return pursuant to this Rule. Rather, the respective rights, obligations and claims of the Carrying Clearing Member and the Executing Clearing Member with respect to such position shall be governed by the CMTA Agreement between the Clearing Members. A Carrying Clearing Member shall also be responsible for any position for which it did not effect a Return notwithstanding that it had the right to do so.

(f) – (j) [no change]

(k) The Carrying Clearing Member shall be responsible for the clearance and settlement of all confirmed trades [Exchange transactions] properly submitted for transfer prior to the effective termination of the CMTA registration, subject to any right that it may have to Return such transaction. After the termination of a CMTA registration, all transactions submitted for transfer pursuant to such registration shall be deemed to be failed CMTA transactions and shall be transferred as specified in paragraph (b) hereof.

(l) Until such time as the Corporation shall provide otherwise, CMTA transactions in OTC options shall not be permitted. Transfers of OTC options between accounts of the same Clearing Member or between accounts of different Clearing Members is a manual process and may be

effected only with the consent of the Corporation and for such purposes and subject to such procedures as the Corporation may provide.

...Interpretation and Policies: [no change]

Reporting of [Matched] Confirmed Trades in OTC Options

RULE 404. (a) Reports of confirmed trades in OTC options shall be submitted to the Corporation for clearance through the applicable OTC Trade Source in accordance with the By-Laws and Rules and the applicable OTC Trade Source Rules. Confirmed trade reports shall contain confirmed trade information which shall include: (i) the identities of the Purchasing Clearing Member and the Selling or Writing Clearing Member and the accounts of each for which the trade is being effected; (ii) the variable terms of the OTC option as provided in Section 6 of Article XVII of the By-Laws; (iii) the number of contracts; (iv) the premium per unit; (v) in the case of transactions in the securities customers' account, a unique customer ID for the customer for whom the trade was executed; and (vi) such other information as the Corporation may require.

(b) Subject to Rule 403, each Clearing Member shall be responsible to the Corporation in respect of each confirmed trade in which such Clearing Member is identified as a Purchasing Clearing Member or Writing or Selling Clearing Member in confirmed trade information reported to the Corporation by an OTC Trade Source, whether or not such confirmed trade information was correct.

(c) The cut-off time on each business day for an OTC Trade Source to submit confirmed trades in OTC options to the Corporation for premium settlement on the next business day shall be 4:00 p.m. Central Time or such other time as the Corporation may establish with prior notice to Clearing Members. Premium settlement for confirmed trades in OTC options submitted after 4:00 p.m. on any business day or on a day other than a business day shall be effected on the second following business day. The Corporation shall prescribe the format of reporting of Confirmed Trades in OTC options.

Allocations of Positions

RULE 405. (a) One or more positions in cleared contracts may be allocated from a designated account of a Giving-Up Clearing Member to a designated account of a Given-Up Clearing Member without the intermediation of a give up service provider through the processes provided for in this Rule; provided, however, that this Rule 405 shall have no application to positions in OTC options.

(b) If (i) the [matching] confirmed trade information submitted to the Corporation in respect of a confirmed trade [an Exchange transaction] instructs that the position resulting therefrom is to be allocated from a designated account of the Giving-Up Clearing Member to a designated account of the Given-Up Clearing Member, or the Giving-Up Clearing Member has submitted an instruction to the Corporation that one or more positions are to be allocated from a designated account of the Giving-Up Clearing Member to a designated account of the Given-Up Clearing

Member, and (ii) the Giving-Up Clearing Member and the Given-Up Clearing Member are parties to an allocation agreement registered with the Corporation at the time the Corporation processes the instruction, then the Corporation shall adjust the positions in the respective designated accounts of the Giving-Up and Given-Up Clearing Member in accordance with the allocation instruction. If the Giving-Up Clearing Member and the Given-Up Clearing Member are not parties to an allocation agreement registered with the Corporation, then the Corporation shall adjust the positions in the respective designated accounts of the Giving-Up and Given-Up Clearing Member in accordance with the allocation instruction only upon receipt of notice from the Given-Up Clearing Member of its affirmative acceptance of the allocation.

(c) – (e) [no change]

(f) If an allocation instruction is submitted after the date the confirmed trade [Exchange transaction](s) resulting in the position(s) to be allocated is reported to the Corporation, the allocation will not be given effect in any Daily Position Reports and no premium, variation or margin adjustments will be made in respect of the allocated position(s) until the business day after the date on which the allocation instruction is executed by the Corporation.

Notwithstanding the foregoing, the Corporation shall be entitled to require intra-day margin settlements and/or other intra-day settlements in respect of any allocated position as otherwise specified in the By-Laws and Rules.

(g) – (j) [no change]

...Interpretations and Policies: [no change]

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CHAPTER V

DAILY CASH SETTLEMENT

* * *

Daily Position report

RULE 501. Prior to 9:00 A.M. Central Time (10:00 A.M. Eastern Time) of each business day, the Corporation shall make available to each Clearing Member a Daily Position Report for each account maintained by the Clearing Member with the Corporation. The Daily Position Report shall list, among other things, all confirmed trades [Exchange transactions] of the Clearing Member in such account settling on such business day and shall show the net daily premiums due to or from the Corporation in such account as a result of such [Exchange] transactions. Net daily premiums shall be further combined and netted with net variation payments due to or from the Corporation in respect of positions and transactions in futures in such accounts as calculated by the Corporation in accordance with Chapter XIII of the Rules

...Interpretations and Policies [no change]

Daily Premium and Futures Variation Settlement

RULE 502. (a) At or before settlement time on each business day, each Clearing Member shall be obligated to pay the Corporation the amount of any net daily premium and variation payments in an account shown to be due to the Corporation on the Daily Position Report for such account for such day (notwithstanding any credit balance which may be due from the Corporation to the Clearing Member in any other account). Subject to the provisions of Rule 607, the Corporation shall be authorized to withdraw from the Clearing Member's bank account established in respect of such account an amount equal to such net amount. Notwithstanding the foregoing, at any settlement time the Corporation may, in its discretion, require any Clearing Member to pay the gross amount of premiums due to the Corporation in respect of all of such Member's confirmed trades [Exchange transactions] in an account reaching settlement on such business day (i.e., without credit for premiums payable to the Member), and the Corporation shall be authorized to withdraw funds from the applicable bank account of such Clearing Member in such amount.

(b) – (c) [no change]

* * *

CHAPTER VI

MARGINS

* * *

Margin Requirements

RULE 601. (a) *Deposit of Margin Assets.* Prior to the time specified by the Corporation on every business day, every Clearing Member shall be obligated to deposit with the Corporation, in accordance with the following provisions of this Rule, margin assets with respect to (1) the positions in cleared contracts maintained in each account with the Corporation at the opening of such business day (including positions resulting from confirmed trades [Exchange transactions] having a settlement time on such business day); (2) the margin-eligible stock loan positions and stock borrow positions maintained in each account with the Corporation at the opening of such business day (including such positions that were established as a result of Stock Loans initiated on the preceding business day); and (3) any settlement obligations in an account arising from the exercise, assignment, or maturity of any of the foregoing. The minimum amount of margin assets that a Clearing Member is required to deposit with the Corporation shall be such that the aggregate margin assets deposited in respect of the Clearing Member's account, including the margin assets deposited on such business day, is equal to the margin requirement for such account calculated pursuant to the applicable provisions of this Rule 601.

(b) – (e) [no change]

...**Interpretations and Policies** [no change]

Segregation of Long Positions

RULE 611. (a) Subject to the provisions of Article VI, Section 4 of the By-Laws, and except as provided in paragraph (d) hereof in the case of long positions in OTC options, all long positions (other than long positions in futures) in securities customers' accounts and firm non-lien accounts shall be deemed to be segregated long positions unless the Corporation receives contrary instructions from a Clearing Member in accordance with the following provisions of this Rule 611. All segregated long positions shall be held by the Corporation free of any charge, lien or claim of any kind in favor of the Corporation or any person claiming through it, until such positions shall be closed or exercised in accordance with the By-Laws and Rules or until the Clearing Member shall file with the Corporation written instructions, in such form as the Corporation may from time to time prescribe, directing that such positions be released from segregation. All positions in futures shall be deemed to be unsegregated for purposes of this Rule 611. All positions in cleared securities that are carried in a customers' lien account shall be deemed to be unsegregated for purposes of this Rule 611.

(b) Each business day, during such hours as the Corporation may from time to time establish, a Clearing Member may file with the Corporation written instructions, in such form as the Corporation may from time to time prescribe, designating any segregated long position in such Clearing Member's customers' account or firm non-lien account which the Clearing Member desires the Corporation to release from segregation. The Clearing Member's Daily Position Report and Daily Margin Report for the following business day, and each business day thereafter while such instructions remain in effect, shall reflect such instructions. The Corporation shall have a lien on each unsegregated long option carried in a customers' account (including any exercised option contracts) as provided in the applicable provisions of Article VI, Section 3 of the By-Laws. The Corporation's lien on any long position which the Corporation has been directed to release from segregation as provided herein shall continue until (i) the Corporation receives written instructions, in such form as the Corporation may from time to time prescribe, directing that such long position be segregated and held free of lien, and (ii) the Clearing Member duly pays to the Corporation in accordance with these Rules, all amounts payable by such Clearing Member on the business day following the Corporation's receipt of such instructions. Notwithstanding the foregoing, Clearing Members shall not be permitted to file instructions to release any long position in an OTC options from segregation, and all such long positions shall be segregated except as provided in paragraph (d) of this Rule 611.

(c) [no change]

(d) In the case of a long position in OTC options carried in the securities customers' account of a Clearing Member and for which the Corporation has received a customer ID, to the extent permitted under all applicable laws and regulations (including the rules of the Financial Industry Regulatory Authority, Inc. and any other regulatory or self-regulatory organization to which the Clearing Member is subject), the Corporation shall automatically unsegregate such long position to the extent that the Corporation identifies a qualifying spread position where the short leg of the spread is carried under the same customer ID. The Clearing Member shall not carry a qualifying spread position for a customer unless the customer's margin requirement has been reduced in recognition of the spread, and the carrying of a qualifying spread position for the

account of a customer shall constitute a representation to the Corporation that the customer's margin has been so reduced.

...*Interpretations & Policies*: [no change]

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CHAPTER VIII

EXERCISE AND ASSIGNMENT

* * *

Exercise of Options

RULE 801. Issued and unexpired option contracts may, subject to Exchange Rules and the By-Laws, be exercised as follows:

(a) [no change]

(b) Any expiring American option contract may be exercised on its expiration date in accordance with Rule 805. Any capped or European option contract may be exercised (other than automatically exercised in the case of a capped option) only on its expiration date in accordance with Rule 805. Any binary options that meet the exercise parameters set forth in Rule 1501 will be automatically exercised in accordance with that rule. Notwithstanding the foregoing, any expiring flexibly structured index option contract, quarterly index option contract, monthly index option contract, weekly index option contract, [or] short term index option contract or OTC index option contract that meets the exercise parameters set forth in Rule 1804(c) will be automatically exercised on its expiration date in accordance with that rule. No expiring option contract other than an American style flexibly structured option contract, a foreign currency option contract, a short term option contract, a quarterly option contract, a monthly option contract, a weekly option contract, a cross-rate foreign currency option contract, an OTC index option contract or a futures option contract may be exercised on the business day immediately preceding its expiration date.

(c) – (d) [no change]

...*Interpretations and Policies* [no change]

Assignment of Exercise Notices to Clearing Members

RULE 803. Exercise notices accepted by the Corporation shall be assigned in accordance with the Corporation's procedures to Clearing Members with open short positions in the series of options involved, provided that:

(a) the Corporation may assign an exercise notice to a Clearing Member in respect of an opening writing transaction made by such Clearing Member on the day on which the exercise notice was accepted by the Corporation; and

(b) the Corporation shall not assign an exercise notice to a Clearing Member in respect of any open short position after the Corporation has received [matching] confirmed trade information for a closing purchase transaction which, upon acceptance by the Corporation, will eliminate such short position, unless and until such closing purchase transaction is rejected by the Corporation.

Subject to the provisions of the By-Laws, exercise notices accepted by the Corporation shall be assigned at or before 8:00 A.M. Central Time (9:00 A.M. Eastern Time) on the following business day. Assignments shall be dated and effective as of the date the applicable exercise notices were accepted by the Corporation. A Clearing Member to which an exercise notice is assigned shall be notified thereof as soon as practicable after such notice is assigned by the Corporation, and, if applicable, a [the] Clearing Member submitting an [such] exercise notice shall (subject to the provisions of Rule 901) be notified of the identity of the Assigned Clearing Member [,] through the transmission of Delivery Advices or as soon as practicable after such notice is assigned by the Corporation.

...Interpretations and Policies:

.01 Under the Corporation's assignment procedures the Corporation will assign exercise notices to Clearing Members in respect of positions in a particular account of such Clearing Member or, in the case of an account divided into sub-accounts, a particular sub-account. In the case of short positions in OTC options in a Clearing Member's securities customers' account for which the Corporation has a customer ID, the Corporation will assign exercise notices to specific customer IDs.

Allocation of Exercises

RULE 804. Except as provided in the last sentence of this Rule 804, [E]each Clearing Member shall establish fixed procedures for the allocation of exercises assigned in respect of short positions in the Clearing Member's accounts to specific option contracts included in such short positions. The allocation shall be made in accordance with the requirements set forth in Exchange Rules and any applicable rules of any self-regulatory organization of which the Clearing Member is a member. During the term of any restriction imposed on a Clearing Member pursuant to Rule 305, the Chairman, the Management Vice Chairman, or the President may require the Clearing Member to report to the Corporation, not later than 8:00 A.M. Central Time (9:00 A.M. Eastern Time) on each business day, the name and address of each writer to whom the Clearing Member allocated an exercise assigned to the Clearing Member on the preceding business day. Such reports shall indicate, for each writer, the series of options for which an exercise was allocated and the number of contracts included in the allocation, and shall state whether any specific deposit or escrow deposit has been made in respect of such writer's short position in such series of options. The foregoing provisions of this Rule 804 shall not apply to the allocation of exercises of OTC options; and in the case of short positions in OTC options in respect of which the Corporation has assigned exercises to a particular customer ID, the Clearing Member shall allocate the exercise only to the customer associated with such customer ID.

...Interpretations and Policies: [no change]

Expiration Date Exercise Procedure

RULE 805. (a) At or before such time as the Corporation shall from time to time specify on each expiration date, the Corporation shall make available to each Clearing Member an Expiration Exercise Report.

(b) Upon retrieving [receiving] an Expiration Exercise Report, each Clearing Member may submit exercise instructions in response to such report through electronic means prescribed by the Corporation for that purpose. Such instructions shall indicate, with respect to each series of options listed for each of the Clearing Member's accounts, the number of option contracts of that series, if any, to be exercised for that account. If no option contracts of a particular series are to be exercised for a particular account, the Clearing Member may so indicate opposite the title of that series. Each Clearing Member desiring to submit instructions in accordance with the preceding provisions of this subparagraph (b) shall submit such instructions to the Corporation before such time as the Corporation shall from time to time specify on the expiration date. Instructions to exercise given pursuant to this subparagraph (b) shall become irrevocable at such time on the expiration date as the Corporation shall from time to time specify.

(c) If, after the deadline prescribed pursuant to subparagraph (b) for the submission of exercise instructions in response to Expiration Exercise Reports, but prior to the expiration time for such option contracts on the expiration date, a Clearing Member desires to exercise option contracts expiring on such expiration date in addition to those which the Clearing Member has previously instructed the Corporation to exercise, the Clearing Member may do so by tendering to the Corporation, prior to such expiration time, a written exercise notice on such form as the Corporation shall prescribe, provided that (i) the Corporation may designate in its procedures classes of futures options with respect to which no late exercise notices will be accepted; and (ii) the Corporation will not accept any late exercise notices with respect to OTC options.

(d) – (m) [no change]

...Interpretations and Policies [no change]

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CHAPTER X

CLEARING FUND CONTRIBUTIONS

* * *

Amount of Contributions

RULE 1001.

(a) [no change]

(b) The contribution to the Clearing Fund of each Clearing Member (except recently admitted Clearing Members whose contributions are fixed pursuant to Article VIII of the By-Laws) for each calendar month shall be the greater of (x) the minimum clearing fund contribution specified in paragraph (c) of this Rule or (y) such Clearing Member's proportionate share of the total amount of the Clearing Fund as determined pursuant to paragraph (a) of this Rule. A Clearing Member's proportionate share shall be a fraction, the numerator of which shall be the daily average number of options and futures contracts (with the number of OTC option contracts adjusted as needed to ensure that the number of such OTC option contracts, as adjusted, is approximately equal to the number of option contracts other than OTC option contracts that would cover the same notional value or units of the same underlying interest), BOUNDS and shares of Eligible Stock underlying stock loan and borrow positions (adjusted by dividing such number of shares by 100), held by such Clearing Member in open positions with the Corporation during the preceding calendar month and the denominator of which shall be the daily average number of options and futures contracts, BOUNDS and shares of Eligible Stock underlying stock loan and borrow positions, in each case (adjusted in the same manner as the numerator), held by all Clearing Members in open positions with the Corporation during such preceding calendar month. The numerator and denominator shall each include the average daily number of contracts held in paired X-M accounts. Notwithstanding clause (x) of this paragraph (b), an entity that is an affiliate of a Clearing Member and that also becomes a Clearing Member solely for the purpose of clearing transactions in security futures, commodity futures, futures options, and/or commodity options shall be deemed to be in compliance with the \$150,000 minimum contribution if its contribution is equal to the amount specified in clause (y) of this paragraph and the earlier-admitted Clearing Member is in compliance with the minimum requirement under clause (x).

(c) – (e) [no change]

...Interpretations and Policies: [no change]

* * *

CHAPTER XI**SUSPENSION OF A CLEARING MEMBER**

* * *

Creation of Liquidating Settlement Account⁵

⁵ The text of Rule 1104 as presented in this rule change reflects material that is proposed to be added, but is not yet approved by the Commission. See SR-OCC-2012-11. If that pending rule change is not approved before this proposed rule change, proposed Interpretation and Policy .03 would be renumbered as .02.

