in this issue:

update from the hill 2

industry insight: box's will easley 3

collateral in margins to improve risk process 4

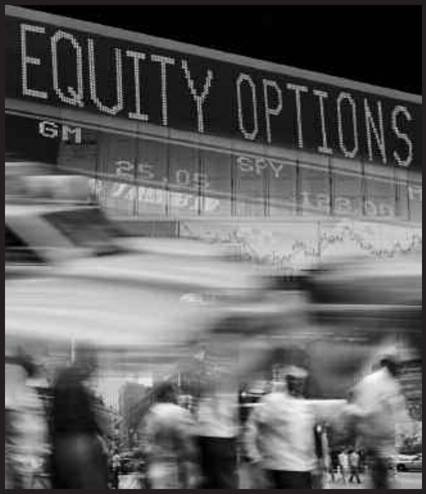
industry initiatives & updates 5

board of directors welcomes new members 6

occc news

the official newsletter of The Options Clearing Corporation **Fall 2009**

record crowds attend content rich equity options conference



The Fourth Annual FIA/OIC Equity Options Conference was held on September 22-23 in New York's bustling Times Square. With more than 350 attendees — well above the 313 attendees last year — it was the most successful Equity Options Conference yet.

Attendees were treated to a full day of informative panels. A measure of the value provided by the conference content can be found in the amount of press coverage it generated. Shortly after the event, around a dozen published articles sourced the conference.

Setting the pace was the first panel, Outlook for U.S. Equity Options Exchanges. Moderated by industry legend Blair Hull, the panel featured the leaders of the options exchanges who engaged in a substantive discussion of some of the most important market structure issues facing the industry today. From disagreements on certain issues, like ISE's qualified clean cross proposal, to areas of more consensus, such as the market maker exemption on short sale rules, the standing-room-only crowd had a clear view of each exchange's position on many of the hottest topics in the business.

continued on page 2

continued from page 1

That discussion was followed by a highly distinguished panel of the last three option's industry Sullivan Award recipients who spoke about the future of exchange-traded derivatives. Interactive Brokers Chairman Thomas Peterffy, ISE Chairman David Krell, and CBOE Chairman and CEO William Brodsky surveyed the financial services landscape in the wake of the economic crisis with an eye toward how the industry will emerge from the recovery.

Other panels covered high frequency trading and how the U.S. options industry appears from an international perspective. A question and answer session with regulatory representatives from the SEC, CFTC and FINRA, moderated by OIC Executive Director Susan Milligan, closed the conference.

Audio of all the sessions is available on the FIA web site, www.futuresindustry.org.

"This year's Equity Options Conference was the best yet, a full day of interesting and important sessions," said Gina McFadden, OIC President. "The conference started strong four years ago and has gained traction every year. I have no doubt next year will be even better."

update from the hill

By Bradley Edgell and Ted Dahlstrom

In the previous Update from the Hill, we discussed financial regulatory reform and what legislative steps Congress and the Obama Administration are taking to prevent future financial crises. Much progress has been made since the Administration's proposal was unveiled, but much more remains to be done.

The SEC and CFTC recently held, for the first time, two days of joint hearings on regulatory harmonization, with the goal of increasing transparency and eliminating regulatory arbitrage. Our own CEO, Wayne Luthringshausen, appeared as a panel witness to discuss OCC's unique regulatory position of being regulated by both agencies. His testimony, along with that of the other witnesses, was useful to the agencies as they continue to prepare the report that will outline their recommendations to harmonize the regulation of securities and futures. The report was released on October 16.

