

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

Form 19b-4 Information

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

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Exhibit 1 - Notice of Proposed Rule Change

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

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

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

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Exhibit Sent As Paper Document

Exhibit 3 - Form, Report, or Questionnaire

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

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Exhibit Sent As Paper Document

Exhibit 4 - Marked Copies

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

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Exhibit 5 - Proposed Rule Text

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

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Partial Amendment

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

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 19b-4

Proposed Rule Change
by

THE OPTIONS CLEARING CORPORATION

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

Item 1. Text of the Proposed Rule Change

The Options Clearing Corporation (“OCC”) proposes to adopt interpretative guidance developed by OCC’s Securities Committee¹ regarding the administration and application of the new adjustment method for cash dividends and distributions (“New Methodology”).² The interpretative guidance, which is in the form of frequently asked questions (“FAQs”) and responses thereto, is set forth in Exhibit 5.

Item 2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by the Board of Directors of OCC at a meeting held on August 24, 2006.

Questions regarding the proposed rule change should be addressed to Jean M. Cawley, Senior Vice President and Deputy General Counsel, at (312) 322-6269.

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

Background

Generally, options are not adjusted to reflect “ordinary” cash dividends or distributions. Under OCC’s existing by-laws (which remain operative until the New Methodology becomes effective), a cash dividend is considered ordinary unless it is greater than 10% of the value of the underlying security on the dividend declaration date. Dividends greater

¹ Unless otherwise provided in OCC’s by-laws and rules, the Securities Committee determines all adjustments to the terms of outstanding cleared contracts. See Article VI, Section 11 of OCC’s by-laws.

than 10% under this definition usually trigger an options contract adjustment, with the criterion for adjustment being the size of the cash dividend. Under the New Methodology, a cash dividend or distribution will be deemed to be ordinary (regardless of size) if it is declared pursuant to a policy or practice or paying such dividends on a quarterly or other regular basis. Dividends paid outside such practice would be considered extraordinary. Extraordinary dividends usually would trigger a contract adjustment unless the amount is less than \$12.50 per contract (i.e., the minimum size threshold). The New Methodology will be effective for cash dividends and distributions announced on or after February 1, 2009, but will not be applied to certain grandfathered flex options as described in Release No. 34-55285.

Interpretative Guidance

OCC's adoption of the New Methodology has prompted market participants to ask how the New Methodology would be administered and applied. The Securities Committee has reviewed those FAQs and has developed responses thereto, which OCC is proposing to adopt as a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule (i.e., Article VI, Section 11A of OCC's by-laws). The FAQ responses are intended to provide investors with useful guidance on how the New Methodology would be applied in practice, subject to an adjustment panel's authority to make adjustment decisions on a case-by-case basis and to make exceptions to the general adjustment rules in cases

² The New Methodology, which is generally described in Item 3 below, was approved by the Commission in Release No. 34-55258 (February 8, 2007).

where such exceptions are determined appropriate.³ The interpretative guidance, which is attached as Exhibit 5, reviews the mechanics of adjustments, the definition of ordinary cash dividends and distributions, the rationale for the New Methodology, the impact of the minimum size threshold, and actual and hypothetical examples to illustrate the application of the New Methodology. OCC, however, does not propose to publish the interpretative guidance in its by-laws and rules. Rather, it would be published on OCC's public website, made available in an information memorandum accessible to clearing members or otherwise available in hard copy form on request.

* * *

The proposed change is consistent with Section 17A of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), because it provides market participants with interpretative guidance on the application of the New Methodology which will be applied to adjustments for cash dividends and distributions. The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended.

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

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

³ Adjustments are individually determined by an adjustment panel of the Securities Committee. Actions of an adjustment panel constitute the action of the Securities Committee. See Article VI, Section 11(c) of OCC's by-laws.

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 none have been received.

Item 6. Extension of Time Period for Commission Action

OCC does not consent to an extension of the time period for Commission action on the proposed rule change.

Item 7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Pursuant to Section 19(b)(3)(A), the proposed rule change is filed for immediate effectiveness inasmuch as it constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule

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

Not applicable.

Item 9. Exhibits

Exhibit 1. Completed Notice of Proposed Rule Change for publication in the Federal Register.

SIGNATURE

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

THE OPTIONS CLEARING CORPORATION

By: _____

Jean M. Cawley
Senior Vice President and
Deputy General Counsel

INTERPRETATIVE GUIDANCE ON THE NEW ADJUSTMENT POLICY FOR CASH DIVIDENDS AND DISTRIBUTIONS

Frequently Asked Questions

Disclaimer: The OCC Securities Committee has reviewed the questions and answers presented below and believes they provide useful guidelines for how the new adjustment policy will be applied in practice. However, as indicated several times below, all adjustments are individually determined by an adjustment panel of the Securities Committee on a case by case basis, and adjustment panels may make exceptions to general rules, interpretations, and policies in cases where they determine such exceptions to be appropriate. In no instance are the examples provided below meant to determine in advance the decisions that any adjustment panel will make in the future.