RULE 1104. (a) – (f) [no change]

...Interpretations and Policies

.01 [no change]

.02 (a) For purposes of this Rule 1104 and Rules 1106, 1107, 2210 and 2210A, in order to minimize the execution and liquidity risks associated with (i) liquidating a suspended Clearing Member's margins deposited with the Corporation and Clearing Fund contributions (collectively referred to in this Interpretation and Policy as "Collateral"), (ii) closing out such Clearing Member's open positions in cleared contracts and stock loans (collectively referred to in this Interpretation and Policy as "Open Positions") and (iii) closing out exercised or matured cleared contracts to which such Clearing Member was a party either as the exercising Clearing Member or as the assigned Clearing Member (collectively referred to in this Interpretation and Policy as "Exercised/Matured Contracts"), the Corporation may elect to use one or more private auctions to liquidate all or any part of such Collateral, Open Positions and/or Exercised/Matured Contracts, as determined by the Board of Directors, the Chairman, the Management Vice-Chairman, or the President of the Corporation. As used in this interpretation, the term "private auction" means an auction open to bidders invited by the Corporation pursuant to this interpretation and with respect to which bidders submit confidential bids. If such determination is made by the Chairman, the Management Vice-Chairman or the President of the Corporation, the Board of Directors shall be notified as soon as practicable of the determination. The option to elect a private auction process is discretionary; the Corporation may use other procedures as provided for or permitted in the By-Laws and Rules to liquidate a suspended Clearing Member's Collateral, Open Positions and/or Exercised/Matured Contracts if the Corporation decides that circumstances warrant. The Corporation shall provide prompt notice to the Membership/Risk Committee (or other committee of the Board of Directors to which the auction oversight function is delegated) whenever a private auction is expected to be conducted.

(b) The Corporation shall conduct each auction within the general framework as approved by the Membership/Risk Committee and described in this Interpretation and Policy. Each auction will be structured to provide an orderly and robust procedure for liquidating Collateral, Open Positions and/or Exercised/Matured Contracts consistent with the By-Laws and Rules of the Corporation. The Corporation shall consult with the Membership/Risk Committee (or other committee of the Board of Directors to which such function is delegated) regarding the structuring and administration of each individual auction, and may work with such advisors as the Corporation deems necessary and appropriate to assist the Corporation in respect of such matters.

(c) The Corporation will invite all Clearing Members to apply to become pre-qualified auction bidders. Any Clearing Member may be included in the pool of pre-qualified auction bidders by completing required auction documentation in advance. By posting notices on the Corporation's website from time to time, the Corporation will also invite non-Clearing Members to apply to become pre-qualified auction bidders. In order for a non-Clearing Member to be pre-qualified as an auction bidder, the non-Clearing Member must (i) actively trade in the asset class in which it proposes to submit bids, (ii) actively trade in markets cleared by the Corporation, (iii) be sponsored by, and submit its bids through, a Clearing Member that has agreed to guarantee and

settle any accepted bid made by such non-Clearing Member and (iv) complete required auction documentation in advance. The Corporation will endeavor to maintain a pool of pre-qualified auction bidders by periodically reviewing such bidders and their qualifications. The Corporation will promptly notify any pre-qualified auction bidder removed from the pool of pre-qualified auction bidders.

(d) With respect to each particular auction, the Corporation shall review pre-qualified auction bidders that seek to participate in the auction on an objective basis and take into consideration criteria including a bidder's (and/or, in the case of a non Clearing-Member bidder, its sponsor Clearing Member's) financial strength, demonstrated activity in the products being auctioned and qualification to clear transactions in the asset class in which it proposes to submit bids before inviting a bidder to participate in the auction. Such review is intended to ensure that each selected bidder, should it be a winner in the auction, would be financially able to make payment for and assume the obligations of the Collateral and other positions it acquires and be able to manage the risk thereof and/or trade out of such positions without creating unnecessary further risk to the Corporation. The Corporation shall endeavor to maximize the effectiveness of the auction process by, among other things, exercising its discretion on a case-by-case basis to fix the number of bidders to be selected for each auction at a level large enough to create robust, efficient auctions that will generate competitive bids but not so large as to create unnecessary delay and jeopardize the confidentiality of positions in the suspended Clearing Member's portfolio and thereby discourage potential bidders from participating competitively in the auction. The Corporation will promptly notify all pre-qualified auction bidders selected to become bidders for a particular auction by electronic or telephonic communication. Each selected bidder may, but will not be required to, submit a bid in the auction.

(e) The Corporation shall have discretion to auction the suspended Clearing Member's Collateral, Open Positions and/or Exercised/Matured Contracts as a single portfolio or as multiple discrete portfolios based on, for example, product type or asset class. The Corporation shall also have discretion to require bidders to post collateral or other deposits in advance of the auction and the submission of bids shall be in accordance with the procedures and timeframes established by the Corporation from time to time. The Corporation and the bidders shall exchange auction information in a secure and confidential manner as specified by the Corporation. At the conclusion of the auction, the Corporation shall, in its discretion, determine the prevailing bid(s) and whether to accept or reject such bid(s); provided, however, that, in the event that accepting the prevailing bid(s) would result in a loss chargeable against the Clearing Fund, any decision by the Corporation to accept such bid(s) shall require review and approval by the Membership/Risk Committee (or other committee of the Board of Directors to which such function is delegated) or the Board of Directors. The Corporation shall provide prompt notice to the winning bidder that its bid has been selected and shall thereafter provide notice to the losing bidders that their bids have not been selected, in each case by electronic or telephonic communication. If the auction is successful, the Corporation shall facilitate the transfer of the suspended Clearing Member's Collateral, Open Positions and/or Exercised/Matured Contracts to the winning bidder(s) with the intention of completing settlement processing of the auctioned portfolio(s) no later than the first business day after the bids are accepted by the Corporation.

(f) The Corporation shall have discretion to select the best bid submitted for any portfolio in an auction, based on the totality of the circumstances, and no bid shall be binding on the Corporation unless accepted by it. Unless the Corporation determines otherwise with respect to any particular auction, the Corporation retains the right, in its discretion, to reject any or all bids submitted for any or all portfolios in an auction. Such bids may be rejected if, for example, the bids are unreasonably far from the market values of the Collateral, Open Positions and/or Exercised/Matured Contracts being auctioned as determined by the Corporation based upon current market data and theoretical pricing models or if the Corporation determines that the rules of the auction have been breached or other circumstances cause the Corporation to conclude that the bids have been tainted by unfairness or illegality. Notwithstanding the foregoing, the Corporation shall have no authority to reject any bid or bids once settlement has been effected through payment and delivery of the auctioned property and assumption of auctioned obligations. To the extent that the Corporation rejects all bids submitted for some or all of the portfolios in an auction, the Corporation shall take such steps to liquidate the Collateral, Open Positions and/or Exercised/Matured Contracts that were the subject of the rejected bids in the most orderly manner practicable, which may include the holding of another private auction.

(g) Clearing Members agree that the private auction process described above is a commercially reasonable method of liquidating a suspended Clearing Member's Collateral and closing out such Clearing Member's open positions, including for purposes of Section 9-610 of the Uniform Commercial Code to the extent such Section is applicable to the private auction process. Clearing Members recognize that their positions may lose value quickly and that a prompt and efficient auction may be the best method for an orderly liquidation and preservation of value. Clearing Members agree that notice of a private auction to a suspended Clearing Member is not required under the auction process or under Section 9-611 of the Uniform Commercial Code, but if notice is given, Clearing Members agree that it is commercially reasonable under Section 9-611 of the Uniform Commercial Code for the notice to be given at or prior to the time that bidders are provided information regarding the auction.

.03 See Rule 1106(e)(2) for a description of the alternative private auction process by which OCC may close out a suspended Clearing Member's open positions in OTC options and related positions and margin assets in certain circumstances.

Pending Transactions and Variation Payments

RULE 1105. Notwithstanding any other provision of the By-Laws and Rules, the Corporation shall have no obligation to accept any [matched]confirmed trade [Exchange transaction] of a suspended Clearing Member that was effected after the time at which the Clearing Member was suspended. In the event a confirmed trade [Exchange transaction] of a suspended Clearing Member is rejected by the Corporation, such transaction shall be closed by the other party thereto in accordance with the Exchange Rules of the Exchange on which the transaction was effected, or, in the case of a confirmed trade in OTC options, as provided in any agreement between the parties. Confirmed trades [Exchange transactions] of a suspended Clearing Member that are accepted by the Corporation shall be treated in the following manner:

(a) – (g) [no change]

... *Interpretations and Policies*: [no change]

Open Positions

RULE 1106 (a) – (e) [no change]

(e) Exceptions [Exception].

(1) Notwithstanding the preceding provisions of this Rule, if the Chairman, the Management Vice Chairman, or the President shall determine in his discretion, taking into account the size and nature of a suspended Clearing Member's positions, the market conditions prevailing at the time, the potential market effects of liquidating transactions that might be directed by the Corporation, and such other circumstances as such officer deems relevant, that the closing out of some or all of the suspended Clearing Member's unsegregated long positions or short positions in options or BOUNDS, or long or short positions in futures, would not be in the best interests of the Corporation, other Clearing Members, or the general public, such positions need not be closed out, provided that any determination made pursuant to this paragraph shall be reported to the Board of Directors within 24 hours. This paragraph shall not apply to positions of any suspended Clearing Member as to which an application for a protective decree may be filed under Section 5(a)(3) of the Securities Investor Protection Act of 1970, as amended, except upon a determination by the Chairman, the Management Vice Chairman, or the President in his discretion, taking into account the circumstances enumerated in the preceding sentence, that the closing out of the suspended Clearing Member's open positions in accordance with the other provisions of this Rule would likely result in a loss to the Corporation (after application of such Clearing Member's margin and Clearing Fund deposits but before any proportionate charge to the Clearing Fund deposits of other Clearing Members).

(2) The Corporation may conduct a private auction in accordance with the procedures summarized below (an "OTC Options Auction") to close out open positions in OTC index options and related positions in other cleared contracts and margin assets (including any securities underlying a stock loan or borrow position in which the Corporation has a security interest but not the stock loan or borrow positions themselves) that the Corporation determines in its discretion are hedging, or are hedged by, positions in OTC index options as determined in the discretion of the Corporation ("hedge positions"). The Corporation intends that these OTC Options Auction procedures will be invoked only in unusual circumstances where the Corporation determines in its discretion that it is not feasible in light of the circumstances existing at the time to close out such positions through any of the other means provided under this Chapter XI of the Rules. The summary of the OTC Options Auction procedures set forth in this Rule 1106(e)(2) is subject to the specific procedures set forth in a document entitled "OTC Options Auction Procedures," which is incorporated herein by reference and which is available from the Corporation upon request and posted on the Corporation's website.

(A) All non-suspended OTC Index Option Clearing Members ("Participants") are required to participate in the OTC Options Auction by submitting competitive bids for all or a portion of the suspended Clearing Member's portfolio of OTC Index Options and hedge positions. Each Participant shall be subject to a minimum participation level based on the proportion such Participant's risk margin requirement (calculated as the sum of the average daily

margin requirement, consisting of the amount of margin held by the Corporation with respect to an OTC Index Option Clearing Member's accounts eligible to hold OTC positions ("OTC Eligible Accounts") in excess of the net asset value of the positions held in such OTC Eligible Accounts, for each OTC Index Option Clearing Member for the previous month across all positions in all OTC Eligible Accounts of such Clearing Member) represents in relation to the total amount of such margin posted by all Participants. The Corporation shall rank the submitted bids from best to worst and the auction portfolio shall be allocated among the bidding Participants accordingly until the entire auction portfolio is exhausted. The bid price that is sufficient to clear the entire auction portfolio shall be the single price to be used for all winning bids (the "Clearing Price").

(B) In the event the Clearing Price is set by an outlier bid, as determined by the Corporation, the Corporation may choose an alternative clearing price that clears at least 80% of the auction portfolio. The remaining auction portfolio shall then be re-auctioned pursuant to the OTC Auction Procedures.

(C) If the liquidation of the suspended Clearing Member's business with the Corporation pursuant to this Chapter XI results in a deficiency that would result in a proportionate charge against the Clearing Fund contributions of all other Clearing Members pursuant to Article VIII, Section 5 of the By-Laws, then each Participant that failed to purchase or assume a percentage of the auction portfolio at least equal to its minimum participation level shall be subject to a priority charge ("Priority Charge") against such Participant's Clearing Fund contribution. The amount of the Priority Charge shall be determined in accordance with a formula set forth in the OTC Options Auction Procedures; provided that the Priority Charge shall not exceed the amount of the Clearing Member's required Clearing Fund deposit at the time the Priority Charge is made. If a deficiency remains after application of such Priority Charges, the Corporation shall then make a proportionate charge against the Clearing Fund contributions of all Clearing Members, including Participants, pursuant to Article VIII, Section 5 of the By-Laws; provided, however, that if a Participant notifies the Corporation within the specified time following such proportionate charge that it will terminate its status as a Clearing Member as permitted, and in satisfaction of the conditions imposed, under Article VIII, Section 6 of the By-Laws, then the amount of any Priority Charge to which such Participant was subject shall be treated as if it had been a part of the proportionate charge and shall not be construed to increase the maximum liability of the Participant to make additional contributions to the Clearing Fund pursuant to such Section 6.

(f) – (g) [no change]

[...Interpretations and Policies (Effective January 1, 2008)]

.01 When a stock option contract is adjusted to require delivery of a fixed amount of cash and the expiration date is accelerated pursuant to Rule 807, the "exercise by exception" threshold for such contract for purposes of paragraph (a)(iii) shall be \$.01 per share.]⁶

⁶ This interpretation is redundant to the identical provision under Rule 807 and is proposed to be deleted because it was placed here in error.

.02 See Interpretation and Policy .02 following Rule 1104 for a description of the private auction process by which OCC may close out a suspended Clearing Member's open positions in cleared contracts generally.⁷ See Rule 1106(e)(2) for a description of the alternative private auction process by which OCC may close out a suspended Clearing Member's open positions in OTC options, related positions and margin assets in certain circumstances.

* * *

CHAPTER XIII

FUTURES, FUTURES OPTIONS AND COMMODITY OPTIONS

* * *

Price Differential Spreads

RULE 1301A. (a) A "Price Differential Spread" is a pair of confirmed trades [Exchange transactions] resulting from a type of order where the party placing the order seeks to simultaneously buy and sell futures contracts on the same underlying interest but with different contract months (each such transaction referred to as a "leg" of the Price Differential Spread), provided that the price at which contracts are bought in one leg less the price at which contracts are sold in the other leg (the "price differential") is no greater than the limit specified by such party. The party placing the order may choose to (i) record the contract prices of both legs of a Price Differential Spread at the prices at which the contracts are [matched] confirmed on the Exchange ("Spread Engine Prices"), or (ii) record the contract price of the contracts with the nearer contract month (the leg in which such contracts are bought or sold referred to as the "front leg") at the Exchange-reported closing price for such contracts on the trading day immediately preceding the day on which such contracts are executed, and record the contract price of the contracts with the more distant contract month (the leg in which such contracts are bought or sold referred to as the "back leg") at (A) the contract price of the front leg plus the price differential, if the front leg is the sale of futures contracts, or (B) the contract price of the front leg less the price differential, if the front leg is the purchase of futures contracts ("Spread Settle Prices").

(b) For purposes of Rule 401(a)(2), the [matched trade] report [for] of a confirmed trade [an Exchange transaction] in futures contracts that is part of a Price Differential Spread shall (i) include both the Spread Engine Price and the Spread Settle Price, identifying which of these two prices is to be initially recorded as the contract price; and (ii) include the Exchange-assigned identification number (the "Price Differential Spread ID") which links the two legs of a Price Differential Spread to each other. In the case where each counterparty to the trade has entered into the trade as part of its own Price Differential Spread, the [matched] confirmed trade report shall identify separately with respect to each counterparty the price to be initially recorded as the contract price and the Price Differential Spread ID.

⁷ The text of the first sentence of Interpretation and Policy .02 as presented in this rule change reflects material that is proposed to be added or deleted, but is not yet approved by the Commission. See SR-OCC-2012-11.

(c) – (d) [no change]

... *Interpretations and Policies:*

.01 [no change]

.02 A Clearing Member may modify contract prices only with respect to confirmed trades [Exchange transactions] in futures contracts for which a Price Differential Spread ID has been reported by the Exchange.

* * *

CHAPTER XVIII

INDEX OPTIONS AND CERTAIN OTHER CASH-SETTLED OPTIONS

* * *

Introduction

The Rules in this Chapter are applicable only to cash-settled options that are not specifically addressed elsewhere in the By-Laws and Rules, including index options (as defined in the By-Laws and which also include OTC index options) and cash-settled commodity options other than those that are binary options or range options (which are governed by the provisions of Article XIV of the By-Laws and Chapter XV of the Rules). The provisions of Chapter XIII of the Rules, other than Rule 1303, are not applicable to cash-settled commodity options. The Rules in Chapters I through XII are also applicable to cash-settled options, in some cases supplemented by one or more Rules in this Chapter, except for Rules that have been replaced in respect of such options by one or more Rules in this Chapter and except where the context otherwise requires. Whenever a Rule in this Chapter supplements or, for purposes of this Chapter, replaces one or more of the By-Laws or Rules in Chapters I through XII, that fact is indicated in brackets following the Rule in this Chapter.

Index Option Escrow Deposits

RULE 1801. (a) Escrow deposits may be made in respect of index option contracts, other than OTC index option contracts, carried by a Clearing Member in a short position in its customers' account with the Corporation in accordance with the provisions of this Rule. Such escrow deposits are referred to herein as "index option escrow deposits."

(b) – (l) [no change]

...*Interpretations and Policies* [no change]

Assignment and Allocation of Cash-Settled Option Exercises

RULE 1803. (a) Exercises accepted by the Corporation in respect of cash-settled option contracts shall be assigned and allocated in accordance with Rules 803 and 804 except as provided in paragraph (b) of this Rule and except that Delivery Advices shall not be made available by the Corporation for exercises of such option contracts. In lieu thereof, the Corporation shall make available to each Index Clearing Member information with respect to exercises and assignments of cash-settled option contracts [Exercise and Assignment Activity Reports] as provided in paragraph (c) of this Rule.

(b) Following the automatic exercise of the capped cash-settled option contracts in any series of capped cash-settled options, the exercises shall be assigned and allocated to all open short positions (including all short positions established in an opening writing transaction on the trading day preceding the day of the automatic exercise, but excluding short positions that were subject to closing purchase transactions on such day) in such series of options. Subject to the provisions of the By-Laws, the Corporation shall assign such obligations at or before 7:00 A.M. Chicago Time (8:00 A.M. Eastern Time) on the business day following the date of the automatic exercise. Rule 804 shall apply to allocations of automatic exercises of capped options.

(c) On each business day, the Corporation shall make available to each Index Clearing Member information [an Exercise and Assignment Activity report] reflecting:

(1) all exercises effected by such Clearing Member with respect to cash-settled option contracts and accepted by the Corporation on the preceding business day (or, in the case of the business day following an expiration date, on such expiration date), and all exercises effected by other Index Clearing Members and accepted by the Corporation on such day with respect to cash-settled option contracts that were assigned by the Corporation to an account of such Clearing Member;

(2) all automatic exercises of capped options in the accounts of such Clearing Member effected on the preceding business day, and all assignments of obligations relating to exercises on such day of capped options in the accounts of other Index Clearing Members to short positions in the accounts of such Clearing Member.

[Rule 1803 supplements Rules 803 and 804.]