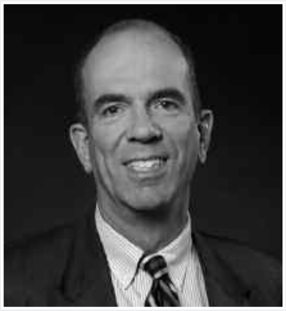
Congressional efforts on regulatory reform are ongoing and the timetable for considering legislation remains fluid. The House Financial Services Committee (HFSC) marked-up a total of 7 bills during October and November. The house will likely consider all of these bills in December. The Senate Banking Committee (SBC) is expected to mark-up a massive regulatory reform bill during December. Because of the likelihood of significant differences between the versions considered by the SBC and HFSC, efforts to reform our nation's financial regulatory system will probably continue into next year.

One subject of discussion in Congress is the issue of possibly providing a regulatory scheme for OTC derivatives contracts, which are currently not regulated or overseen by any federal regulator. OCC has been working closely with Congressional leaders on this issue and is exploring the possibility of clearing some types of these contracts. Both House Committees of jurisdiction have taken a keen interest in this issue and legislation will likely be approved in this area.

industry insight

box vice chairman will easley

In this final installment of interviews with prominent industry leaders from the U.S. options exchanges, OCC News sits down with BOX's Vice Chairman, Will Easley. During the conversation, Mr. Easley discusses the origins of the Price Improvement Period (PIP), the move away from Make or Take pricing and the exchange's role in a constantly evolving industry.



How did you get your start in the options industry?

I came out of business school in 1982 when jobs were hard to come by. I have colleagues who joke that I must have been the only person hired in the Canadian securities industry at that time. I started in Montreal, working in business development and marketing for a very new product...options. After three years, I moved to London to work in options marketing, and then I was hired by a clearing firm who sent me to Paris. One thing led to another and I stayed in France for the next 15 years. I didn't work in the U.S. until the start of BOX in 2004.

Looking back, as an undergraduate I was once told by a New York stockbroker to "go to Chicago because there was all this stuff going on with financial futures and I could probably make a lot of money." I didn't follow his advice, but I was lucky to have a second chance at it.

One thing that distinguishes BOX from other exchanges is its electronic auction model known as the PIP. How did this model come into existence?

Five years ago, everything traded in nickels and dimes. Although we knew there was a willingness to do better, the prices had to be in nickels or dimes. The original impetus for the PIP was to allow for trading in pennies. The concern was that it would generate so much additional quote traffic that it would overwhelm the system technology. The price improvement auction was a way to trade in pennies without broadcasting in pennies and causing additional problems.

The idea was that the penny should go to the customer and not into the broker's pocket, so by using this option, it would become transparent to the public. It was also our cannon shot against Payment for Order Flow. We didn't win that battle, but the fact that one-third to half of the market now trades in pennies shows that we may have actually won the war. We pushed the market to pennies. I think the Penny Pilot is really a result of BOX having the PIP.

We proved that there was an appetite for trading in pennies. While it didn't necessarily result in BOX gaining as much business or market share as we might have liked, I think we accomplished the goal of improving the market for investors.

With the increasing global demand for U.S. listed options, where does BOX fit in as an exchange that has long ago established strong international ties through its relationship with the Montreal Exchange?

Our first tie, of course, was via Montreal but Canadians are peculiar foreigners in the sense that in many ways Canada is part of the domestic U.S. market. It's a close border and has been very fluid for investment activity. We certainly did not become the conduit for Canadian business in the U.S. because that business had already been coming down well before BOX existed.

An interesting development for us internationally is that the London Stock Exchange has licensed the software [SOLA®] that we use for their options market. The platform will be implemented in the London equity options market first and then the Italian derivatives market. Once that happens, we think there is potential for being the gateway for brokers in Milan and London. It will be very easy to have a switch that will send an order to BOX, which is akin to what Eurex and ISE have done recently.

Europe is really different in terms of distribution networks because investors often use their bank as their broker, or they trade online. Frankly, I don't think BOX is big enough to take a big bite out of the European market. The brokers are already out there doing it. What is up to us is to have the best quality market so when the broker brings the order in — whether it is from California or France — it comes to BOX because we have the best price and service.