Overview of the New Adjustment Policy

Q. [Who decides if an option adjustment shall be made?](#)

A. All adjustments are determined on a case by case basis by an adjustment panel of the OCC Securities Committee. Each adjustment panel is comprised of two representatives from each exchange that trades the option in question, plus an OCC representative. The OCC member only casts a vote to break a tie. The adjustment panel decides whether an adjustment is called for and how it should be done.

Q. [What cash dividends call for an adjustment?](#)

A. “Ordinary” cash dividends do not call for adjustments. An “ordinary” cash dividend is defined as one paid “pursuant to a policy or practice of paying such dividend on a quarterly or other regular basis”. A cash dividend which is considered to be *outside* this regular policy is non-ordinary, or “special”. Assuming a given dividend is “special” according to this definition, a size test is also imposed: the value of the dividend must be at least \$12.50 per option contract. Thus, if the dividend is “special” and yields at least \$12.50 per option contract, then an adjustment will be made.

Q. [What’s the rationale for this approach?](#)

A. In general, dividends declared pursuant to a policy or practice of a company can be anticipated and priced into option premiums according to standard models. (For example, Pfizer has announced it will pay \$.24 quarterly dividends as part of an established dividend program.) “Special” dividends declared outside the normal policy of the company cannot be anticipated and integrated into pricing with the same degree of assurance.. Thus, when special dividends are announced, if no adjustment is made, the only way a call holder can capture the dividend is through exercise prior to the ex-dividend date. When this happens, significant option time value can be lost and financial losses due to operational error in submitting exercises may occur. The intention is to allow “special” dividends to accrue to the benefit of call holders without requiring them to exercise their options.

Q. [So any dividend that can’t be *anticipated* will be deemed a special dividend?](#)

A. No. Although special dividends may be unanticipated, the important criterion is whether a dividend is paid pursuant to a program or policy of paying dividends on a quarterly or other regular basis. In some cases, the dividends of a company paid according to such a policy may be

highly variable and subject to increases or decreases that some may consider “unanticipated”. Nevertheless, these dividends would not normally be deemed “special”.

Examples: What if...?

Q. Who determines if a cash dividend is “special”?

A. The adjustment panels of the OCC Securities Committee will make this determination. In most cases, we anticipate being able to rely on the description of the company itself in describing its dividend. In our experience, dividends that are called “special” or “extraordinary” (or similar terms) by the company in fact describe the non-ordinary dividend events that we want to capture by adjustment. However, the company’s characterization of a dividend is not binding on adjustment panels.

Q. What if a company that previously paid no dividends initiates a regular dividend program – would the initial dividend be considered “special” and therefore adjustable?

A. No. The initial dividend would be paid pursuant to a policy under which the company intends to pay dividends on a regular basis. Therefore, it would not be deemed “special” and adjustable.

Q. What if a company announced a dramatic increase in a regular dividend? For example, what if a company’s last quarterly dividend was \$.20 and the current quarterly dividend was bumped to \$1.00 – wouldn’t that be a “special”, one-time event that would call for an adjustment?

A. No – most likely not. As mentioned earlier, we would start with the company’s description of its dividend. If the company has a quarterly dividend program and the company says this quarter’s dividend is \$1.00, then we anticipate the adjustment panel would deem the dividend to be ordinary and not adjustable. However, as mentioned, the decisions of the adjustment panels are always made on a case by case basis, in light of the circumstances and facts as understood at the time.

Q. What about REITs, natural resource trusts, and similar companies that pay very irregular dividends? Such companies could pay no dividends for many months and then suddenly pay a dividend. Would that be considered a “special”, adjustable dividend?

A. No – most likely not. The kinds of companies mentioned in the question often have very regular dividend *policies* but will *actually* pay dividends only when certain conditions are met, or in response to market conditions. REITs, for example, are generally required to pay out profits to shareholders when and if profits are realized. They may determine dividends monthly, although the cash amount available for distribution may actually be zero in any given month. Thus, although the dividend payouts of such companies may be irregular, insofar as they occur *pursuant to the policy of the company*, they would be considered ordinary and not adjustable. The adjustment panels would look to the company’s characterization of the dividend and its dividend policy.

Q. What if a company is reorganizing itself into a REIT and is required to pay out accumulated profits in a large dividend as it commences a dividend program. You said before that *initial* dividends would not normally call for adjustment. Would you adjust in this case?