Expiration Date Exercise Procedure for Cash-Settled [Index] Options

RULE 1804. (a) [no change]

(b) A Clearing Member shall be deemed to have properly and irrevocably tendered to the Corporation, immediately prior to the expiration time on each expiration date, an exercise notice with respect to every expiring cash-settled option contract identified [listed] in the Clearing Member's Expiration Exercise Report, other than a flexibly structured index option contract, quarterly index option contract, monthly index option contract, weekly index option contract, short term index option contract or OTC index option contract, that has an exercise settlement value of \$1.00 or more per contract, or such other amount as the Corporation may from time to time establish on not less than 30 days prior notice to all Index Clearing Members, unless the Clearing Member shall have duly instructed the Corporation, in accordance with Rule 805(b), to exercise none, or fewer than all, of such contracts. If a Clearing Member desires that any such

option contract not be exercised, it shall be the responsibility of the Clearing Member to give appropriate instructions to the Corporation in accordance with Rule 805(b).

(c) A Clearing Member shall be automatically deemed to have exercised, immediately prior to the Expiration Time on each expiration date, every expiring OTC index option contract, flexibly structured index option contract, quarterly index option contract, monthly index option contract, weekly index option contract, and short term index option contract identified [listed] in the Clearing Member's Expiration Exercise Report that has an exercise settlement amount of \$0.01 or more per contract in the case of OTC index option contracts and \$1.00 or more per contract in the case of all other types of index option contracts, or such other amount as the Corporation may from time to time establish on not less than 30 days prior notice to all Index Clearing Members.

(d) [no change]

[Rule 1804 supplements Rules 805 and, together with Rule 1802, replaces Rule 802.]

...Interpretations and Policies

.01 – .02 [no change]

.03 The Corporation has determined that, for purposes of paragraph (c) of this Rule 1804, an OTC index option will be automatically exercised at expiration if the exercise settlement amount is any positive amount.

* * *

CHAPTER XXI

CROSS-RATE FOREIGN CURRENCY OPTIONS

* * *

Daily Cash Settlements

RULE 2112. (a) On each business day, the Corporation shall make available to each Cross-Rate Clearing Member a report listing, among other things, all confirmed trades [Exchange transactions] of the Clearing Member in cross-rate foreign currency options in each account of the Clearing Member as to which the Corporation received [matching] confirmed trade information on such business day and shall show the amount of the net daily premium payable to or by the Clearing Member in each trading currency with respect to each such account.

(b) In the event that the net daily premium listed in the report delivered to a Clearing Member pursuant to paragraph (a) of this Rule is payable by such Clearing Member to the Corporation, the Corporation shall be authorized to withdraw such amount from the bank account designated by the Clearing Member in respect of the applicable trading currency at or prior to the settlement time for confirmed trades [Exchange transactions] settled in such trading currency.

(c) The Corporation shall be obligated to credit to each Clearing Member any net daily premium amount due from the Corporation to such Clearing Member in such trading currency in each

account as shown in the report referred to in paragraph (a) of this Rule only to the extent that such amount exceeds the net amount of premiums payable to the Corporation at a later settlement time (or at an earlier settlement time, but not yet paid) in respect of confirmed trades [Exchange transactions] in cross-rate foreign currency options in the same account as to which the Corporation received [matching] confirmed trade information on the preceding day. Any net daily premiums so credited shall be retained by the Corporation and shall be treated as cash margin deposits [and shall be applied to reduce the provisional margin deficit or increase the provisional margin excess for purposes of settlements in trading currencies having a later settlement time. The Clearing Member may obtain the release of premium amounts held as margin to the extent that the Clearing Member makes a timely deposit of additional margin assets to reduce or eliminate the margin deficit plus any net daily premiums payable by the Clearing Member that have not yet been paid]. Premiums held as margin shall be released by the Corporation in accordance with such procedures as the Corporation shall specify.

(d) [no change]

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CHAPTER XXIV

FLEXIBLY STRUCTURED INDEX OPTIONS DENOMINATED IN A FOREIGN CURRENCY

* * *

Daily Cash Settlements

RULE 2410. (a) At or before such time as the Corporation shall prescribe on each business day, the Corporation shall make available to each FX Index Option Clearing Member a report listing, among other things, all confirmed trades [Exchange transactions] of the Clearing Member in FX Index Options in each account of the Clearing Member as to which the Corporation received [matching] confirmed trade information on such business day and shall show the amount of the net daily premium payable to or by the Clearing Member in each trading currency with respect to each such account.

(b) In the event that the net daily premium listed in the report delivered to a Clearing Member pursuant to paragraph (a) of this Rule is payable by such Clearing Member to the Corporation, the Corporation shall be authorized to withdraw such amount from the bank account designated by the Clearing Member in respect of the applicable trading currency at or prior to the settlement time for confirmed trades [Exchange transactions] settled in such trading currency.

(c) The Corporation shall be obligated to credit to each Clearing Member any net daily premium amount due from the Corporation to such Clearing Member in such trading currency in each account as shown in the report referred to in paragraph (a) of this Rule only to the extent that such amount exceeds the net amount of premiums payable to the Corporation at a later settlement time (or at an earlier settlement time, but not yet paid) in respect of confirmed trades [Exchange transactions] in FX Index Options in the same account as to which the Corporation

received [matching] confirmed trade information on the preceding day. Any net daily premiums so credited shall be retained by the Corporation and shall be treated as cash margin deposits. Premiums held as margin shall be released by the Corporation in accordance with such procedures as the Corporation shall specify.

(d) [no change]

Item 2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by OCC's Board of Directors at a meeting held on August 23, 2010.

Questions regarding the proposed rule change should be addressed to Stephen Szarmack, Vice President and Associate General Counsel, at (312) 322-4802.

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

The purpose of this proposed rule change is to allow OCC to provide central clearing of OTC index options on the S&P 500 Index. OCC will clear the proposed OTC options in a manner that is highly similar to the manner in which it clears listed options, with only such modifications as are appropriate to reflect the unique characteristics of OTC options.

OTC Options

OCC has entered into a license agreement with Standard & Poor's Financial Services LLC ("S&P") that allows OCC to clear OTC options on three equity indices published by the S&P: the S&P 500 Index, the S&P MidCap 400 Index and the S&P Small Cap 600 Index. The initial OTC options to be cleared by OCC will consist of options on the S&P 500 Index. OCC may clear OTC options on other indices and on individual equity securities in the future, subject to Commission approval of one or more additional rule filings. The current rule filing

defines “OTC option” and “OTC index option” generically in order to simplify future amendments to provide for additional underlying interests. OTC options will have predominantly common terms and characteristics, but also include unique terms negotiated by the parties. Transactions in OTC options will not be executed through the facilities of any exchange, but will instead be entered into bilaterally and submitted to OCC for clearance through one or more providers of trade affirmation services.⁸

OTC options will be similar to exchange-traded standardized equity index options called “FLEX Options” that are currently traded on certain options exchanges.⁹ FLEX Options are exchange-traded put and call options that allow for customization of certain terms. For example, FLEX index Options traded on the Chicago Board Options Exchange have six customizable terms: (1) underlying index, (2) put or call, (3) expiration date, (4) exercise price, (5) American or European exercise style, and (6) method of calculating settlement value. OCC is the issuer and guarantor of FLEX Options and clears FLEX Options traded on multiple exchanges.

Similar to FLEX Options, OTC options will allow for customization of a limited number of variable terms with a specified range of values that may be assigned to each as agreed between the buyer and seller. Parties submitting transactions in OTC options for clearing by OCC will be able to customize six discrete terms: (1) underlying index;¹⁰ (2) put or call; (3)

⁸ The initial provider of the trade affirmation services in connection with the OTC options will be MarkitSERV.

⁹ Note that FINRA Rule 2360(a)(16) refers to FLEX Options as “FLEX Equity Options,” which it defines as “any options contract issued, or subject to issuance by, The Options Clearing Corporation whereby the parties to the transaction have the ability to negotiate the terms of the contract consistent with the rules of the exchange on which the options contract is traded.” OCC does not believe this definition would capture OTC options as they are not traded on any exchange. Nevertheless, as discussed below, OCC is working with FINRA to amend certain of FINRA’s rules to clarify the proper application of such rules to OTC options.

¹⁰ Initially, however, the S&P 500 Index will be the only permitted underlying index.

exercise price; (4) expiration date; (5) American or European exercise style; and (6) method of calculating exercise settlement value on the expiration date.¹¹ The variable terms and permitted values will be specified in the proposed Section 6 of Article XVII of the By-Laws. With respect to future OTC options accepted for clearing, OCC intends that such future OTC options will conform to the general variable terms and limits on the variable terms set forth in proposed Section 6 of the By-Laws, and will either amend the Interpretations and Policies thereunder to specify additional requirements for specific OTC options or publish such requirements on OCC's website.

Clearing of OTC Options

OCC proposes to clear OTC options subject to the same basic rules and procedures used for the clearance of listed index options. The proposed rules require that the counterparties to the OTC options must be eligible contract participants ("ECPs"), as defined in Section 3a(65) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and Section 1a(18) of the Commodity Exchange Act, as amended (the "CEA").¹² Because an OTC option will be a "security" as defined in the Exchange Act, the proposed rules also require that the transactions be cleared through a clearing member of OCC that is registered with the Commission as a broker-dealer or one of the small number of clearing members that are "non-U.S. securities firms" as defined in OCC's By-Laws.¹³ OCC is not proposing to require clearing

¹¹ The expiration date of an OTC option must fall on a business day. The method of determining the exercise settlement value of an OTC option on its expiration date may be either the opening settlement value or the closing settlement value of the underlying index (calculated by S&P using the opening or closing price, as applicable, in the primary market of each component security of the underlying index on the specified expiration date), in each case as reported to OCC by CBOE.

¹² See proposed Section 6(f), Article XVII of the By-Laws.

¹³ See proposed Interpretation and Policy .11 of Section 1, Article V of the By-Laws.

members to meet any different financial standards for clearing OTC options. However, clearing members must be specifically approved by OCC to clear OTC options pursuant to new Interpretation and Policy .11 to Section 1 of Article V in order to assure the operational readiness of such clearing members to clear OTC options. Clearing members seeking to clear OTC options will be required to submit a business expansion request and complete an operational review. The operational review consists of an initial meeting with the clearing member's staff to evaluate the staff's experience, confirm the staff's familiarity with current OCC systems and procedures, complete an operational questionnaire, perform a high level review of the clearing member's systems and processing capabilities, and review other pertinent operational information. Successful testing of messaging capability between the clearing member, MarkitSERV and OCC is also necessary. These procedures will determine whether the firm is operationally ready to clear OTC Index Options.

Exercise of an OTC option will be settled by payment of cash by the assigned writer and to the exercising holder through OCC's cash settlement system on the business day following exercise in exactly the same manner as is the case with exercise settlement of listed index options. As in the case of listed index options, the exercise-settlement amount will be equal to the difference between the current value of the underlying interest and the exercise price of the OTC option, times the multiplier that determines the size of the OTC option. In the case of OTC index options on the S&P 500, the multiplier will be fixed at 1. The multipliers for additional OTC index options that OCC may in the future clear may be fixed at such value as OCC determines and provides for in its By-Laws and Rules.

OCC will calculate clearing margin for the OTC options using its STANS margin system on the same basis as for listed index options and will otherwise apply the same risk

management practices to both OTC options and listed index options, including new risk modeling enhancements for longer-tenor options discussed below under “Risk Management Enhancement for Longer-Tenor Options.” Because OCC currently clears listed options on all three of the underlying indexes on which OCC is currently licensed to clear OTC options, and because the customizable terms of these OTC options are relatively limited and the range of values that customizable terms may be given is limited, OCC does not believe that valuation and risk management for these OTC options present challenges that are different from those faced in the listed options market. Nevertheless, as discussed further below, OCC is proposing special OTC Options Auctions to be used in the unlikely event that OCC would be unable to close out positions in OTC options of a failed clearing member through other means.

OTC options may be carried in a clearing member’s firm account, in market-maker accounts or in its securities customers’ account, as applicable. Although customer positions in OTC options will be carried in the securities customers’ account (an omnibus account), OCC will use a “customer ID” to identify positions of individual customers based on information provided by clearing members.¹⁴ However, positions are not presently intended to be carried in individual customer sub-accounts, and positions in OTC options will be margined at OCC in the omnibus customers’ account on the same basis as listed options. If a clearing member takes the other side of a transaction with its customer in an OTC option, the transaction will result in the creation of a long or short position (as applicable) in the clearing member’s customers’ account and the opposite short or long position in the clearing member’s firm

¹⁴ Such customer IDs are necessary in order to allow OCC to comply with certain terms of OCC’s license agreement with S&P. As described further below, customer IDs will be used for other purposes as well.

account. The positions could also be includable in the internal cross-margining account, subject to any necessary regulatory approvals.

The trade data for an OTC option trade will be entered into the system of MarkitSERV or another trade confirmation/affirmation vendor approved by OCC for this purpose (the "OTC Trade Source").¹⁵ While MarkitSERV will be the only OTC Trade Source at launch, OCC will permit additional OTC Trade Sources in the future in response to sufficient market demand from OCC's clearing members and subject to the ability of any such OTC Trade Source to meet OCC's requirements for operational readiness and interoperability with OCC's systems, as well as requirements with respect to relevant business experience and reputation, adequate personnel and expertise, financial qualification and such other factors as OCC deems relevant. OCC will receive confirmed trades from the OTC Trade Source. It will be permissible for parties to submit trades for clearance that were entered into bilaterally at any time in the past, provided that the eligibility for clearance will be determined as of the date the trade is submitted to OCC for clearance.¹⁶ The OTC Trade Source will process the trade and submit it as a confirmed trade to OCC for clearing. If the trade meets OCC's validation requirements, OCC will so notify the OTC Trade Source, which will notify the submitting parties. Customers of clearing members may have direct access to the OTC Trade Source for purposes of entering or

¹⁵ MarkitSERV, LLC is owned by Markit Group Limited, Markit Group Holdings Limited and The Depository Trust & Clearing Corporation. MarkitSERV Limited is a wholly-owned U.K. subsidiary of MarkitSERV, LLC. MarkitSERV, LLC and MarkitSERV Limited (collectively, "MarkitSERV") provide derivatives transaction processing, electronic confirmation, portfolio reconciliation services, and other related services for firms that conduct business in the over-the-counter derivatives markets through a variety of electronic systems, including the MarkitWire system. MarkitWire, owned by MarkitSERV Limited, is an OTC derivatives electronic confirmation/affirmation service offered by MarkitSERV as part of its post-trade processing suite of products. The role of MarkitSERV and MarkitWire in OCC's clearing of OTC options is described in further detail below.

¹⁶ OCC's license agreement with S&P imposes certain requirements relating to minimum time remaining to expiration of an OTC option, as set forth in proposed Interpretation and Policy .01 of Section 6, Article XVII of the By-Laws.

affirming trade data and receiving communications regarding the status of transactions, in which case mechanisms will be put in place for a clearing member to authorize a customer to enter a trade for the clearing member's customers' account or for the clearing member to affirm a trade once entered.

In order for a clearing member to be approved for clearing OTC options, the clearing member must enter into a standard agreement with MarkitSERV (or another OTC Trade Source with which the clearing member intends to enter trade data, if and when OCC enters into arrangements with other OTC Trade Sources). At launch, OTC options will not be subject to the same clearing member trade assignment rules and procedures through which exchange-traded options can be cleared by a clearing member other than the executing clearing member. This functionality may be added at a later date. OCC and MarkitSERV will adopt procedures to permit a customer that has an account with Clearing Member A ("CM A") to enter into an OTC option transaction with Clearing Member B ("CM B") and have the position included in its account at CM A and cleared in CM A's customers' account at OCC.

OTC options will be fungible with each other to the extent that there are OTC options in the system with identical terms. However, OCC will not treat OTC options as fungible with index options listed on any exchange, even if an OTC option has terms identical to the terms of the exchange-listed option.

Clearing members that carry customer positions in cleared OTC options will be subject to all OCC rules governing OCC-cleared options generally, as well as all applicable rules of the Commission and of any self-regulatory organization, including the Financial Industry Regulatory Authority ("FINRA"), of which they are a member. Section 8 of Article III of OCC's By-Laws provides that, subject to the By-Laws and Rules, "the Board of Directors may

suspend Clearing Members and may prescribe and impose penalties for the violation of the By-Laws or the Rules of the Corporation, and it may, by Rule or otherwise, establish all disciplinary procedures applicable to Clearing Members and their partners, officers, directors and employees.” As a condition to admission, Section 3(c) of Article V of the By-Laws provides that a clearing member must agree, among other things, to “pay such fines as may be imposed on it in accordance with the By-Laws and Rules.” Rule 305 permits OCC to impose restrictions on the clearing activities of a clearing member if it finds that the financial or operational condition of the clearing member makes it necessary or advisable to do so for the protection of OCC, other clearing members, or the general public. Rule 1201(a) provides that OCC “may censure, suspend, expel or limit the activities, functions or operations of any Clearing Member for any violation of the By-Laws and Rules or its agreements with the Corporation.” In addition to, or in lieu of, such actions, OCC is permitted under the same paragraph to impose fines. Rule 1202(b) establishes procedures for taking any such disciplinary actions. The foregoing provisions are sufficient to permit OCC to fine or otherwise discipline a clearing member that fails to abide by OCC’s By-Laws and Rules applicable to OTC options, or to prohibit such clearing member from continuing to clear such options.

Regulatory Status of the OTC Options

An OTC option will be a “security” as defined in both the Securities Act of 1933, as amended (the “Securities Act”) and, as noted above, the Exchange Act. OCC will be the “issuer” of the OTC options. The OTC options will be neither “swaps” nor “security-based

swaps” for purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”).¹⁷

Most of OCC’s clearing members are members of FINRA and subject to FINRA’s rules, which have different provisions for “listed” and “OTC options” and contain various definitions distinguishing between the two. In some cases, OTC options would fall into neither category under FINRA’s definitions and in other cases, they would fall within what OCC perceives to be the wrong category. FINRA and OCC are working together to implement appropriate amendments to FINRA rules to clarify the proper application of such rules to cleared OTC options.

MarkitSERV Trade Submission Mechanics

MarkitSERV provides an interface to OCC that allows OCC to receive messages containing details of transactions in OTC options submitted for clearing by clearing members with access to MarketWire and also allows OCC to transmit messages to MarkitWire participants identifying the status of submitted transactions. MarkitWire applications use product-specific templates to simplify deal entry and negotiations. The templates specify the data required for a given product and also the business validation rules for each field. MarkitSERV has included OCC’s validation requirements for OTC options in its trade templates.