While BOX maintains a smaller market share than some of the other exchanges, it continues to grow at a steady pace. What are the reasons that BOX remains competitive in this constantly evolving market?

We don't compete in all dimensions. There are things like block trading, complex orders, solicitation, facilitation, delta neutrals that we don't do. We are working on closing some of those holes, but we haven't done it yet. Arguably, our five percent of the market share is more like 12-13 percent if you took out all the things we don't do. We focus on our expertise and where we can bring value.

Ultimately because all of the exchanges trade the same thing, clear through the same clearinghouse, broadcast by the same broadcaster, and are regulated by the same regulator, we compete on service, price and technology. I think you can talk to people and find that most would say that BOX has been a good thing for the industry because we have consistently pushed towards more transparency.

An investor doesn't care whether there are 130 or 380 contracts at the top of the book when he's selling 20. He does care that he's getting $2-3 better on his orders. That's indisputably true for small investors and that's who we have focused on. We have always believed that the institutional and professional segments of the market will adapt because it's their job whereas we think that we should always be building ourselves for the private investor and we are comfortable with that.

In September, BOX announced the elimination of Make or Take pricing. What were some of the factors that went into making this decision and how do you see this move impacting the industry?

Make or Take was not a philosophy for us. It was a commercial thing. Would it attract business? There should be no effect on the overall industry as other exchanges offer these market models.

The theory behind Make or Take was that by paying a liquidity provider a credit some of the time, the provider would post a better price on the market than he would elsewhere. If a provider was posting on one exchange and paying 50 cents, but on BOX he traded and was getting paid $30 that is almost 80 cents — nearly a dollar. That's a penny tick. Ideally, people would send orders because you were a penny better.

It turned out we weren't a penny better very often. The theory didn't work in practice. I don't think Make or Take is necessarily a dead issue. It works best on options classes that are less active because that's where you need to pay somebody to post liquidity. The Penny Pilot was on classes that were less apt to work with Make or Take. It just didn't work for us on the most active penny classes.

BOX's main office is located in Chicago. What is the tie to the Midwest and is there still a direct connection to Boston?

The Boston connection was originally with the Boston Stock Exchange, who was one of our founders, so it was natural to have people there. The problem is that our customers — brokers, banks, larger institutional investors — are predominately located in New York and Chicago. We hired some marketing representatives in Chicago, and it just became natural to open a Chicago office. Eventually, half our staff was in Boston, the other half in Chicago. Boston Stock Exchange was recently bought by NASDAQ, so now we are regulated by our competitor. We are in the process of trying to become our own SRO, which is a lengthy process. Once we are done, we won't have that particular connection to Boston. I expect though that we will continue to have Boston staff. We have people there that have been with us for several years and they do their job well. We might just have to change the name on the door.

collateral in margins to improve risk process

OCC has recently been working on an effort to enhance risk management measures for its clearing members. This effort, dubbed Collateral in Margins (CIM), is expected to take effect in early December and will provide margin offsets between derivatives contracts and certain margin deposits. Specifically, CIM will combine clearing members' options positions with their margin deposits in the form of common stock, including ETFs, recognizing hedges between these positions in risk calculations to produce a combined margin requirement.

The most significant changes associated with CIM include security-specific haircuts versus one conservative haircut applied to all positions, risk-based versus market value-based concentration charges, and the recognition of hedges between options positions and equity margin deposits. Clearing members can take advantage of these changes by pledging less volatile securities as well as those securities that hedge their existing options portfolio. OCC expects this will have the effect of lowering systemic risk and increasing liquidity of its member firms.