A. In our experience, companies reorganizing themselves into REITs or income trusts often designate this initial required pay-out as a “special” dividend. Precedent exists for adjusting for such dividends under OCC’s existing adjustment rules, and it is likely that they will be adjusted for under the new rules. Even if the company did not specifically characterize such a dividend as “special”, the adjustment panels could decide to deem them special and adjust.

- Q. Fund share or ETF options have previously been adjusted in response to special dividends declared with respect to component securities of the fund. The most notable instance was the Microsoft \$3.00 special dividend in 2004. How will these kinds of distributions be handled?
- A. If a fund (ETF, HOLDR, etc.) is making a cash distribution which is identified (in whole or part) by the fund as attributable to a special dividend on a component security, then the appropriate amount of the cash distribution will also be considered a special, adjustable distribution. For example, if an ETF is making a \$1.00 quarterly cash distribution, \$.25 of which is attributable to a special dividend on a component security, the adjustment panel will normally consider \$0.25 of the aggregate distribution as a special dividend and adjust for \$25.00 per option contract (assuming a 100 share option).

Note: The \$12.50 size test will also be applied: the portion of the distribution attributable to the component security's special dividend must yield \$12.50 value per option contract before an adjustment is done.

- Q. What if a company declares a special dividend which is ex-distribution on the same date that a regular dividend is "ex"? Would these be considered one event or two separate events?
- A. Two separate events.
- Q. The Phelps Dodge (PD) special dividends present an interesting case. PD announced they intended to pay a certain aggregate cash amount in a series of special dividends and/or effect stock buy-backs over the upcoming year. Would these dividends be considered "special"; or would they be considered "ordinary" because they were paid pursuant to an announced program?
- A. In the case of PD, each dividend was characterized *by the company* as "special" and although paid pursuant to a "program", PD gave no indications it would be permanent. The "program" allowed special cash dividends to be paid in lieu of stock buy-backs. PD also continued to pay quarterly dividends which were separate from the special dividends. Thus, it is likely the adjustment panels would consider each dividend paid by PD pursuant to this program to be "special" and call for an adjustment. As mentioned earlier, the adjustment panels address each dividend on a case by case basis.
- Q. What if a company's regular quarterly dividend is a "return of capital"? Would that make it a special, adjustable dividend?
- A. No. Insofar as the dividend is still a regular quarterly dividend, it would not call for an adjustment. Ordinarily, the source of cash to be paid will not be determinative of the adjustment decision. In the past, however, adjustment panels have determined to adjust for any dividends paid pursuant to a plan of liquidation – even regular dividends of the company included in the plan. They may follow this precedent in the future as well for companies undergoing liquidation.

Operational Matters

- Q. Will we have to wait until the official declaration date of a dividend before a decision is made about option adjustment?
- A. Not necessarily. The adjustment panels will be motivated to make their adjustment decisions as soon as practicable. The panels may decide it is appropriate to base a decision on the company's press release or similar announcement, in advance of the formal declaration date. Of course, if

this is done, the adjustment decision would be appropriately conditional. For example, “if declared and paid as described in the press release, then...”

For example, suppose a company announces its intention in a press release to pay a special dividend, but this dividend is contingent on shareholder approval or other conditions. Until the conditions are met, it will not be officially declared. Under the new policy, it will be easy to see if the dividend meets the size criterion: would it yield \$12.50 per contract? If “yes”, then if the adjustment panel determines it is a “special” dividend, investors will immediately know an adjustment will occur if the dividend is actually declared.

Q. Won't this new adjustment policy result in option symbol proliferation?

A. Yes, to some extent. Contract adjustments under the new policy will be more frequent and in many cases a new symbol will be required. However, OCC and the exchanges feel the benefits of the new policy outweigh the operational costs.

One should note that when equity option strike prices can be denominated in decimals and the need for “ticker codes” for each strike is eliminated, adjustments will be possible *without* the need to change option symbols (as the strike prices can be reduced by the exact amount of the dividend). When that happens, symbol proliferation will not occur. The option industry is looking forward to this capability in 2010.

Q. If an adjustment is called for, *how* will it be done?

A. There will be no changes to the *methods* of adjustment. There are two methods of adjustment: 1) simply reduce the strike prices by the amount of the dividend. This is the preferred method and will normally be used if the strike prices can be reduced *without rounding*. 2) If strike prices can't be reduced without rounding, then the amount of the dividend will be added as a cash component to the option deliverable. When this is done, an option symbol change normally occurs.

Adjustments will continue to be made on the ex-date for the cash dividend as determined by the appropriate market.