The trade data for each OTC option transaction must be entered into MarkitWire. MarkitSERV will use a “confirmation/affirmation” procedure in which one party to the trade enters the trade data to the MarkitWire platform, which issues a confirmation to the counterparty

¹⁷ Section 1a(47)(A)(i) of CEA, as added by Section 721(a)(21) of Dodd-Frank, defines “swaps” broadly to include options on indices. However, Section 1a(47)(B)(iii) of the CEA excludes from the “swap” definition any option on any index of securities that is subject to the Securities Act and the Exchange Act. A contract that is excluded from

to be affirmed, rejected or requested to be revised. If the trade details are confirmed, the trade will then be submitted to OCC for clearance and MarkitSERV will affirm such submission to both parties. OCC then validates the trade information for compliance with applicable requirements, such as the identification of an account of an eligible clearing member in which each side of the trade will be cleared, that the variable terms are within permissible ranges, and that minimum size requirements under OCC's license agreement with S&P are met. This validation will be completed by OCC immediately upon submission. OCC's clearing system will automatically accept the trade if it passes the validation process and will otherwise reject it.¹⁸ A trade that is rejected by OCC may be corrected and submitted as a new transaction. Clearing members and customers with access to MarkitSERV will be able to determine whether a trade has been accepted or rejected both through MarkitSERV and, in the case of clearing members, through their interface with OCC's clearing system.

MarkitSERV's Regulatory Status¹⁹

MarkitSERV is not registered as a clearing agency under the Exchange Act, and the Commission staff has asked OCC to consider whether MarkitSERV would be required to so register in order to provide the proposed services to the OTC options market. OCC believes that no such registration is necessary based upon relevant interpretive guidance issued by the Commission.

the definition of a "swap" under Section 1a(47)(B) (other than Section 1a(47)(B)(x)) is not a "security-based swap" for purposes of Section 3a(68) of the Exchange Act.

¹⁸ Once accepted, a trade is guaranteed by OCC. Note, however, that OTC options for which the premium payment date communicated by MarkitSERV to OCC is prior to the business day on which the OTC option is submitted to OCC for clearing (referred to as a "Backloaded OTC Option") will not be accepted and guaranteed until the selling clearing member has met its initial morning cash settlement obligations to OCC on the following business day.

¹⁹ MarkitSERV offers different services in different markets, and this discussion is addressed only to the "confirmation/affirmation" procedure to be used in submitting trades to OCC.

Section 3(a)(23)(A) of the Exchange Act defines a “clearing agency” broadly.

The definition includes, in relevant part, “any person who . . . provides facilities for comparison of data respecting the terms of settlement of securities transactions[.]” In 1998, the Commission issued a release entitled “Confirmation and Affirmation of Securities Trades; Matching” (the “Matching Release”).²⁰ In the Matching Release, the Commission published “its interpretation that a ‘matching’ service that compares securities trade information from a broker-dealer and the broker-dealer’s customer is a clearing agency function.” The Matching Release distinguishes between such a matching service and a “confirmation/affirmation service” where the “vendor intermediary will only transmit information between the parties to a trade, and the parties will confirm and affirm the accuracy of the information.” The Commission noted that “matching” constitutes the “comparison of data respecting the terms of settlement of securities transactions” and that such services therefore trigger status as a clearing agency, while confirmation/affirmation services would not, by themselves, constitute such a data comparison. The Commission concluded in the Matching Release that “an intermediary that captures trade information from a buyer and a seller of securities and performs an independent reconciliation or matching of that information is providing facilities for the comparison of data within the scope of Exchange Act Section 3(a)(23).” The Commission stated that “matching” is “so closely tied to the clearance and settlement process that it is different not only in degree but also different in kind from the . . . confirmation and affirmation process.” The Matching Release goes on to state: “a vendor that provides confirmation/affirmation services only will exchange messages between a broker-dealer and its institutional customer. The broker-dealer and its institutional customer will compare the trade information contained in those messages, and the institution itself will

²⁰ 63 Fed. Reg. 17943 (April 13, 1998).

issue the affirmed confirmation.” This is precisely what occurs when a counterparty to a trade affirms the trade data through MarkitSERV and requests submission to OCC for clearance. MarkitSERV transmits messages only; it does not “compare” or “match” trade data submitted by two parties.

The “confirmation/affirmation” functionality (as described above) to be provided by MarkitSERV (through MarkitWire) with respect to OTC options is functionally identical to the confirmation/affirmation service described in the Matching Release and OCC believes such service would not be a “matching” service within the meaning of the release. OCC believes that MarkitSERV will not be a “clearing agency” with respect to the services to be provided in connection with OTC options. The confirmation/affirmation service described in the Matching Release referred “to the transmission of messages among broker-dealers, institutional investors, and custodian banks regarding the terms of a trade executed for the institutional investor.” MarkitWire’s confirmation/affirmation process will allow for the transmission of messages among OCC’s clearing members (most of which are registered broker-dealers), their customers (all of whom will be ECPs and will therefore be large and financially sophisticated market participants) and OCC, which is itself registered and subject to the Commission’s oversight as a clearing agency.

By contrast, the “matching” services contemplated in the Matching Release would involve “the process whereby an intermediary compares the broker dealer’s trade data submission . . . with the institution’s allocation instructions . . . to determine whether the two descriptions of the trade agree.” MarkitWire performs no such comparison. Under the confirmation/affirmation procedure, trade data is entered into MarkitWire by one party and such data is made available to the counterparty to be affirmed, rejected or requested to be revised.

MarkitWire merely facilitates the transfer of information between the parties sufficient to allow the comparison to be made. A binding transaction (*i.e.*, an “affirmed confirmation” in the language of the Matching Release) is not produced through any action of MarkitSERV, but is instead created by the completion, by the counterparty, of an affirmation of the trade data entered by the first party. MarkitWire provides no “independent reconciliation or matching” of trade data. Rather MarkitWire is providing essentially a messaging service among OCC and the parties to trades in OTC Options. The Matching Release is clear as to the distinction between a matching service and a confirmation/affirmation service, and OCC believes that there is no ambiguity that the services to be provided by MarkitWire with respect to OTC options fall into the latter, rather than the former, category.

Risk Management Enhancements for Longer-Tenor Options

Although OCC’s license agreement with S&P allows OCC to clear OTC options with tenors of up to fifteen years, OCC has elected at this time to clear only OTC options on the S&P 500 index with tenors of up to five years. However, OCC currently clears FLEX Options on the S&P 500 with tenors of up to 15 years. While OCC believes that its current risk management practices are adequate for current clearing activity, OCC is in the process of implementing risk modeling enhancements with respect to longer-tenor options, including OTC options. The enhancements are part of OCC’s ongoing efforts to test and improve its risk management operations with respect to all longer-tenor options that OCC currently clears. These procedures will be submitted for review in a separate “advance notice” filing and OCC will not commence clearing of OTC options until such procedures have been approved and implemented.

The proposed enhancements are as follows:

- First, OCC will introduce indicative over-the-counter quotations into the daily dataset of prices used to risk manage OCC-cleared products. These quotations will be obtained from a service provider that will collect OTC dealer polling information on a daily basis and provide such data to OCC.
- Second, OCC will introduce variations in the implied volatilities used in the modeling of all cleared options whose residual tenors are at least three years. To date, OCC's margin methodology has assumed that implied volatilities of option contracts are static over the two-day risk horizon. While OCC's backtesting has identified few exceedances related to implied volatility shocks, such shocks could occur and taking them into account in OCC's margin model will allow more robust risk management. OCC proposes to achieve this result by incorporating into the risk factors included in OCC's models time series of proportional changes in implied volatilities for a range of representative volatilities.
- Third, OCC will introduce a valuation adjustment into its calculation of portfolio net asset value. This adjustment will be based on the aggregate sensitivity of the longer-tenor options in a portfolio to the overall level of implied volatilities at three and five years, and to the implied volatility skew.

A review of individual S&P 500 Index put and call options positions that are in the money by varying amounts and have expiration dates between four and nine years out indicates that the inclusion of modeled implied volatilities tends to result in less margin being held against short call positions and more being held against short put positions. These results

are consistent with what would be expected given the strong negative correlation that exists between changes in implied volatility and market returns. On average, we observed a decrease in the margin requirement of approximately 24% on the nine call options tested and a 63% increase associated with the nine put options.

Proposed By-Law and Rule Changes

The specific proposed changes to OCC's By-Laws and Rules to provide for the clearing of OTC options relate primarily to: (i) specification of customizable terms; (ii) procedures for submission and acceptance of trades for clearance; and (iii) specification of criteria for eligibility of clearing members to clear transactions in OTC options and limitation of the types of customers for whom clearing members may effect transactions in OTC options. Otherwise, the currently proposed OTC options will be cleared and settled under the same provisions applicable to clearance of listed index options. Many of the proposed amendments are self-explanatory, and we have therefore attempted to confine the following discussion to a broad overview with specific explanation only where the reasons for the change may be less obvious.

Article I of the By-Laws contains defined terms used throughout the By-Laws and Rules. OCC proposes to modify certain existing definitions and include certain new definitions in order to incorporate OTC options into existing rules and facilitate the creation of new provisions unique to OTC options. Throughout the By-Laws and Rules, OCC proposes to replace the term "Exchange transaction," which is currently defined in Article I, in relevant part, as "a transaction on or through the facilities of an Exchange for the purchase, writing or sale of a cleared contract" with the term "confirmed trade" so as to make the relevant portions of the By-Laws and Rules applicable to transactions in OTC options as well as listed options, without

causing confusion about the role of the OTC Trade Source in OCC's clearing of OTC options. "Confirmed trade" is proposed to be defined in Article I to include transactions "effected on or through the facilities of an exchange" or "affirmed through the facilities of an OTC Trade Source" in order to include transactions in both listed options and OTC options. The current definition of "confirmed trade" in Rule 101 is proposed to be deleted as unnecessary given the new definition. Much of the length of this rule filing is attributable to the fact that the term "Exchange transaction" is used so many places in the rules. OCC has entered into agreements in the past which reference the term "Exchange transaction" or "exchange transaction." OCC is also proposing to add an Interpretation and Policy to the new definition of "confirmed trade" in order to avoid any ambiguity concerning how such terms should be interpreted in any such agreement.

OCC proposes to add a new Interpretation and Policy .11 to Section 1 of Article V of the By-Laws, providing the additional criteria that must be met by a clearing member in order to clear OTC index options. Among these new criteria are that clearing members seeking to clear OTC index options on underlying indices published by Standard & Poor's Financial Services LLC ("S&P") must execute and maintain in effect a short-form license agreement in such form as specified from time to time by S&P. The current form of S&P short-form index license agreement is attached hereto as Exhibit 3.

The Interpretations and Policies under Section 1, Article VI allow clearing members to adjust their positions with OCC for certain enumerated reasons. OCC proposes to amend the Interpretations and Policies to clarify that adjustment of positions in OTC options will be effected through a manual process (as opposed to the electronic process available to post-trade adjustments in listed options), to the extent permitted by OCC. For the same reason, OCC is

proposing to amend Rule 403 to prohibit clearing member trade assignment (“CMTA”) transactions in OTC options. Trade “give-ups” that are effected through the CMTA process in the case of listed options will, in the case of OTC options, be effected through MarkitSERV before the trades are submitted to OCC for clearing.

Article XVII of the By-Laws governs index options in general and OCC is proposing amendments to Article XVII in order to set forth the terms applicable to the initial OTC options proposed to be cleared by OCC — options on the S&P 500 Index — and to differentiate OTC index options from other index options cleared by OCC. For example, certain amendments to the definitions are necessary because OTC options will be permitted to have a much wider range of expiration dates than exchange-traded options (other than FLEX Options). Additional definitional amendments ensure that OTC index options will constitute a separate class of options from other cash-settled index options even if both index options have the same terms and cover the same underlying interest.

Section 3 of Article XVII provides for adjustment of the terms of outstanding index options as necessary to reflect possible changes in the underlying index — such as those creating a discontinuity in the level of the index — that could theoretically make an adjustment necessary to protect the legitimate expectations of holders and writers of options on the index. Pursuant to paragraph (g) of Section 3, most but not all such adjustments would be made, in the case of listed index options, by an adjustment panel consisting of representatives of the exchanges on which the options are traded. In the case of OTC options, any such adjustments will be made by OCC in its sole discretion. However, in exercising that discretion, OCC may

take into consideration adjustment made by the adjustment panel with respect to exchange-traded options covering the same underlying index.²¹

OCC proposes to add a new Section 6 to Article XVII to set forth certain provisions unique to OTC index options, including the variable terms allowed for OTC index options and the general limitations on such variable terms. In general, all OTC index options must conform to the terms and limitations set forth in Section 6, and additional specific requirements applicable to specific OTC index options will either be set forth in the Interpretations and Policies under Section 6 or published separately on OCC's website. Section 6 also makes clear that although OTC index options are not fungible with exchange-traded index options, OTC index options of the same series (*i.e.*, options having identical terms) will be fungible with each other. In addition to the terms and limitations applicable to OTC index options, Section 6 will establish that clearing members will be deemed to have made a number of representations and warranties in connection with their activities in OTC options each time they affirm a confirmed trade entered into an OTC Trade Source.

OCC has submitted a rulemaking petition to the Commission²² seeking an amendment to Commission Rule 238 that would exempt the OTC Options from most provisions of the Securities Act. Unless another exemption from the registration requirements of the Securities Act is available, OCC intends to rely upon Rule 506 of Regulation D under the Securities Act, which is a safe harbor under the Securities Act exemption in Section 4(a)(2) for offerings by an issuer not involving a public offering. OCC intends to satisfy the conditions of

²¹Because index options, unlike options on individual stocks, rarely, if ever, require adjustments, allocation of the adjustment authority may have little practical significance.

²² See SEC File No. 4-644 (Submitted January 13, 2012), *available at* <http://www.sec.gov/rules/petitions/2012/petn4-644.pdf>.

Rule 506 of Regulation D as in effect at the time OCC relies upon the safe harbor. Participants in the existing markets for OTC equity options offered and sold in the United States commonly rely on the private offering exemption under these provisions and such reliance is therefore consistent with existing practice. OTC Options will be available for purchase only by highly sophisticated investors that are both “eligible contract participants,” as defined in Section 3a(65) of the Exchange Act, and “accredited investors,” as defined in Rule 501(a) under Regulation D. Section 6(f) of Article XVII includes representations of clearing members necessary to ensure that there is no general solicitation or general advertising in connection with the offer or sale of the OTC Options until such time as OCC notifies clearing members that such restriction no longer applies.

Chapter IV of the Rules sets forth the requirements for reporting of confirmed trades to OCC, and Rule 401 thereunder governs reporting of transactions in listed options by participant Exchanges. OCC is proposing to add new Rule 404 to govern the details of reporting of confirmed trades in OTC options by an OTC Trade Source.

As discussed above, positions in OTC options will generally be margined in the same manner as positions in listed options using STANS and pursuant to Chapter VI of the Rules. However, OCC proposes to amend Rule 611 to establish different procedures for the segregation of long positions in OTC options for margining purposes. Long positions in listed options are held in a clearing member’s customers’ account or firm non-lien account and by default are deemed to be “segregated,” meaning that they are not subject to OCC’s lien and are given no collateral value when determining the margin requirement in the account. Such positions may be unsegregated only when a clearing member instructs OCC to unsegregate a long position and represents to OCC that the long position is part of a spread transaction carried

for a single customer whose margin requirement on the corresponding short position has been reduced in recognition of the spread. OCC will then unsegregate the long position and so reduce OCC's margin requirement. However, in case of long positions in OTC options that are carried in a clearing member's customers' account and for which OCC has received a customer ID, OCC proposes that it will automatically unsegregate such long positions if OCC identifies a qualifying short position in OTC options carried under the same customer ID. Clearing members will not be required to give an affirmative instruction to OCC to unsegregate a long position in OTC options or make a separate representation regarding the spread transaction. Instead, by carrying a qualifying spread position in a customer account, clearing members are deemed to have represented to OCC that the customer's margin has been reduced in recognition of the spread. Based on discussion with the clearing members, it is OCC's understanding that, in practice, broker-dealers reduce customers' margin requirements to reflect spread positions. Therefore, OCC believes that automatic recognition of such spreads by OCC together with the deemed representation will greatly increase operational efficiency while providing equal assurance that long positions in OTC options will be unsegregated only if an identified customer will receive the benefit of the reduced margin required for spread transactions.

Rule 1001 sets forth the amount of the contribution that each clearing member is required to make to the clearing fund. OCC proposes to amend Rule 1001(c) so that, for purposes of calculating the daily average number of cleared contracts held by a clearing member in open positions with OCC during a calendar month (which number is used in turn to determine the clearing member's contribution to the clearing fund), open positions in OTC options will be adjusted as needed to account for any differences between the multiplier or unit of trading with respect to OTC options relative to non-OTC options covering the same underlying index or

interest so that OTC options and non-OTC options are given comparable weight in the computation.²³

In general, the rules in Chapter XI governing the suspension of a clearing member will apply equally to clearing members that transact in OTC options. Rule 1104 provides broad authority for OCC to liquidate a suspended clearing member's margin and clearing fund deposits "in the most orderly manner practicable." Rule 1106 provides similarly worded authority to close out open positions in options and certain other cleared contacts carried by a suspended clearing member. In 2011, the Commission approved an OCC rule change providing OCC the express authority to use a private auction as one of the means by which OCC may close out open positions and liquidate margin and clearing fund deposits of a suspended clearing member.²⁴ OCC anticipates it will use this auction process for OTC options as well. As an additional tool to ensure its ability to close out positions in OTC options promptly, OCC is proposing to amend Rule 1106 to provide for an alternative auction procedure specifically applicable only to OTC index options and related positions hedging, or hedged by, OTC index options (an "OTC Options Auction"). An OTC Options Auction would be used only in unusual circumstances where OCC determines it is not feasible to close out open positions in OTC index options through the other means provided for in OCC's Rules and By-Laws.²⁵ The amendments to Rule 1106 summarize the OTC Options Auction procedures and incorporate by reference the

²³ For example, the index multiplier applicable to OTC index options on the S&P 500 Index will be fixed at 1. See proposed Interpretation and Policy .01 of Section 6, Article XVII of the By-Laws. In comparison, the index multiplier applicable to listed index options is 100.

²⁴ See Securities Exchange Act Release 34-65654 (October 28, 2011), 76 FR 68238 (November 3, 2011). OCC subsequently filed a rule change, currently pending Commission approval, providing detailed procedures for the conduct of such an auction. See SR-OCC-2012-11.

²⁵ OCC anticipates that these procedures would be applicable to other OTC derivatives that may be cleared by OCC in the future. However, OCC has limited the currently proposed rule to OTC index options, and will amend it as and if appropriate to apply to other over-the-counter products that OCC may propose to clear in the future.

detailed procedures contained in a document entitled “OTC Options Auction Procedures,” which will be posted on the Corporation’s website and otherwise made available to clearing members upon request of OCC. A copy of the OTC Options Auction Procedures is attached hereto as Exhibit 5.

Rule 1106(e)(2)(C) clarifies that, in the event that the liquidation of a clearing member results in a deficiency that would otherwise result in a proportionate charge against the clearing fund contributions of other clearing members, each OTC Index Option Member (as defined below) that failed to purchase or assume its share of an auction portfolio will be the first to absorb the deficiency, through a “Priority Charge” against such clearing members’ clearing fund contributions. The Priority Charge is a “first loss” mechanism, and is not intended to increase a clearing member’s total maximum exposure to OCC.