It is anticipated that once OCC begins to recognize these offsets, clearing members will receive more value for their margin deposits, which could result in clearing members having to post less collateral in total. Potential savings will depend on a number of factors, but could range from 10% to 30%. Since early October, OCC has been providing firms with a forecasting report — the Collateral in Margins Memo — that highlights potential savings associated with this enhancement. The report summarizes a firm's margin requirement by account type, collateral deposits, and margin excess or deficit, both pre- and post-CIM implementation. To assist firms in making collateral substitutions with their equity margin deposits, OCC will provide intra-day margin values via a Direct Data Service transmission as well as a comma-delimited text file that can be exported through OCC's clearing system, ENCORE. Clearing members will continue to follow the same process used today to adjust their collateral inventory balances. The collateral efficiencies associated with CIM will not only potentially reduce margin expenses for its clearing members, but will reduce overall systemic risk for OCC.

If you have any questions regarding Collateral in Margins or how the new process might benefit your firm, contact your OCC Financial Services representative.

options in the media

►"The U.S. options market has held up relatively well in the financial crisis. Volumes so far this year are flat compared with last year, says The Options Clearing Corporation, which clears for all seven U.S. options exchanges. But volumes could overtake last year, as trading was muted in the post-Lehman world of the last two months of 2008. The trend compares favourably with the futures industry, where volumes are down about a quarter on last year."

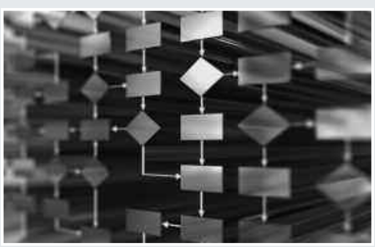
- Financial Times, "The Tectonic Plates Are Shifting," October 20, 2009

►"The [Loosening Your Collar: Alternative Implementations of QQQ Collars] study found that over a 10-year period the collar strategy outperformed the traditional buy and hold strategy, and significantly reduced investment risk. The important takeaway from the study is that it is a mistake to idly accept whatever it is that the stock market gives you. Innovate. Take action. Protect your assets. It's much easier than having to start over from scratch."

- Barron's, "Hedging Under the Academic Microscope," September 24, 2009

►"A U.S. Treasury plan to end preferential tax treatment for derivatives traders may be losing steam after the so-called 60/40 benefit was excluded from a recent healthcare reform bill... 'Later this year, I expect the Congress to do another tax bill and 60/40 is one of the potential things they would look at,' Susan Milligan, senior vice president of government relations for The Options Clearing Corporation said, citing a huge drive for revenue and growing concerns on Capitol Hill about the rising deficit."

- Reuters, "U.S. Tax Plan May Be Losing Steam-Exchange Execs," September 23, 2009



industry initiatives & updates

OCC continues its efforts to provide value-based services to its clearing members and exchanges through several key initiatives:

► **Intermarket Symbol Reservation Authority (ISRA)**

To address growing concern about the availability and accessibility of trading symbols, known as "ticker symbols," the SEC called for the adoption of a national market system that would streamline the ticker reservation and allocation procedure. Early this year, ISRA selected OCC to host and manage a centralized ticker reservation service. OCC initially worked with the ISRA committee, which is comprised of securities exchanges and FINRA, to build an initial central repository for tickers that would be used for planned new listings. The repository has helped to reduce the effort needed by exchange staff to secure potential new tickers. It has also provided all users with a formal process for reserving tickers and a convenient centralized ticker reservation listing.

Moving forward, OCC will create a more robust automated system that will provide participants with an online database featuring powerful search capabilities as well as the ability to be notified when a symbol is in use or has been reserved. Speaking to OCC's involvement with the ISRA project, Amy L. Lawson, OCC Vice President, Product Development, commented that, "OCC is pleased to provide additional services to the securities industry. The implementation of a formalized central system for ticker symbols will serve to streamline operations and bring efficiencies to the entire industry."

For more information regarding ISRA, visit the Products and Services section on OCC's web site at www.optionsclearing.com.