Under the OTC Options Auction procedures, all clearing members authorized to clear transactions in OTC index options (“OTC Index Option Members”), other than the defaulting clearing member, will be required to participate in the OTC Options Auction by submitting competitive bids for all or a portion of the defaulting clearing member’s OTC index option portfolio. Each such participant will be subject to a minimum participation level based on the participant’s proportionate share of the total “risk margin” requirement posted by all OTC Index Options Members in the previous month for all positions (not limited to OTC option positions) held in accounts eligible to hold OTC options positions (“OTC Eligible Accounts”), after removing the defaulting clearing member.²⁶ This method of calculating the minimum participation level in the OTC Options Auction results in all OTC Index Option Members being

²⁶ This minimum participation level will be multiplied by 1.15 to calculate each participant’s minimum bid size, such that the sum of all participants’ bids will equal 115% of the auction portfolio, in order to increase the likelihood that the entire auction portfolio will be allocated to participants.

required to participate in the OTC Options Auction based on their clearing activity related to all positions in OTC Eligible Accounts. Required participation ensures that the OTC Options Auction will have sufficient participants authorized to clear transactions in OTC index options and that the most active clearing members in OTC index options will submit bids for the largest percentage of the auction portfolio, increasing the likelihood of the acquisition of OTC options positions by clearing members with appropriate financial strength, risk management capabilities and trading expertise. Each participant may submit bids at varying quantities and varying prices, so long as the participant's bids equal or exceed its minimum participation level. A participant may use bids from non-OTC Index Options Members and non-clearing members in order to meet its minimum participation level, subject to certain Corporation requirements including that it guarantee the performance of such third parties. Each bid will indicate what percentage of the auction portfolio the participant is bidding on and the amount of the bid. Bids will be stated in terms of a price for the entire auction portfolio, and may be either positive or negative.

(Negative bids imply an auction portfolio that has a negative net asset value and indicate how much the Corporation would be required to pay the participant to assume the relevant percentage of the auction portfolio.) The Corporation will rank the submitted bids from best to worst and the auction portfolio will be allocated among the bidding participants accordingly until the auction portfolio is exhausted. The bid price that is sufficient to clear the entire auction portfolio will become the single price to be used for all winning bids, even if a participant's stated bid was better.

In order to provide a strong incentive to ensure competitive bidding by the OTC Index Option Members required to participate in an OTC Options Auction, OTC Index Options Members who fail to win their minimum participation in the auction will be subject to a potential

priority charge against its clearing fund contribution. If the cost of liquidating a suspended clearing member's positions exhausts the clearing member's margin and clearing fund contribution and any other assets of the suspended clearing member available to OCC, then OCC, pursuant to Section 5 of Article VIII of the By-Laws, would ordinarily withdraw the amount of the deficiency from the clearing fund and charge it on a proportionate basis against all other clearing members' computed contributions as fixed at the time. When an OTC Options Auction has been held in respect of a suspended OTC Index Options Member, however, some or all of any such remaining loss would be assessed first against the clearing fund contributions of any OTC Options Auction participant(s) whose bids are insufficiently competitive to be allocated a portion of the auction portfolio equal to such participant's minimum required participation. This priority charge would be made regardless of the reason for the shortfall—*i.e.*, whether or not the loss resulted from the closing out of OTC options positions. The priority charge would be calculated based on an "assessment ratio," which is formulated to provide incentive to all OTC Options Auction participants to participate to their full minimum participation level in the auction. The method of calculating the assessment ratio is such that if the net asset value of the auction portfolio is zero the assessment ratio will also be zero and no priority charge will be made. As the absolute net asset value of the auction portfolio (whether positive or negative) increases, the assessment ratio also increases, all other factors being equal. If all OTC Options Auction participants submit bids such that each receives an allocation of OTC options positions equal to its minimum participation level, no priority charge will be made regardless of whether or not there is a liquidation shortfall. If a liquidation shortfall remains after any priority charges, or if no priority charges were required, the Corporation will then make a proportionate charge against the clearing fund contributions of all clearing members, including those that participated

in the OTC Options Auction, in the usual manner pursuant to Section 5 of Article VIII of OCC's By-Laws.

In order to protect the estate of the suspended clearing member, OCC reserves some discretion in supervising the auction. In the event that the bid price that clears the entire auction portfolio is determined by OCC to be an outlier bid, OCC may choose as the winning bid a price that clears at least 80% of the auction portfolio. The remaining auction portfolio will then be re-auctioned as described above.

OCC anticipates that the likelihood of having to use this alternative auction is small. Nevertheless, in view of the fact that positions in OTC index options are expected to be large and that there may be no active trading market in options with terms precisely identical to the terms of the OTC index options in question, OCC believes that this is an appropriate failsafe provision. It should be noted that the Chicago Mercantile Exchange Inc. ("CME") has rules allowing its clearing house and certain CME committees to administer an auction process to liquidate positions in interest rate swaps ("IRS") in the event of a default of a CME clearing member authorized to submit IRS for clearing (an "IRS Member").²⁷ Although the financial safeguards supporting IRS clearing, including its "guaranty fund," and the IRS auction process are different from OCC's clearing fund and OTC Options Auction in that, among other things, there is a separate guaranty fund for IRS, the IRS auction shares certain similarities with the OTC Options Auction. In particular, the IRS auction process requires mandatory participation of IRS clearing members with open interest in a position being auctioned and, in order to provide incentive for IRS Members to submit quality bids in an IRS auction, provides that in the event

²⁷ See CME Rules 8G14, 8G25 and 8G802.B. See also Commodity Futures Trading Commission Rule Change Submission No. 12-061RR of CME, the Board of Trade of the City of Chicago Inc. and the New York Mercantile Exchange, available at: <http://www.cmegroup.com/market-regulation/files/12-061rr.pdf>

there is a loss to CME's clearing house associated with an IRS Member's default, IRS Members that do not submit quality bids in an IRS auction are subject to having their IRS guaranty fund deposit assessed before assessments are made against other IRS clearing members' guaranty fund deposits. In its original rule filing, OCC had proposed a different failsafe solution whereby OCC could terminate open positions of a suspended clearing member by setting a close-out value that non-defaulting clearing members holding the opposite side of the suspended clearing member's positions would be required to accept or pay in settlement of the terminated positions. However, clearing members objected to that proposed method and have advocated the auction procedures proposed here in lieu of the early termination proposal.²⁸ Clearing members in an OTC advisory group were active in designing the OTC Options Auction procedures, including the priority charges.

Impact of Clearing OTC Options on Other OCC-Cleared Products

Cleared OTC options will not be fungible with listed options. However, an OTC option may have economic characteristics that are substantially similar or identical to the characteristics of options in series of listed options that OCC clears. While it is possible that in any given instance a market participant may elect to enter into an OTC option in lieu of an economically similar listed product, OCC does not believe that its clearing of OTC options will adversely affect the efficiency or liquidity of the listed markets. The OTC options markets currently exist to accommodate a variety of commercial and other needs of market participants, including the ability to customize the terms of transactions. While the availability of an OCC guarantee for OTC transactions in which the parties would otherwise be exposed to each others'

²⁸ See comment letter from Alessandro Cocco, Managing Director of J.P. Morgan Clearing Corporation and J.P. Morgan Securities LLC, to Ms. Elizabeth M. Murphy, Secretary, Securities and Exchange Commission (January 30, 2012), available at <http://www.sec.gov/comments/sr-occ-2011-19/occ201119-2.pdf>.

creditworthiness may cause transactions that currently occur in the non-cleared OTC markets to migrate to the cleared-OTC markets, OCC does not believe it will cause significant migration from the listed markets to the cleared OTC markets. The limitation of the OTC options markets to ECPs as well as the significant minimum transaction size and tenor requirements that are applicable to certain transactions in the currently proposed OTC options under the S&P License Agreement will limit the use of cleared OTC options and should help to ensure that there is no substantial migration from the listed markets to the OTC markets for this product. The existing bilateral OTC options markets have existed for years alongside the listed options markets, and OCC believes that dealers in such bilateral options often use the listed markets to hedge positions taken in such bilateral options and other OTC derivatives.

Notice of Launch Date

Following approval of this rule change by the Commission, OCC expects to provide notice to its clearing members of the date on which it intends to implement this rule change and begin clearing OTC options.

* * *

The proposed changes to OCC's By-Laws are consistent with the purposes and requirements of Section 17A of the Exchange Act because they are designed to permit OCC to clear OTC options subject to the same basic rules, procedures and risk management practices that have been used successfully by OCC in clearing transactions in listed options. OCC believes that clearance and settlement of OTC options pursuant to this rule filing is fully consistent with OCC's obligations with respect to the prompt and accurate clearance and settlement of securities transactions and the protection of securities investors and the public interest. The proposed rule change is not inconsistent with any existing rule of OCC.

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

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

Item 5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others.

Written comments were not and are not intended to be solicited with respect to the proposed rule change, and, except as discussed below in this Item 5, none have been received. OCC has been actively engaged with a number of clearing members that have expressed an interest in clearing OTC Options. The following are the only substantive written comments that were received, and they have been addressed, in the manner indicated:

- OCC received a written comment that the role of the Default Management Advisory Committee, as described in the OTC Options Auction procedures attached as Exhibit 5 to this rule filing, should be clarified. We have revised the procedures to clarify that the Default Management Advisory Committee will be a standing committee and will be formed from the inception of OCC's clearing of OTC Options. It will not be an *ad hoc* committee formed at the time of a default.
- OCC received a written comment asking that the Membership/Risk Committee have a role in setting exercise settlement values with respect to OTC index options in unusual circumstances pursuant to Section 4(a)(2) of Article XVII of the ByLaws. We have revised the rules to provide that OCC will consult with that committee when appropriate in setting exercise settlement values pursuant to Section 4(a)(2).

- OCC received a written comment asking for limitations on the indemnification of OCC by clearing members under Section 6(f) of Article XVII of the ByLaws. In response to this comment we have added an exclusion from the indemnity for claims, liabilities, or expenses that result primarily from OCC's gross negligence or willful misconduct or from OCC conduct that causes the offer or sale of the OTC Options to become subject to the registration provisions of Section 5 of the Securities Act.

Item 6. Extension of Time Period for Commission Action

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

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)

Neither summary effectiveness nor accelerated effectiveness is sought.

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

The proposed rule change is not based on a rule change of another self-regulatory organization.

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

OCC is filing this proposed rule change as an “advance notice” pursuant to Section 806(e)(2) of the Payment, Clearing, and Settlement Supervision Act of 2010 because it could be deemed to materially affect the nature or level of risks presented by OCC.

Notwithstanding the foregoing, OCC believes that the risks presented by OTC options are not truly unique to OTC options but rather are highly similar to risks presented to OCC, OCC clearing members and the market by exchange-traded “FLEX” options.

OTC options are nearly identical to listed FLEX options on the S&P 500 that OCC has cleared for many years. OTC options have the same degree of customization as FLEX options except that OTC options are limited to a maximum tenor of 5 years whereas FLEX options can have tenors of up to 15 years. In this respect, OTC options pose less of a challenge from a risk management perspective than do FLEX options. However, OCC believes (based on activity in the existing over-the-counter market for uncleared, bilateral options) that there may be greater open interest in OTC options with tenors exceeding 3 years as compared to FLEX options, in which open interest is more concentrated in shorter term options. In addition, it is inherent in the nature of the over-the-counter option markets that there are no market makers with affirmative duties to create liquidity by standing ready to buy and sell OTC options in response to market interest as there are in the listed options markets, including the FLEX options market.

In order to address the potentially greater open interest in longer-tenor options, OCC is proposing to supplement its existing risk management procedures by enhancing its STANS margining system by:

(i) including pricing data from daily polls of dealers in the uncleared over-the-counter market conducted by a service provider that makes such data available to anyone for a subscription fee. OCC will use such data to supplement pricing data available in the cleared OTC options market itself and in the listed options market.

(ii) introducing variations in the implied volatilities used in the modeling of all cleared options whose residual tenors are at least three years, and

(iii) introducing a valuation adjustment into its calculation of portfolio net asset value based on the aggregate sensitivity of the longer-tenor options in a portfolio to the overall level of implied volatilities at three and five years, and to the implied volatility skew.

These proposed changes are described in more detail in Item 3 above and will be the subject of a separate Advance Notice filing to be submitted by OCC in the near future. As noted above, OCC will not commence clearing of OTC options unless and until the proposed enhancements have been submitted to, and approved by, the Commission.

Any additional risk that might be presented by the absence of market-makers in OTC options can be managed by OCC and by clearing members through the use of the listed options markets, including the FLEX options markets. Although positions in OTC options are not fungible with positions in listed options, it is nevertheless possible to completely offset the risk of a position in OTC options by entering into an opposite position in FLEX options having

identical terms. The traditional listed options markets are also commonly used by dealers in uncleared over-the-counter options to hedge their positions. Accordingly, any lack of liquidity that may exist in the OTC options markets is neutralized by the ability to access the liquidity in the listed options markets.

Item 11. Exhibits

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

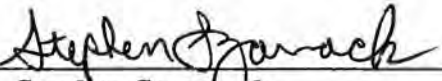
Exhibit 3 The current form of S&P short-form index license agreement

Exhibit 5 OTC Options Auction Procedures

SIGNATURES

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

THE OPTIONS CLEARING CORPORATION

By: 

Stephen Szarnack
Vice President and
Associate General Counsel

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-_____; File No. SR-OCC-2012-14)

August 30, 2012

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change and Advance Notice Relating to the Clearance and Settlement of Over-the-Counter Options

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934¹ and Rule 19b-4² notice is hereby given that on August 30, 2012, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission the proposed rule change and advance notice as described in Items I, II and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change and advance notice from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change and Advance Notice

The proposed rule change would allow OCC to provide central clearing of index options on the S&P 500 that are negotiated bilaterally in the over-the-counter market and submitted to OCC for clearance.

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

In its filing with the Commission, OCC included statements concerning the purpose of and basis for the proposed rule change and advance notice and discussed any comments it received on the proposed rule change and advance notice. The text of these statements may be

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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 such statements.

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

The purpose of this proposed rule change and advance notice is to allow OCC to provide central clearing of OTC index options on the S&P 500 Index. The proposed rule change replaces a previously proposed rule change which was withdrawn by OCC.³ OCC will clear the proposed OTC options in a manner that is highly similar to the manner in which it clears listed options, with only such modifications as are appropriate to reflect the unique characteristics of OTC options.

OTC Options

OCC has entered into a license agreement with Standard & Poor's Financial Services LLC ("S&P") that allows OCC to clear OTC options on three equity indices published by the S&P: the S&P 500 Index, the S&P MidCap 400 Index and the S&P Small Cap 600 Index. The initial OTC options to be cleared by OCC will consist of options on the S&P 500 Index. OCC may clear OTC options on other indices and on individual equity securities in the future, subject to Commission approval of one or more additional rule filings. The current rule filing defines "OTC option" and "OTC index option" generically in order to simplify future amendments to provide for additional underlying interests. OTC options will have predominantly common terms and characteristics, but also include unique terms negotiated by the parties. Transactions in OTC options will not be executed through the facilities of any

³ Securities Exchange Act Release No. 34-66090 (January 3, 2012), 77 FR 1107 (January 9, 2012) (SR-OCC-2011-19).

exchange, but will instead be entered into bilaterally and submitted to OCC for clearance through one or more providers of trade affirmation services.⁴

OTC options will be similar to exchange-traded standardized equity index options called “FLEX Options” that are currently traded on certain options exchanges.⁵ FLEX Options are exchange-traded put and call options that allow for customization of certain terms. For example, FLEX index Options traded on the Chicago Board Options Exchange have six customizable terms: (1) underlying index, (2) put or call, (3) expiration date, (4) exercise price, (5) American or European exercise style, and (6) method of calculating settlement value. OCC is the issuer and guarantor of FLEX Options and clears FLEX Options traded on multiple exchanges.

Similar to FLEX Options, OTC options will allow for customization of a limited number of variable terms with a specified range of values that may be assigned to each as agreed between the buyer and seller. Parties submitting transactions in OTC options for clearing by OCC will be able to customize six discrete terms: (1) underlying index;⁶ (2) put or call; (3) exercise price; (4) expiration date; (5) American or European exercise style; and (6) method of calculating exercise settlement value on the expiration date.⁷ The variable terms and permitted

⁴ The initial provider of the trade affirmation services in connection with the OTC options will be MarkitSERV.

⁵ Note that FINRA Rule 2360(a)(16) refers to FLEX Options as “FLEX Equity Options,” which it defines as “any options contract issued, or subject to issuance by, The Options Clearing Corporation whereby the parties to the transaction have the ability to negotiate the terms of the contract consistent with the rules of the exchange on which the options contract is traded.” OCC does not believe this definition would capture OTC options as they are not traded on any exchange. Nevertheless, as discussed below, OCC is working with FINRA to amend certain of FINRA’s rules to clarify the proper application of such rules to OTC options.

⁶ Initially, however, the S&P 500 Index will be the only permitted underlying index.

⁷ The expiration date of an OTC option must fall on a business day. The method of determining the exercise settlement value of an OTC option on its expiration date may be either the opening settlement value or the closing settlement value of the underlying index (calculated by S&P using the opening or closing price, as applicable, in the primary market of each component security of the underlying index on the specified expiration date), in each case as reported to OCC by CBOE.

values will be specified in the proposed Section 6 of Article XVII of the By-Laws. With respect to future OTC options accepted for clearing, OCC intends that such future OTC options will conform to the general variable terms and limits on the variable terms set forth in proposed Section 6 of the By-Laws, and will either amend the Interpretations and Policies thereunder to specify additional requirements for specific OTC options or publish such requirements on OCC's website.

Clearing of OTC Options

OCC proposes to clear OTC options subject to the same basic rules and procedures used for the clearance of listed index options. The proposed rules require that the counterparties to the OTC options must be eligible contract participants ("ECPs"), as defined in Section 3a(65) of the Securities Exchange Act of 1934,⁸ as amended (the "Exchange Act") and Section 1a(18) of the Commodity Exchange Act,⁹ as amended (the "CEA"). Because an OTC option will be a "security" as defined in the Exchange Act, the proposed rules also require that the transactions be cleared through a clearing member of OCC that is registered with the Commission as a broker-dealer or one of the small number of clearing members that are "non-U.S. securities firms" as defined in OCC's By-Laws. OCC is not proposing to require clearing members to meet any different financial standards for clearing OTC options. However, clearing members must be specifically approved by OCC to clear OTC options pursuant to new Interpretation and Policy .11 to Section 1 of Article V in order to assure the operational readiness of such clearing members to clear OTC options. Clearing members seeking to clear OTC options will be required to submit a business expansion request and complete an operational

⁸ 15 U.S.C. 78c(a)(65),

⁹ 7 U.S.C. 1a(18),

review. The operational review consists of an initial meeting with the clearing member's staff to evaluate the staff's experience, confirm the staff's familiarity with current OCC systems and procedures, complete an operational questionnaire, perform a high level review of the clearing member's systems and processing capabilities, and review other pertinent operational information. Successful testing of messaging capability between the clearing member, MarkitSERV and OCC is also necessary. These procedures will determine whether the firm is operationally ready to clear OTC Index Options.

Exercise of an OTC option will be settled by payment of cash by the assigned writer and to the exercising holder through OCC's cash settlement system on the business day following exercise in exactly the same manner as is the case with exercise settlement of listed index options. As in the case of listed index options, the exercise-settlement amount will be equal to the difference between the current value of the underlying interest and the exercise price of the OTC option, times the multiplier that determines the size of the OTC option. In the case of OTC index options on the S&P 500, the multiplier will be fixed at 1. The multipliers for additional OTC index options that OCC may in the future clear may be fixed at such value as OCC determines and provides for in its By-Laws and Rules.

OCC will calculate clearing margin for the OTC options using its STANS margin system on the same basis as for listed index options and will otherwise apply the same risk management practices to both OTC options and listed index options, including new risk modeling enhancements for longer-tenor options discussed below under "Risk Management Enhancement for Longer-Tenor Options." Because OCC currently clears listed options on all three of the underlying indexes on which OCC is currently licensed to clear OTC options, and because the customizable terms of these OTC options are relatively limited and the range of

values that customizable terms may be given is limited, OCC does not believe that valuation and risk management for these OTC options present challenges that are different from those faced in the listed options market. Nevertheless, as discussed further below, OCC is proposing special OTC Options Auctions to be used in the unlikely event that OCC would be unable to close out positions in OTC options of a failed clearing member through other means.

OTC options may be carried in a clearing member's firm account, in market-maker accounts or in its securities customers' account, as applicable. Although customer positions in OTC options will be carried in the securities customers' account (an omnibus account), OCC will use a "customer ID" to identify positions of individual customers based on information provided by clearing members.¹⁰ However, positions are not presently intended to be carried in individual customer sub-accounts, and positions in OTC options will be margined at OCC in the omnibus customers' account on the same basis as listed options. If a clearing member takes the other side of a transaction with its customer in an OTC option, the transaction will result in the creation of a long or short position (as applicable) in the clearing member's customers' account and the opposite short or long position in the clearing member's firm account. The positions could also be includable in the internal cross-margining account, subject to any necessary regulatory approvals.

The trade data for an OTC option trade will be entered into the system of MarkitSERV or another trade confirmation/affirmation vendor approved by OCC for this purpose (the "OTC Trade Source").¹¹ While MarkitSERV will be the only OTC Trade Source at

¹⁰ Such customer IDs are necessary in order to allow OCC to comply with certain terms of OCC's license agreement with S&P. As described further below, customer IDs will be used for other purposes as well.

¹¹ MarkitSERV, LLC is owned by Markit Group Limited, Markit Group Holdings Limited and The Depository Trust & Clearing Corporation. MarkitSERV Limited is a wholly-owned U.K. subsidiary of MarkitSERV, LLC.

launch, OCC will permit additional OTC Trade Sources in the future in response to sufficient market demand from OCC's clearing members and subject to the ability of any such OTC Trade Source to meet OCC's requirements for operational readiness and interoperability with OCC's systems, as well as requirements with respect to relevant business experience and reputation, adequate personnel and expertise, financial qualification and such other factors as OCC deems relevant. OCC will receive confirmed trades from the OTC Trade Source. It will be permissible for parties to submit trades for clearance that were entered into bilaterally at any time in the past, provided that the eligibility for clearance will be determined as of the date the trade is submitted to OCC for clearance.¹² The OTC Trade Source will process the trade and submit it as a confirmed trade to OCC for clearing. If the trade meets OCC's validation requirements, OCC will so notify the OTC Trade Source, which will notify the submitting parties. Customers of clearing members may have direct access to the OTC Trade Source for purposes of entering or affirming trade data and receiving communications regarding the status of transactions, in which case mechanisms will be put in place for a clearing member to authorize a customer to enter a trade for the clearing member's customers' account or for the clearing member to affirm a trade once entered.

In order for a clearing member to be approved for clearing OTC options, the clearing member must enter into a standard agreement with MarkitSERV (or another OTC Trade Source with which the clearing member intends to enter trade data, if and when OCC enters into

MarkitSERV, LLC and MarkitSERV Limited (collectively, "MarkitSERV") provide derivatives transaction processing, electronic confirmation, portfolio reconciliation services, and other related services for firms that conduct business in the over-the-counter derivatives markets through a variety of electronic systems, including the MarkitWire system. MarkitWire, owned by MarkitSERV Limited, is an OTC derivatives electronic confirmation/affirmation service offered by MarkitSERV as part of its post-trade processing suite of products. The role of MarkitSERV and MarkitWire in OCC's clearing of OTC options is described in further detail below.

¹² OCC's license agreement with S&P imposes certain requirements relating to minimum time remaining to expiration of an OTC option.

arrangements with other OTC Trade Sources). At launch, OTC options will not be subject to the same clearing member trade assignment rules and procedures through which exchange-traded options can be cleared by a clearing member other than the executing clearing member. This functionality may be added at a later date. OCC and MarkitSERV will adopt procedures to permit a customer that has an account with Clearing Member A ("CM A") to enter into an OTC option transaction with Clearing Member B ("CM B") and have the position included in its account at CM A and cleared in CM A's customers' account at OCC.

OTC options will be fungible with each other to the extent that there are OTC options in the system with identical terms. However, OCC will not treat OTC options as fungible with index options listed on any exchange, even if an OTC option has terms identical to the terms of the exchange-listed option.

Clearing members that carry customer positions in cleared OTC options will be subject to all OCC rules governing OCC-cleared options generally, as well as all applicable rules of the Commission and of any self-regulatory organization, including the Financial Industry Regulatory Authority ("FINRA"), of which they are a member. Section 8 of Article III of OCC's By-Laws provides that, subject to the By-Laws and Rules, "the Board of Directors may suspend Clearing Members and may prescribe and impose penalties for the violation of the By-Laws or the Rules of the Corporation, and it may, by Rule or otherwise, establish all disciplinary procedures applicable to Clearing Members and their partners, officers, directors and employees." As a condition to admission, Section 3(c) of Article V of the By-Laws provides that a clearing member must agree, among other things, to "pay such fines as may be imposed on it in accordance with the By-Laws and Rules." Rule 305 permits OCC to impose restrictions on the clearing activities of a clearing member if it finds that the financial or operational condition of

the clearing member makes it necessary or advisable to do so for the protection of OCC, other clearing members, or the general public. Rule 1201(a) provides that OCC “may censure, suspend, expel or limit the activities, functions or operations of any Clearing Member for any violation of the By-Laws and Rules or its agreements with the Corporation.” In addition to, or in lieu of, such actions, OCC is permitted under the same paragraph to impose fines. Rule 1202(b) establishes procedures for taking any such disciplinary actions. The foregoing provisions are sufficient to permit OCC to fine or otherwise discipline a clearing member that fails to abide by OCC’s By-Laws and Rules applicable to OTC options, or to prohibit such clearing member from continuing to clear such options.

Regulatory Status of the OTC Options

An OTC option will be a “security” as defined in both the Securities Act of 1933, as amended (the “Securities Act”) and, as noted above, the Exchange Act. OCC will be the “issuer” of the OTC options. The OTC options will be neither “swaps” nor “security-based swaps” for purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”).¹³

Most of OCC’s clearing members are members of FINRA and subject to FINRA’s rules, which have different provisions for “listed” and “OTC options” and contain various definitions distinguishing between the two. In some cases, OTC options would fall into neither category under FINRA’s definitions and in other cases, they would fall within what OCC perceives to be the wrong category. FINRA and OCC are working together to implement

¹³ Section 1a(47)(A)(i) of CEA, 7 U.S.C. 1a(47)(A)(i), as added by Section 721(a)(21) of Dodd-Frank, defines “swaps” broadly to include options on indices. However, Section 1a(47)(B)(iii) of the CEA, 7 U.S.C. 1a(47)(B)(iii), excludes from the “swap” definition any option on any index of securities that is subject to the Securities Act and the Exchange Act. A contract that is excluded from the definition of a “swap” under Section 1a(47)(B) of the CEA, 7 U.S.C. 1a(47)(B) (other than Section 1a(47)(B)(x), 7 U.S.C. 1a(47)(B)(x)) is not a “security-based swap” for purposes of Section 3a(68) of the Exchange Act, 15 U.S.C. 78c(a)(68).

appropriate amendments to FINRA rules to clarify the proper application of such rules to cleared OTC options.

MarkitSERV Trade Submission Mechanics

MarkitSERV provides an interface to OCC that allows OCC to receive messages containing details of transactions in OTC options submitted for clearing by clearing members with access to MarketWire and also allows OCC to transmit messages to MarkitWire participants identifying the status of submitted transactions. MarkitWire applications use product-specific templates to simplify deal entry and negotiations. The templates specify the data required for a given product and also the business validation rules for each field. MarkitSERV has included OCC's validation requirements for OTC options in its trade templates.

The trade data for each OTC option transaction must be entered into MarkitWire. MarkitSERV will use a "confirmation/affirmation" procedure in which one party to the trade enters the trade data to the MarkitWire platform, which issues a confirmation to the counterparty to be affirmed, rejected or requested to be revised. If the trade details are confirmed, the trade will then be submitted to OCC for clearance and MarkitSERV will affirm such submission to both parties. OCC then validates the trade information for compliance with applicable requirements, such as the identification of an account of an eligible clearing member in which each side of the trade will be cleared, that the variable terms are within permissible ranges, and that minimum size requirements under OCC's license agreement with S&P are met. This validation will be completed by OCC immediately upon submission. OCC's clearing system will automatically accept the trade if it passes the validation process and will otherwise reject

it.¹⁴ A trade that is rejected by OCC may be corrected and submitted as a new transaction. Clearing members and customers with access to MarkitSERV will be able to determine whether a trade has been accepted or rejected both through MarkitSERV and, in the case of clearing members, through their interface with OCC's clearing system.

MarkitSERV's Regulatory Status¹⁵

MarkitSERV is not registered as a clearing agency under the Exchange Act, and the Commission staff has asked OCC to consider whether MarkitSERV would be required to so register in order to provide the proposed services to the OTC options market. OCC believes that no such registration is necessary based upon relevant interpretive guidance issued by the Commission.

Section 3(a)(23)(A) of the Exchange Act¹⁶ defines a "clearing agency" broadly. The definition includes, in relevant part, "any person who . . . provides facilities for comparison of data respecting the terms of settlement of securities transactions[.]" In 1998, the Commission issued a release entitled "Confirmation and Affirmation of Securities Trades; Matching" (the "Matching Release").¹⁷ In the Matching Release, the Commission published "its interpretation that a 'matching' service that compares securities trade information from a broker-dealer and the broker-dealer's customer is a clearing agency function." The Matching Release distinguishes between such a matching service and a "confirmation/affirmation service" where the "vendor

¹⁴ Once accepted, a trade is guaranteed by OCC. Note, however, that OTC options for which the premium payment date communicated by MarkitSERV to OCC is prior to the business day on which the OTC option is submitted to OCC for clearing (referred to as a "Backloaded OTC Option") will not be accepted and guaranteed until the selling clearing member has met its initial morning cash settlement obligations to OCC on the following business day.

¹⁵ MarkitSERV offers different services in different markets, and this discussion is addressed only to the "confirmation/affirmation" procedure to be used in submitting trades to OCC.

¹⁶ 15 U.S.C. 78c(a)(23)(A),

¹⁷ Securities Exchange Act Release No. 34-39829 (April 13, 1998), 63 FR 17943 (April 13, 1998).

intermediary will only transmit information between the parties to a trade, and the parties will confirm and affirm the accuracy of the information.” The Commission noted that “matching” constitutes the “comparison of data respecting the terms of settlement of securities transactions” and that such services therefore trigger status as a clearing agency, while confirmation/affirmation services would not, by themselves, constitute such a data comparison. The Commission concluded in the Matching Release that “an intermediary that captures trade information from a buyer and a seller of securities and performs an independent reconciliation or matching of that information is providing facilities for the comparison of data within the scope of Exchange Act Section 3(a)(23).” The Commission stated that “matching” is “so closely tied to the clearance and settlement process that it is different not only in degree but also different in kind from the . . . confirmation and affirmation process.” The Matching Release goes on to state: “a vendor that provides confirmation/affirmation services only will exchange messages between a broker-dealer and its institutional customer. The broker-dealer and its institutional customer will compare the trade information contained in those messages, and the institution itself will issue the affirmed confirmation.” This is precisely what occurs when a counterparty to a trade affirms the trade data through MarkitSERV and requests submission to OCC for clearance. MarkitSERV transmits messages only; it does not “compare” or “match” trade data submitted by two parties.

The “confirmation/affirmation” functionality (as described above) to be provided by MarkitSERV (through MarkitWire) with respect to OTC options is functionally identical to the confirmation/affirmation service described in the Matching Release and OCC believes such service would not be a “matching” service within the meaning of the release. OCC believes that MarkitSERV will not be a “clearing agency” with respect to the services to be provided in

connection with OTC options. The confirmation/affirmation service described in the Matching Release referred “to the transmission of messages among broker-dealers, institutional investors, and custodian banks regarding the terms of a trade executed for the institutional investor.” MarkitWire’s confirmation/affirmation process will allow for the transmission of messages among OCC’s clearing members (most of which are registered broker-dealers), their customers (all of whom will be ECPs and will therefore be large and financially sophisticated market participants) and OCC, which is itself registered and subject to the Commission’s oversight as a clearing agency.

By contrast, the “matching” services contemplated in the Matching Release would involve “the process whereby an intermediary compares the broker dealer’s trade data submission . . . with the institution’s allocation instructions . . . to determine whether the two descriptions of the trade agree.” MarkitWire performs no such comparison. Under the confirmation/affirmation procedure, trade data is entered into MarkitWire by one party and such data is made available to the counterparty to be affirmed, rejected or requested to be revised. MarkitWire merely facilitates the transfer of information between the parties sufficient to allow the comparison to be made. A binding transaction (*i.e.*, an “affirmed confirmation” in the language of the Matching Release) is not produced through any action of MarkitSERV, but is instead created by the completion, by the counterparty, of an affirmation of the trade data entered by the first party. MarkitWire provides no “independent reconciliation or matching” of trade data. Rather MarkitWire is providing essentially a messaging service among OCC and the parties to trades in OTC Options. The Matching Release is clear as to the distinction between a matching service and a confirmation/affirmation service, and OCC believes that there is no

ambiguity that the services to be provided by MarkitWire with respect to OTC options fall into the latter, rather than the former, category.

Risk Management Enhancements for Longer-Tenor Options

Although OCC's license agreement with S&P allows OCC to clear OTC options with tenors of up to fifteen years, OCC has elected at this time to clear only OTC options on the S&P 500 index with tenors of up to five years. However, OCC currently clears FLEX Options on the S&P 500 with tenors of up to 15 years. While OCC believes that its current risk management practices are adequate for current clearing activity, OCC is in the process of implementing risk modeling enhancements with respect to longer-tenor options, including OTC options. The enhancements are part of OCC's ongoing efforts to test and improve its risk management operations with respect to all longer-tenor options that OCC currently clears. These procedures will be submitted for review in a separate "advance notice" filing and OCC will not commence clearing of OTC options until such procedures have been approved and implemented.

The proposed enhancements are as follows:

- First, OCC will introduce indicative over-the-counter quotations into the daily dataset of prices used to risk manage OCC-cleared products. These quotations will be obtained from a service provider that will collect OTC dealer polling information on a daily basis and provide such data to OCC.
- Second, OCC will introduce variations in the implied volatilities used in the modeling of all cleared options whose residual tenors are at least three years. To date, OCC's margin methodology has assumed that implied volatilities of option contracts are static over the two-day risk horizon. While OCC's backtesting has identified few exceedances related to implied volatility

shocks, such shocks could occur and taking them into account in OCC's margin model will allow more robust risk management. OCC proposes to achieve this result by incorporating into the risk factors included in OCC's models time series of proportional changes in implied volatilities for a range of representative volatilities.

- Third, OCC will introduce a valuation adjustment into its calculation of portfolio net asset value. This adjustment will be based on the aggregate sensitivity of the longer-tenor options in a portfolio to the overall level of implied volatilities at three and five years, and to the implied volatility skew.

A review of individual S&P 500 Index put and call options positions that are in the money by varying amounts and have expiration dates between four and nine years out indicates that the inclusion of modeled implied volatilities tends to result in less margin being held against short call positions and more being held against short put positions. These results are consistent with what would be expected given the strong negative correlation that exists between changes in implied volatility and market returns. On average, OCC observed a decrease in the margin requirement of approximately 24% on the nine call options tested and a 63% increase associated with the nine put options.

Proposed By-Law and Rule Changes

The specific proposed changes to OCC's By-Laws and Rules to provide for the clearing of OTC options relate primarily to: (i) specification of customizable terms; (ii) procedures for submission and acceptance of trades for clearance; and (iii) specification of criteria for eligibility of clearing members to clear transactions in OTC options and limitation of the types of customers for whom clearing members may effect transactions in OTC options.

Otherwise, the currently proposed OTC options will be cleared and settled under the same provisions applicable to clearance of listed index options. Many of the proposed amendments are self-explanatory, and OCC has therefore attempted to confine the following discussion to a broad overview with specific explanation only where the reasons for the change may be less obvious.

Article I of the By-Laws contains defined terms used throughout the By-Laws and Rules. OCC proposes to modify certain existing definitions and include certain new definitions in order to incorporate OTC options into existing rules and facilitate the creation of new provisions unique to OTC options. Throughout the By-Laws and Rules, OCC proposes to replace the term “Exchange transaction,” which is currently defined in Article I, in relevant part, as “a transaction on or through the facilities of an Exchange for the purchase, writing or sale of a cleared contract” with the term “confirmed trade” so as to make the relevant portions of the By-Laws and Rules applicable to transactions in OTC options as well as listed options, without causing confusion about the role of the OTC Trade Source in OCC’s clearing of OTC options. “Confirmed trade” is proposed to be defined in Article I to include transactions “effected on or through the facilities of an exchange” or “affirmed through the facilities of an OTC Trade Source” in order to include transactions in both listed options and OTC options. The current definition of “confirmed trade” in Rule 101 is proposed to be deleted as unnecessary given the new definition. Much of the length of this rule filing is attributable to the fact that the term “Exchange transaction” is used so many places in the rules. OCC has entered into agreements in the past which reference the term “Exchange transaction” or “exchange transaction.” OCC is also proposing to add an Interpretation and Policy to the new definition of “confirmed trade” in

order to avoid any ambiguity concerning how such terms should be interpreted in any such agreement.

OCC proposes to add a new Interpretation and Policy .11 to Section 1 of Article V of the By-Laws, providing the additional criteria that must be met by a clearing member in order to clear OTC index options. Among these new criteria are that clearing members seeking to clear OTC index options on underlying indices published by Standard & Poor's Financial Services LLC ("S&P") must execute and maintain in effect a short-form license agreement in such form as specified from time to time by S&P. The current form of S&P short-form index license agreement is attached hereto as Exhibit 3.