► **Large Options Position Reporting (LOPR)**

Progress on the development of a revamped Large Options Position Reporting system continues as OCC prepares for its transition to being the central hub for LOPR data. Since August, firms that submit LOPR data have been testing connectivity and data format as well as performing limited cycle testing within OCC's External Test Environment. After completing these initial testing activities, firms may begin transmitting LOPR data to OCC's production environment on a nightly basis. From November 23, 2009 through January 18, 2010, firms will be required by their SRO to dually submit LOPR

continued on page 6

continued from page 5

data transmissions to OCC and to SIAC, the current LOPR data aggregator. Beginning January 19, firms will submit LOPR transmissions exclusively to OCC. Firms should refer to their SRO for definitive instructions on the dual submission timeline.

For more information, contact the Member Services Help Desk at 1-800-544-6091 or 1-800-621-6072 (within Canada, dial 800-424-7320). Clearing members may also contact Member Services via email at memberservices@theocc.com.

►Options Symbology Initiative (OSI)

As much of the work on the Options Symbology Initiative has been completed, industry participants now shift their focus to scripted industry testing throughout fall 2009.

The beta test for OSI took place on September 12, 2009. More than 6,000 trades were submitted by 32 OCC clearing members through the seven options exchanges during the voluntary beta test. These clearing members account for 78 percent of the year-to-date cleared contract volume. Trade and post-trade data were processed through OCC's ENCORE system with cleared data being delivered to participating firms.

The beta test was designed to highlight possible technical issues associated with clearing member, exchange and OCC test environments in preparation of the mandated Scripted Industry Testing scheduled for the coming months. OCC has received positive feedback from the exchanges and clearing members regarding the results of the beta test.

A Scripted Industry test took place on October 10, 2009. Updated information regarding testing can be found on the OSI testing blog at http://osi-testing.blogspot.com. Clearing members should also visit the Symbology section on OCC's web site to stay informed on upcoming milestones.

Clearing members who have additional questions regarding testing should contact OSI_Testing@theocc.com.

board of directors welcomes new members

OCC recently announced the elections of Andrew D. Kolinsky, President of Citadel Execution Services, Philip A. Pendergraft, Chief Executive Officer at Penson Worldwide, Inc. and Tom Stern, Chief Executive Officer of optionsXpress International, to OCC's Board of Directors.

Mr. Kolinsky is President of Citadel Execution Services, which is part of the Citadel Derivatives Group. Previously he served as Managing Director and Head of Broker Dealers Sales and Marketing with Knight Capital Group where he was in charge of maintaining and growing the broker dealer business. He also served as a member of Executive Management where he helped lead the overall direction of the company.

Mr. Pendergraft serves as Chief Executive Officer at Penson Worldwide, Inc. With more than 25 years in the securities industry, he has extensive experience, especially in regards to his work at affiliated Penson entities. In 1995, Mr. Pendergraft co-founded Penson Financial Services, Inc. and throughout his career he has been involved in the start up of three clearing operations.

Mr. Stern, Chief Executive Officer of optionsXpress International, is responsible for the development of international business with registered companies in Europe, Singapore, Australia and Canada. Additionally, he serves as the Chief Administrative Officer for optionsXpress Holdings and Chief Financial Officer of optionsXpress and brokersXpress. He also acts as FINRA's primary Executive Representative and Financial and Operations Principal for optionsXpress.

"We are pleased to be able to add these three distinguished new members to OCC's Board of Directors. Their industry experience and perspective will further enhance our Board," said Wayne Luthringshausen, OCC Chairman and Chief Executive Officer.

occ news

www.optionsclearing.com

OCC News is now published seasonally, four times per year. If you would like to receive OCC News, please contact Leisha Nicol at lnicol@theocc.com. To receive OCC News via email, send a blank email message to join-occ_online_news@list.theocc.com. Inquiries and letters to the editor should be directed to Leisha Nicol, The Options Clearing Corporation, Corporate Communications Department, One North Wacker Drive, Suite 500, Chicago, Illinois 60606. Telephone (312) 322-6276 or email lnicol@theocc.com.

Editor/Designer: Leisha Nicol