The Interpretations and Policies under Section 1, Article VI allow clearing members to adjust their positions with OCC for certain enumerated reasons. OCC proposes to amend the Interpretations and Policies to clarify that adjustment of positions in OTC options will be effected through a manual process (as opposed to the electronic process available to post-trade adjustments in listed options), to the extent permitted by OCC. For the same reason, OCC is proposing to amend Rule 403 to prohibit clearing member trade assignment ("CMTA") transactions in OTC options. Trade "give-ups" that are effected through the CMTA process in the case of listed options will, in the case of OTC options, be effected through MarkitSERV before the trades are submitted to OCC for clearing.

Article XVII of the By-Laws governs index options in general and OCC is proposing amendments to Article XVII in order to set forth the terms applicable to the initial OTC options proposed to be cleared by OCC — options on the S&P 500 Index — and to differentiate OTC index options from other index options cleared by OCC. For example, certain amendments to the definitions are necessary because OTC options will be permitted to have a

much wider range of expiration dates than exchange-traded options (other than FLEX Options). Additional definitional amendments ensure that OTC index options will constitute a separate class of options from other cash-settled index options even if both index options have the same terms and cover the same underlying interest.

Section 3 of Article XVII provides for adjustment of the terms of outstanding index options as necessary to reflect possible changes in the underlying index — such as those creating a discontinuity in the level of the index — that could theoretically make an adjustment necessary to protect the legitimate expectations of holders and writers of options on the index. Pursuant to paragraph (g) of Section 3, most but not all such adjustments would be made, in the case of listed index options, by an adjustment panel consisting of representatives of the exchanges on which the options are traded. In the case of OTC options, any such adjustments will be made by OCC in its sole discretion. However, in exercising that discretion, OCC may take into consideration adjustment made by the adjustment panel with respect to exchange-traded options covering the same underlying index.¹⁸

OCC proposes to add a new Section 6 to Article XVII to set forth certain provisions unique to OTC index options, including the variable terms allowed for OTC index options and the general limitations on such variable terms. In general, all OTC index options must conform to the terms and limitations set forth in Section 6, and additional specific requirements applicable to specific OTC index options will either be set forth in the Interpretations and Policies under Section 6 or published separately on OCC's website. Section 6 also makes clear that although OTC index options are not fungible with exchange-traded index

¹⁸Because index options, unlike options on individual stocks, rarely, if ever, require adjustments, allocation of the adjustment authority may have little practical significance.

options, OTC index options of the same series (*i.e.*, options having identical terms) will be fungible with each other. In addition to the terms and limitations applicable to OTC index options, Section 6 will establish that clearing members will be deemed to have made a number of representations and warranties in connection with their activities in OTC options each time they affirm a confirmed trade entered into an OTC Trade Source.

OCC has submitted a rulemaking petition to the Commission¹⁹ seeking an amendment to Commission Rule 238²⁰ that would exempt the OTC Options from most provisions of the Securities Act. Unless another exemption from the registration requirements of the Securities Act is available, OCC intends to rely upon Rule 506 of Regulation D²¹ under the Securities Act, which is a safe harbor under the Securities Act exemption in Section 4(a)(2)²² for offerings by an issuer not involving a public offering. OCC intends to satisfy the conditions of Rule 506 of Regulation D as in effect at the time OCC relies upon the safe harbor. Participants in the existing markets for OTC equity options offered and sold in the United States commonly rely on the private offering exemption under these provisions and such reliance is therefore consistent with existing practice. OTC Options will be available for purchase only by highly sophisticated investors that are both “eligible contract participants,” as defined in Section 3a(65) of the Exchange Act,²³ and “accredited investors,” as defined in Rule 501(a) under Regulation

¹⁹ See SEC File No. 4-644 (Submitted January 13, 2012), available at <http://www.sec.gov/rules/petitions/2012/petn4-644.pdf>.

²⁰ 17 CFR 230.238.

²¹ 17 CFR 230.506.

²² 15 U.S.C. 77d(a)(2).

²³ 15 U.S.C. 77c(a)(65).

D.²⁴ Section 6(f) of Article XVII includes representations of clearing members necessary to ensure that there is no general solicitation or general advertising in connection with the offer or sale of the OTC Options until such time as OCC notifies clearing members that such restriction no longer applies.

Chapter IV of the Rules sets forth the requirements for reporting of confirmed trades to OCC, and Rule 401 thereunder governs reporting of transactions in listed options by participant Exchanges. OCC is proposing to add new Rule 404 to govern the details of reporting of confirmed trades in OTC options by an OTC Trade Source.

As discussed above, positions in OTC options will generally be margined in the same manner as positions in listed options using STANS and pursuant to Chapter VI of the Rules. However, OCC proposes to amend Rule 611 to establish different procedures for the segregation of long positions in OTC options for margining purposes. Long positions in listed options are held in a clearing member's customers' account or firm non-lien account and by default are deemed to be "segregated," meaning that they are not subject to OCC's lien and are given no collateral value when determining the margin requirement in the account. Such positions may be unsegregated only when a clearing member instructs OCC to unsegregate a long position and represents to OCC that the long position is part of a spread transaction carried for a single customer whose margin requirement on the corresponding short position has been reduced in recognition of the spread. OCC will then unsegregate the long position and so reduce OCC's margin requirement. However, in case of long positions in OTC options that are carried in a clearing member's customers' account and for which OCC has received a customer ID, OCC

²⁴ 17 CFR 230.501.

proposes that it will automatically unsegregate such long positions if OCC identifies a qualifying short position in OTC options carried under the same customer ID. Clearing members will not be required to give an affirmative instruction to OCC to unsegregate a long position in OTC options or make a separate representation regarding the spread transaction. Instead, by carrying a qualifying spread position in a customer account, clearing members are deemed to have represented to OCC that the customer's margin has been reduced in recognition of the spread. Based on discussion with the clearing members, it is OCC's understanding that, in practice, broker-dealers reduce customers' margin requirements to reflect spread positions. Therefore, OCC believes that automatic recognition of such spreads by OCC together with the deemed representation will greatly increase operational efficiency while providing equal assurance that long positions in OTC options will be unsegregated only if an identified customer will receive the benefit of the reduced margin required for spread transactions.

Rule 1001 sets forth the amount of the contribution that each clearing member is required to make to the clearing fund. OCC proposes to amend Rule 1001(c) so that, for purposes of calculating the daily average number of cleared contracts held by a clearing member in open positions with OCC during a calendar month (which number is used in turn to determine the clearing member's contribution to the clearing fund), open positions in OTC options will be adjusted as needed to account for any differences between the multiplier or unit of trading with respect to OTC options relative to non-OTC options covering the same underlying index or interest so that OTC options and non-OTC options are given comparable weight in the computation.²⁵

²⁵ For example, the index multiplier applicable to OTC index options on the S&P 500 Index will be fixed at 1. In comparison, the index multiplier applicable to listed index options is 100.

In general, the rules in Chapter XI governing the suspension of a clearing member will apply equally to clearing members that transact in OTC options. Rule 1104 provides broad authority for OCC to liquidate a suspended clearing member's margin and clearing fund deposits "in the most orderly manner practicable." Rule 1106 provides similarly worded authority to close out open positions in options and certain other cleared contacts carried by a suspended clearing member. In 2011, the Commission approved an OCC rule change providing OCC the express authority to use a private auction as one of the means by which OCC may close out open positions and liquidate margin and clearing fund deposits of a suspended clearing member.²⁶ OCC anticipates it will use this auction process for OTC options as well. As an additional tool to ensure its ability to close out positions in OTC options promptly, OCC is proposing to amend Rule 1106 to provide for an alternative auction procedure specifically applicable only to OTC index options and related positions hedging, or hedged by, OTC index options (an "OTC Options Auction"). An OTC Options Auction would be used only in unusual circumstances where OCC determines it is not feasible to close out open positions in OTC index options through the other means provided for in OCC's Rules and By-Laws.²⁷ The amendments to Rule 1106 summarize the OTC Options Auction procedures and incorporate by reference the detailed procedures contained in a document entitled "OTC Options Auction Procedures," which will be posted on the Corporation's website and otherwise made available to clearing members

²⁶ See Securities Exchange Act Release No. 34-65654 (October 28, 2011), 76 FR 68238 (November 3, 2011) (SR-OCC-2011-08). OCC subsequently filed a rule change, currently pending Commission approval, providing detailed procedures for the conduct of such an auction. See Securities Exchange Act Release No. 34-67443 (July 16, 2012), 77 FR 42784 (July 20, 2012) (SR-OCC-2012-11).

²⁷ OCC anticipates that these procedures would be applicable to other OTC derivatives that may be cleared by OCC in the future. However, OCC has limited the currently proposed rule to OTC index options, and will amend it as and if appropriate to apply to other over-the-counter products that OCC may propose to clear in the future.

upon request of OCC. A copy of the OTC Options Auction Procedures is attached hereto as Exhibit 5.

Rule 1106(e)(2)(C) clarifies that, in the event that the liquidation of a clearing member results in a deficiency that would otherwise result in a proportionate charge against the clearing fund contributions of other clearing members, each OTC Index Option Member (as defined below) that failed to purchase or assume its share of an auction portfolio will be the first to absorb the deficiency, through a “Priority Charge” against such clearing members’ clearing fund contributions. The Priority Charge is a “first loss” mechanism, and is not intended to increase a clearing member’s total maximum exposure to OCC.

Under the OTC Options Auction procedures, all clearing members authorized to clear transactions in OTC index options (“OTC Index Option Members”), other than the defaulting clearing member, will be required to participate in the OTC Options Auction by submitting competitive bids for all or a portion of the defaulting clearing member’s OTC index option portfolio. Each such participant will be subject to a minimum participation level based on the participant’s proportionate share of the total “risk margin” requirement posted by all OTC Index Options Members in the previous month for all positions (not limited to OTC option positions) held in accounts eligible to hold OTC options positions (“OTC Eligible Accounts”), after removing the defaulting clearing member.²⁸ This method of calculating the minimum participation level in the OTC Options Auction results in all OTC Index Option Members being required to participate in the OTC Options Auction based on their clearing activity related to all positions in OTC Eligible Accounts. Required participation ensures that the OTC Options

²⁸ This minimum participation level will be multiplied by 1.15 to calculate each participant’s minimum bid size, such that the sum of all participants’ bids will equal 115% of the auction portfolio, in order to increase the likelihood that the entire auction portfolio will be allocated to participants.

Auction will have sufficient participants authorized to clear transactions in OTC index options and that the most active clearing members in OTC index options will submit bids for the largest percentage of the auction portfolio, increasing the likelihood of the acquisition of OTC options positions by clearing members with appropriate financial strength, risk management capabilities and trading expertise. Each participant may submit bids at varying quantities and varying prices, so long as the participant's bids equal or exceed its minimum participation level. A participant may use bids from non-OTC Index Options Members and non-clearing members in order to meet its minimum participation level, subject to certain Corporation requirements including that it guarantee the performance of such third parties. Each bid will indicate what percentage of the auction portfolio the participant is bidding on and the amount of the bid. Bids will be stated in terms of a price for the entire auction portfolio, and may be either positive or negative. (Negative bids imply an auction portfolio that has a negative net asset value and indicate how much the Corporation would be required to pay the participant to assume the relevant percentage of the auction portfolio.) The Corporation will rank the submitted bids from best to worst and the auction portfolio will be allocated among the bidding participants accordingly until the auction portfolio is exhausted. The bid price that is sufficient to clear the entire auction portfolio will become the single price to be used for all winning bids, even if a participant's stated bid was better.

In order to provide a strong incentive to ensure competitive bidding by the OTC Index Option Members required to participate in an OTC Options Auction, OTC Index Options Members who fail to win their minimum participation in the auction will be subject to a potential priority charge against its clearing fund contribution. If the cost of liquidating a suspended clearing member's positions exhausts the clearing member's margin and clearing fund

contribution and any other assets of the suspended clearing member available to OCC, then OCC, pursuant to Section 5 of Article VIII of the By-Laws, would ordinarily withdraw the amount of the deficiency from the clearing fund and charge it on a proportionate basis against all other clearing members' computed contributions as fixed at the time. When an OTC Options Auction has been held in respect of a suspended OTC Index Options Member, however, some or all of any such remaining loss would be assessed first against the clearing fund contributions of any OTC Options Auction participant(s) whose bids are insufficiently competitive to be allocated a portion of the auction portfolio equal to such participant's minimum required participation. This priority charge would be made regardless of the reason for the shortfall—*i.e.*, whether or not the loss resulted from the closing out of OTC options positions. The priority charge would be calculated based on an "assessment ratio," which is formulated to provide incentive to all OTC Options Auction participants to participate to their full minimum participation level in the auction. The method of calculating the assessment ratio is such that if the net asset value of the auction portfolio is zero the assessment ratio will also be zero and no priority charge will be made. As the absolute net asset value of the auction portfolio (whether positive or negative) increases, the assessment ratio also increases, all other factors being equal. If all OTC Options Auction participants submit bids such that each receives an allocation of OTC options positions equal to its minimum participation level, no priority charge will be made regardless of whether or not there is a liquidation shortfall. If a liquidation shortfall remains after any priority charges, or if no priority charges were required, the Corporation will then make a proportionate charge against the clearing fund contributions of all clearing members, including those that participated in the OTC Options Auction, in the usual manner pursuant to Section 5 of Article VIII of OCC's By-Laws.

In order to protect the estate of the suspended clearing member, OCC reserves some discretion in supervising the auction. In the event that the bid price that clears the entire auction portfolio is determined by OCC to be an outlier bid, OCC may choose as the winning bid a price that clears at least 80% of the auction portfolio. The remaining auction portfolio will then be re-auctioned as described above.

OCC anticipates that the likelihood of having to use this alternative auction is small. Nevertheless, in view of the fact that positions in OTC index options are expected to be large and that there may be no active trading market in options with terms precisely identical to the terms of the OTC index options in question, OCC believes that this is an appropriate failsafe provision. It should be noted that the Chicago Mercantile Exchange Inc. ("CME") has rules allowing its clearing house and certain CME committees to administer an auction process to liquidate positions in interest rate swaps ("IRS") in the event of a default of a CME clearing member authorized to submit IRS for clearing (an "IRS Member").²⁹ Although the financial safeguards supporting IRS clearing, including its "guaranty fund," and the IRS auction process are different from OCC's clearing fund and OTC Options Auction in that, among other things, there is a separate guaranty fund for IRS, the IRS auction shares certain similarities with the OTC Options Auction. In particular, the IRS auction process requires mandatory participation of IRS clearing members with open interest in a position being auctioned and, in order to provide incentive for IRS Members to submit quality bids in an IRS auction, provides that in the event there is a loss to CME's clearing house associated with an IRS Member's default, IRS Members that do not submit quality bids in an IRS auction are subject to having their IRS guaranty fund

²⁹ See CME Rules 8G14, 8G25 and 8G802.B. See also Commodity Futures Trading Commission Rule Change Submission No. 12-061RR of CME, the Board of Trade of the City of Chicago Inc. and the New York Mercantile Exchange, available at: <http://www.cmegroup.com/market-regulation/files/12-061rr.pdf>

deposit assessed before assessments are made against other IRS clearing members' guaranty fund deposits. In its original rule filing, OCC had proposed a different failsafe solution whereby OCC could terminate open positions of a suspended clearing member by setting a close-out value that non-defaulting clearing members holding the opposite side of the suspended clearing member's positions would be required to accept or pay in settlement of the terminated positions. However, clearing members objected to that proposed method and have advocated the auction procedures proposed here in lieu of the early termination proposal.³⁰ Clearing members in an OTC advisory group were active in designing the OTC Options Auction procedures, including the priority charges.

Impact of Clearing OTC Options on Other OCC-Cleared Products

Cleared OTC options will not be fungible with listed options. However, an OTC option may have economic characteristics that are substantially similar or identical to the characteristics of options in series of listed options that OCC clears. While it is possible that in any given instance a market participant may elect to enter into an OTC option in lieu of an economically similar listed product, OCC does not believe that its clearing of OTC options will adversely affect the efficiency or liquidity of the listed markets. The OTC options markets currently exist to accommodate a variety of commercial and other needs of market participants, including the ability to customize the terms of transactions. While the availability of an OCC guarantee for OTC transactions in which the parties would otherwise be exposed to each others' creditworthiness may cause transactions that currently occur in the non-cleared OTC markets to migrate to the cleared-OTC markets, OCC does not believe it will cause significant migration

³⁰ See comment letter from Alessandro Cocco, Managing Director of J.P. Morgan Clearing Corporation and J.P. Morgan Securities LLC, to Ms. Elizabeth M. Murphy, Secretary, Securities and Exchange Commission (January 30, 2012), available at <http://www.sec.gov/comments/sr-occ-2011-19/occ201119-2.pdf>.

from the listed markets to the cleared OTC markets. The limitation of the OTC options markets to ECPs as well as the significant minimum transaction size and tenor requirements that are applicable to certain transactions in the currently proposed OTC options under the S&P License Agreement will limit the use of cleared OTC options and should help to ensure that there is no substantial migration from the listed markets to the OTC markets for this product. The existing bilateral OTC options markets have existed for years alongside the listed options markets, and OCC believes that dealers in such bilateral options often use the listed markets to hedge positions taken in such bilateral options and other OTC derivatives.

Notice of Launch Date

Following approval of this rule change by the Commission, OCC expects to provide notice to its clearing members of the date on which it intends to implement this rule change and begin clearing OTC options.

* * *

The proposed changes to OCC's By-Laws are consistent with the purposes and requirements of Section 17A of the Exchange Act³¹ because they are designed to permit OCC to clear OTC options subject to the same basic rules, procedures and risk management practices that have been used successfully by OCC in clearing transactions in listed options. OCC believes that clearance and settlement of OTC options pursuant to this rule filing is fully consistent with OCC's obligations with respect to the prompt and accurate clearance and settlement of securities transactions and the protection of securities investors and the public interest. The proposed rule change is not inconsistent with any existing rule of OCC.

³¹ 15 U.S.C. 78q-1.

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

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

(C) **Clearing Agency's Statement on Comments on the Proposed Rule Change and Advance Notice 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 advance notice, and, except as discussed below, none have been received. OCC has been actively engaged with a number of clearing members that have expressed an interest in clearing OTC Options. The following are the only substantive written comments that were received, and they have been addressed, in the manner indicated:

- OCC received a written comment that the role of the Default Management Advisory Committee, as described in the OTC Options Auction procedures attached as Exhibit 5 to this rule filing, should be clarified. OCC has revised the procedures to clarify that the Default Management Advisory Committee will be a standing committee and will be formed from the inception of OCC's clearing of OTC Options. It will not be an *ad hoc* committee formed at the time of a default.
- OCC received a written comment asking that the Membership/Risk Committee have a role in setting exercise settlement values with respect to OTC index options in unusual circumstances pursuant to Section 4(a)(2) of Article XVII of the ByLaws. OCC has revised the rules to provide that OCC will consult with that committee when appropriate in setting exercise settlement values pursuant to Section 4(a)(2).

- OCC received a written comment asking for limitations on the indemnification of OCC by clearing members under Section 6(f) of Article XVII of the ByLaws. In response to this comment OCC has added an exclusion from the indemnity for claims, liabilities, or expenses that result primarily from OCC's gross negligence or willful misconduct or from OCC conduct that causes the offer or sale of the OTC Options to become subject to the registration provisions of Section 5 of the Securities Act.³²

III. Date of Effectiveness of the Proposed Rule Change and Advance Notice 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 such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

The clearing agency shall post notice on its website of any clearing requirement that is implemented.

The proposed change may be implemented if the Commission does not object to the proposed change within 60 days of the later of (i) the date that the proposed change was filed with the Commission or (ii) the date that any additional information requested by the

³² 15 U.S.C. 77e.

Commission is received. The clearing agency shall not implement the proposed change if the Commission has any objection to the proposed change.

The Commission may extend period for review by an additional 60 days if the proposed change raises novel or complex issues, subject to the Commission or the Board of Governors of the Federal Reserve System providing the clearing agency with prompt written notice of the extension. A proposed change may be implemented in less than 60 days from the date the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the proposed change and authorizes the clearing agency to implement the proposed change on an earlier date, subject to any conditions imposed by the Commission.

The clearing agency shall post notice on its website of proposed changes that are Implemented.

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

IV. Solicitation of Comments

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

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>);
- or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-OCC-

2012-14 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2012-14. 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 and advance notice that are filed with the Commission, and all written communications relating to the proposed rule change and advance notice between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at <http://www.optionsclearing.com/about/publications/bylaws.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 Number SR-OCC-2012-14 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.³³

Kevin M. O'Neill
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: _____

³³ 17 CFR 200.30-3(a)(12).

EXHIBIT 3

Form of Short-form Index License (S&P 500 Index)

INDEX LICENSE AGREEMENT

This **S&P INDEX LICENSE AGREEMENT** ("Agreement") is entered into as of the Effective Date (as set forth below), by and between Standard & Poor's Financial Services LLC, a limited liability company organized under the laws of the state of Delaware ("S&P") whose principal office is located at 55 Water Street, New York, New York 10041; and

LICENSEE NAME: _____ ("Licensee")

STREET ADDRESS: _____

CITY, STATE, ZIP CODE: _____

TYPE OF ENTITY/PLACE OF FORMATION: _____

EFFECTIVE DATE: _____

1. Subject to the terms and conditions of this Agreement, S&P hereby grants to Licensee a royalty-free, non-exclusive, limited and nontransferable license to (i) use the S&P 500 Index as the sole underlying interest of options contracts that are traded over-the-counter and cleared by a third party clearing agency (referred to herein as "Product") to be issued, entered into, written, sold and/or purchased by Licensee and (ii) use and refer to the trademarks "S&P", "Standard & Poor's", "Standard & Poor's 500" and "S&P 500" (referred to herein as the "S&P Marks" in connection with the distribution, marketing and promotion of the Product and in connection with making such disclosure about the Product as Licensee deems necessary or desirable under any applicable laws, rules, regulations or provisions of this Agreement, but, in each case, only to the extent necessary to indicate the source of the S&P 500 Index. Any rights not expressly granted herein are hereby reserved by S&P.

2. TERM AND TERMINATION.

A. In the event of any breach of the material terms or conditions of this Agreement by either party, the other party may terminate this Agreement by giving thirty (30) days prior written notice thereof; provided, however, that such termination shall not take effect if the party in breach cures or corrects the breach within such notice period.

B. Either party may terminate this Agreement immediately upon written notice to the other if the other party is adjudicated as bankrupt or if a petition in bankruptcy is filed by or against the other party or if the other party makes an assignment for the benefit of creditors or an arrangement pursuant to any bankruptcy act or insolvency laws.

C. Licensee may terminate this Agreement upon written notice to S&P.

D. S&P may terminate this Agreement upon ninety (90) days (or upon such lesser period of time if required pursuant to a court order) prior written notice to Licensee if (i) S&P is informed of the final adoption of any legislation or regulation or the issuance of any interpretation that in S&P's reasonable judgment materially impairs S&P's ability to license and provide the S&P 500 Index and/or the S&P Marks under this Agreement in connection with the Product; or (ii) any litigation or proceeding is threatened or commenced and S&P reasonably believes that such litigation or proceeding would have a

material and adverse effect upon the S&P 500 Index and/or S&P Marks or upon the ability of S&P to perform under this Agreement.

E. Upon termination of this Agreement by either party, Licensee shall cease all use of the S&P 500 Index and the S&P Marks and Licensee shall not issue, enter into, write, sell and/or purchase any additional Products, other than Products closing out preexisting positions in Products. At S&P's request, Licensee shall certify to S&P in writing that Licensee has fully complied with this requirement.

3. PROPRIETARY RIGHTS.

A. Licensee acknowledges that the S&P 500 Index is selected, coordinated, arranged and prepared by S&P through the application of methods and standards of judgment used and developed through the expenditure of considerable work, time and money by S&P and Licensee acknowledges that it has no proprietary interest therein. Licensee also acknowledges that the S&P 500 Index and the S&P Marks are the exclusive property of S&P, that S&P has and retains all proprietary rights therein and that the S&P 500 Index and its compilation and composition and changes therein are in the control and discretion of S&P.

B. Licensee acknowledges that S&P, or its third party licensors, is the owner of all right, title and interest in an to the S&P Marks and the goodwill appurtenant thereto. Licensee shall not use or authorize any other party to use the S&P Marks or any confusingly similar designation, trademark, service mark or trade name anywhere in the world for any purposes whatsoever other than as permitted in this Agreement or as otherwise duly licensed.

4. DISCLAIMERS; LIMITATION OF LIABILITY.

Licensee agrees expressly to be bound itself by and furthermore to include all of the following disclaimer and limitation language in the informational materials relating to the Product and upon request, shall furnish a copy or copies thereof to S&P:

"The Product is not sponsored, endorsed, sold or promoted by Standard & Poor's ("S&P"). S&P does not make any representation or warranty, express or implied, to the owners of the [insert Product] or any member of the public regarding the advisability of investing in securities generally or in the Product particularly or the ability of the S&P 500 Index to track general stock market performance. NEITHER S&P NOR ITS AFFILIATES GUARANTEE THE ADEQUACY, ACCURACY, TIMELINESS OR COMPLETENESS OF THE S&P 500 INDEX OR ANY DATA INCLUDED THEREIN. S&P AND ITS AFFILIATES SHALL NOT BE SUBJECT TO ANY DAMAGES OR LIABILITY FOR ANY ERRORS, OMISSIONS OR DELAYS THEREIN. S&P MAKES NO EXPRESS OR IMPLIED WARRANTIES, AND EXPRESSLY DISCLAIMS ALL WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE WITH RESPECT TO THE S&P 500 INDEX AND THE S&P MARKS. WITHOUT LIMITING ANY OF THE FOREGOING, IN NO EVENT WHATSOEVER SHALL S&P OR ITS AFFILIATES BE LIABLE FOR ANY INDIRECT, SPECIAL, INCIDENTAL, PUNITIVE OR CONSEQUENTIAL DAMAGES, INCLUDING BUT NOT LIMITED TO, LOSS OF PROFITS, TRADING LOSSES, LOST TIME OR GOODWILL, EVEN IF THEY HAVE BEEN ADVISED OF THE POSSIBILITY OF SUCH DAMAGES, WHETHER IN CONTRACT, TORT, STRICT LIABILITY OR OTHERWISE.

5. GENERAL.

A. *Governing Law.* This Agreement shall be governed by and construed in accordance with the laws of the State of New York, U.S.A., without giving effect to its rules of conflict of laws. Licensee agrees to the exclusive jurisdiction of the state and federal courts sitting in New York, New York, U.S.A. for the resolution of any disputes arising from or related to this Agreement.

B. *Assignment.* This Agreement shall not be assigned or transferred by Licensee without the prior written consent of S&P, and any attempt to so assign or transfer this Agreement without such consent shall be null and void.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the Effective Date.

Standard & Poor's Financial Services LLC

Signature: _____ Signature: _____

Name: _____ Name: _____
(Please print) (Please print)

Title: _____ Title: _____
(Please print) (Please print)

Email: _____ Date: _____
(Please print) (Please print)

Date: _____

EXHIBIT 5**OTC Options Auction Procedures****OTC Options Auction**

To facilitate the liquidation of positions in OTC Index Options and related positions in other cleared contracts and margin assets (including any securities underlying a stock loan or borrow position in which the Corporation has a security interest but not the stock loan or borrow positions themselves) (all such positions being collectively referred to herein as “OTC positions”) of a suspended OTC Index Option Clearing Member, as defined in the By-Laws of the Corporation (an “OTC Member”), the Corporation may determine to hold an OTC Options Auction as provided in Rule 1106(e)(2). Any such auction (the “Auction”) will be conducted in accordance with the procedures described below, which are incorporated by reference in Rule 1106(e)(2) and constitute a part thereof.

OTC Options Auction Participants

All OTC Members other than a suspended OTC Member must participate in the Auction (each referred to hereafter as a “Participant”). In addition, other persons who are “eligible contract participants” (as defined in the Securities Exchange Act of 1934) and otherwise eligible to hold positions in OTC Index Options may also submit bids in an Auction by making appropriate arrangements with a Participant.

Required Participation Level

Each Participant shall be assigned a minimum percentage of the Auction Portfolio (as defined below) in respect of which the Participant will be required to submit one or more bids to purchase or assume in the Auction. This “Minimum Participation” level in the Auction for each Participant will be determined by calculating the Participant’s proportionate share of the total “risk margin” requirement of OTC Members with respect to accounts eligible to hold OTC positions (“OTC Eligible Accounts”) after removing the suspended OTC Member. The total risk margin requirement will be calculated as the sum of the average daily margin requirement, consisting of the amount of margin held by OCC with respect to an OTC Member’s OTC Eligible Accounts in excess of the net asset value (“NAV”) of the positions held in such OTC Eligible Accounts, for each OTC Member for the previous month across all positions in all OTC Eligible Accounts of such OTC Member. Each Participant’s pro rata share is determined by dividing the Participant’s own average daily risk margin requirement for the preceding month by the total average daily risk margin requirement of all Participants (excluding the suspended OTC Member’s average daily risk margin requirement). To illustrate, below is an example with 5 OTC Members. Assuming a default by Firm D, the risk margin requirement breakdown and proportionate share of the risk margin requirement before and after Firm D’s default will be:

OTC Member	Previous month's avg. daily risk margin req.	Pre-default share	Post-default share ("Minimum Participation")
Firm A	\$20,000,000	20%	40%
Firm B	\$12,000,000	12%	24%
Firm C	\$4,000,000	4%	8%
Firm D	\$50,000,000	50%	Default
Firm E	\$14,000,000	14%	28%
Total	\$100,000,000	100%	100%

Auction Information

Prior to the Auction, the Corporation will calculate the Minimum Participation for each Participant and make such information available to the Participant, provide details of the OTC Index Options positions and other positions that may be hedging, or hedged by, OTC Index Options contained in the suspended OTC Member's portfolio (the "Auction Portfolio") and provide the calculated NAV of the Auction Portfolio based upon the Corporation's marking prices. (The NAV may be positive or negative.) The Corporation may determine to divide the suspended OTC Member's portfolio into more than one Auction Portfolio and auction the separate Auction Portfolios in separate Auctions, each of which will be conducted in the same manner.

Minimum Bid Size

Each Participant will be required to submit one or more bids for a portion of the entire Auction Portfolio with a required total minimum bid size equal to 1.15 x the Participant's Minimum Participation, up to a maximum of 100% of the Auction Portfolio (the "Minimum Bid Size"). (Note that the Minimum Bid Size refers to the minimum percentage of the portfolio that the Participant is required to bid on and not a minimum bid price. There is no minimum bid price.) Each Participant may submit up to 4 bids at varying quantities and varying prices such that the aggregate size meets the Minimum Bid Size. Participants may also utilize bids from clearing members and non-clearing members that are "eligible contract participants" in order to meet their Minimum Bid Size, provided that the Participant has such agreements in place with the clearing member or non-clearing member as required by the Corporation and guarantees the performance of the non-clearing member.

Bid Price

Each Participant will submit its bid(s) indicating for each bid the percentage of the Auction Portfolio it is bidding on and the amount of the bid (which may be positive or negative), such that each bid indicates, in the case of a negative bid, how much the Participant would be entitled to receive from the Corporation or, in the case of a positive bid, how much the Participant would be required to pay to the Corporation, to assume or acquire the relevant percentage of the Auction Portfolio. Bids will be expressed in terms of a price for the entire Auction Portfolio. The Corporation will rank bids from best to worst and the Auction Portfolio will be allocated in segments to Participants from the best bid to the worst bid until the entire Auction Portfolio is

allocated. The bid price that ultimately clears the entire Auction Portfolio will become the single price that determines the amount that all winning Participants will receive or pay (the "Clearing Price"); *i.e.*, all Participants with fulfilled bids will receive or pay the Clearing Price even if a Participant's stated bid was better.

For example:

Assuming a default by OTC Member Firm "D" with an OTC Index Option portfolio having a NAV of (\$35,000,000), the remaining OTC Members submit the following bids:¹

Firm A:	25% at \$40,000,000; 25% at \$50,000,000; 50% at \$80,000,000
Firm B:	27.6% at \$45,000,000
Firm C:	9.2% at \$100,000,000
Firm E:	32.2% at \$75,000,000

Based on bids submitted, they would be ranked in the following order:

1. Firm A: 25% at \$40,000,000
2. Firm B: 27.6% at \$45,000,000
3. Firm A: 25% at \$50,000,000
4. Firm E: 32.2% at \$75,000,000 (this becomes the Clearing Price)
5. Firm A: 50% at \$80,000,000
6. Firm C: 9.2% at \$100,000,000

Resulting winning allocations:

1. Firm A: 50% at \$75,000,000
2. Firm B: 27.6% at \$75,000,000
3. Firm E: 22.4% at \$75,000,000

Liquidation Deficiency/Priority Assessment

If a Participant does not succeed in purchasing or assuming a percentage of the Auction Portfolio at least equal to its Minimum Participation, such Participant shall become subject to a potential

¹ Prices in this example represent prices for the entire auction portfolio. Thus, a bid for 25% at \$40 million would be a bid to acquire 25% of the auction portfolio on the assumption that the value for the entire auction portfolio is \$40 million. If such a bid established the Clearing Price at \$40 million, the clearinghouse would have to pay the relevant bidder \$10 million to assume 25% of the auction portfolio. The bids in this example are negative bids (*i.e.*, represent the amount that the bidder would require to be paid in order to assume the net liability represented by the portfolio).

priority assessment against such Participants' Clearing Fund contribution (a "Priority Assessment"). Priority Assessments shall be made if the liquidation of the suspended OTC Member's business results in a deficiency that would result in a proportionate charge against the Clearing Fund contributions of all clearing members, regardless of the reason for any such deficiency. In the case of any such deficiency, the Corporation shall first make a Priority Assessment as provided in Rule 1106(e)(2)(C) against the Clearing Fund contribution(s) of such Participant(s). Any deficiency that remains after application of the Priority Assessment(s) shall be satisfied in accordance with Rule 1106(e)(2)(C) and Article VIII, Section 5 of the By-Laws.

Calculation of Priority Assessment

The Priority Assessment will be based upon (i) the NAV of the Auction Portfolio, (ii) the Participant's stated bids relative to the Clearing Price, and (iii) the "Assessment Ratio," as defined below. In order to calculate the Priority Assessment, the Corporation will first identify Participants that did not win a portion of the Auction Portfolio equal to or greater than their Minimum Participation. The amount of the Priority Assessment will be calculated as described below.

First, a Priority Assessment ratio will be based upon each such Participant's winning allocation vs. its Minimum Participation (the "Assessment Ratio"). The Assessment Ratio will be calculated as $1 - (\text{winning allocation} / \text{Minimum Participation})$.

For example:

OTC Member	Minimum Participation	Winning Allocation	Assessment Ratio
Firm A	40%	50%	None
Firm B	24%	27.6%	None
Firm C	8%	0	100%
Firm E	28%	22.4%	20%

Next, the Corporation will calculate how much of a Participant's clearing fund requirement may be subject to the Priority Assessment (the "Clearing Fund Contribution At Risk"). The Clearing Fund Contribution At Risk amount will be calculated as the percentage of the Auction Portfolio the Participant was required to bid for (*i.e.*, the Minimum Bid Size) x the Auction Portfolio NAV x Assessment Ratio.

For example:

OTC Member	Clearing Fund Requirement	Minimum Bid Size x portfolio NAV	Assessment Ratio	Clearing Fund Contribution At Risk
Firm C	\$92,000,000	9.2% of \$35 million =\$3,220,000	100%	\$3,220,000
Firm E	\$90,600,000	32.2% of \$35 million =\$11,270,000	20%	\$2,254,000

Finally, the Corporation will rank the Participants subject to the Priority Assessment in order of their bids submitted. Bids will be ranked from worst to best in order to apply the Priority Assessment.

1. Firm C: 9.2% at \$100,000,000
2. Firm E: 32.2% at \$75,000,000

The Priority Assessment will be satisfied against the Participants in the order their auction bids are ranked. In this example, since Firm C had the worst bid, the Priority Assessment would be exhausted by Firm C's Clearing Fund Contribution at Risk first. If the liquidation of the suspended OTC Member produced a \$3 million shortfall, Firm C would bear the entire Priority Assessment.

If the liquidation of the defaulting OTC Member produced a \$10 million shortfall, losses would be allocated as follows:

1. \$3,220,000 against Firm C
2. \$2,254,000 against Firm E
3. \$4,526,000 against all clearing members' Clearing Fund contributions (including Firm C and Firm E as well as Firms A and B)

Second Auction Option

If the Clearing Price is determined by an outlying bid, the Corporation will have the discretion to choose a clearing price that clears at least 80% of the Auction Portfolio at an improved price. The remaining Auction Portfolio would be re-auctioned using the same process as the first Auction, as described above.

Default Management Advisory Committee

The Corporation will establish a Default Management Advisory Committee that the Corporation will consult prior to determining to hold an OTC Options Auction as provided in Rule 1106(e)(2). If the Corporation determines to hold an OTC Options Auction, the Corporation will utilize the committee to assist in the closing of a suspended OTC Member's OTC Index Option portfolio. The committee will consist of representatives from each non-suspended OTC Member, and its role will be to advise the Corporation on the structure of the Auction Portfolio as well as any hedges to be established pending liquidation of the Auction Portfolio. The committee will serve strictly in an advisory capacity to the Corporation, and the Corporation's management will have full discretion to accept or reject any recommendations.