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Page 1 of * 62

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2017 - * 009
Amendment No. (req. for Amendments *)

Filing by Options Clearing Corporation

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

Initial * ☑ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule
- ☐ 19b-4(f)(1)
- ☐ 19b-4(f)(2)
- ☐ 19b-4(f)(3)
- ☐ 19b-4(f)(4)
- ☐ 19b-4(f)(5)
- ☐ 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document ☐ Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed rule change concerning OCC's Counterparty Credit Risk Management Policy.

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Justin Last Name * Byrne
Title * Vice President, Regulatory Filings
E-mail * jbyrne@theocc.com
Telephone * (202) 971-7238 Fax (312) 322-6280

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 10/12/2017
By Justin W. Byrne
(Name *)

(Title *)
Vice President, Regulatory Filings

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Justin Byrne, jbyrne@theocc.com

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

Form 19b-4 Information *

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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.

Exhibit 1 - Notice of Proposed Rule Change *

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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)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

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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, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

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

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Exhibit Sent As Paper Document

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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.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

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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.

Exhibit 4 - Marked Copies

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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.

Exhibit 5 - Proposed Rule Text

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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.

Partial Amendment

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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.

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

This proposed rule change by The Options Clearing Corporation ("OCC") would formalize OCC's Counterparty Credit Risk Management Policy ("CCRM Policy" or "Policy"), which promotes compliance with multiple requirements applicable to OCC under Rule 17Ad-22, including Rules 17Ad-22(e)(3) concerning frameworks for the comprehensive management of risks, (e)(4) concerning credit risk management, (e)(16) concerning the safeguarding of assets, (e)(18) concerning risk-based participation criteria, (e)(19) concerning risks form indirect participants, and (e)(20) concerning linkages.[1] The CCRM Policy is included as confidential Exhibit 5. The policy is being submitted without marking to improve readability as it is being submitted in its entirety as new rule text.

The proposed rule change does not require any changes to the text of OCC's By-Laws or Rules. All terms with initial capitalization that are not otherwise defined herein have the same meaning as set forth in the OCC By-Laws and Rules.[2]

Item 2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved for filing with the Commission by OCC's Board of Directors ("Board") at a meeting held on February 24, 2017.

Questions should be addressed to Justin Byrne, Vice President, Regulatory Filings, at (202) 971-7238.

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1 17 CFR 240.17Ad-22(e)(3), (4), (16), (18), (19), and (20).

2 OCC's By-Laws and Rules can be found on OCC's public website: http://optionsclearing.com/about/publications/bylaws.jsp.

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

A. Purpose

Background

As a central counterparty providing clearance, settlement, and risk management services, OCC is exposed to and must manage a range of risks, including credit risk. The purpose of the CCRM Policy is to outline OCC's overall approach to identify, measure, monitor, and manage its exposures to direct and indirect participants, Liquidity Providers,[3] asset custodians, settlement banks, letter of credit issuers, investment counterparties, other clearing agencies, and financial market utilities ("FMUs")[4] (each a "Counterparty") arising from its payment, clearing, and settlement processes. OCC notes that the CCRM Policy is part of a broader framework used by OCC to manage credit risk, including OCC's By-Laws, Rules, and other policies and procedures that are designed collectively to ensure that OCC appropriately manages counterparty credit risk and to promote compliance with Rule 17Ad-22.[5]

The CCRM Policy would be maintained by OCC to promote compliance with a number of rules adopted under Section 17A of the Securities Exchange Act of 1934, as amended

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3 Under the CCRM Policy, "Liquidity Provider" is defined as a Commercial Bank or a non-banking institution – generally a pension fund – that provides a committed liquidity facility to OCC.

4 Under the CCRM Policy, "Financial Market Utility" is defined as a derivatives clearing organization partnering with OCC to provide a cross-margin program; a clearing agency providing settlement services of securities arising from the exercise, assignment or maturity of options or futures; or the Depository providing book-entry securities transfers and asset custodian services.

5 17 CFR 240.17Ad-22.

("Act"),[6] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Clearing Supervision Act").[7] In particular, the Policy is designed to address certain aspects of Rules 17Ad-22(e)(3) concerning frameworks for the comprehensive management of risks, (e)(4) concerning credit risk management, (e)(16) concerning the safeguarding of assets, (e)(18) concerning risk-based participation criteria, (e)(19) concerning risks form indirect participants, and (e)(20) concerning linkages.[8]

Counterparty Credit Risk Management Policy

OCC's CCRM Policy outlines the key components of OCC's framework for identifying, measuring, monitoring, and managing OCC's exposures to its Counterparties. This framework includes: (1) the identification of credit risk, (2) Counterparty access and participation standards, (3) the measurement of its Counterparty exposures, (4) the monitoring and managing of Counterparty exposures, and (5) voluntary termination of Counterparty relationships. Each of these components is described in more detail below.

Identification of Credit Risk

The CCRM Policy identifies various ways in which credit risk originates from the failure of a Counterparty to perform. With respect to a Clearing Member, the CCRM Policy details a number of different ways in which OCC may be exposed to credit risk. This includes the potential failure of a Clearing Member to pay for purchased options, to meet expiration-related

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6 15 U.S.C. 78q-1.

7 12 U.S.C. 5461 et. seq.

8 17 CFR 240.17Ad-22(e)(3), (4), (16), (18), (19), and (20).

settlement obligations, or to make certain mark-to-market variation payments or initial margin deposits. It also includes the potential insufficiency of a defaulting Clearing Member's margin and Clearing Fund deposits in a liquidation scenario. Other sources of credit risk identified in the CCRM Policy include the inability of OCC to access collateral (e.g., cash or securities) from a custodian or investment counterparty that is needed to facilitate a liquidation, or a failure by an issuer of a letter of credit to honor its corresponding obligations. The CCRM Policy also identifies that certain relationships with other FMUs, such as cross-margining programs and cash market settlement services, represent critical linkages that may present certain degrees of credit exposure based on the terms and design of the linkage. The CCRM Policy also notes that OCC may face additional risks from Counterparties, such as the potential failure of a Liquidity Provider to honor a borrowing request.

Counterparty Access and Participation Standards

Under the CCRM Policy, OCC's management of Counterparty credit risks begins with an initial evaluation process intended to ascertain that Counterparties meet certain minimum financial and operational standards and are considered as having a low probability of defaulting on their obligations prior to engaging or effecting any new transactions or expansion of business with OCC. To accomplish this objective, OCC shall evaluate each Counterparty against established minimum standards of creditworthiness, overall financial condition, and operational capabilities. Pursuant to the Policy, the standards used to evaluate Counterparties shall be objective, risk-based, and publicly-disclosed in order to permit fair and open access. These standards shall be developed independently for Clearing Members, Commercial and Central

Banks, investment counterparties, Liquidity Providers and FMUs, accounting for differences in their regulatory reporting and overall business operations.

Clearing Membership Standards

OCC's minimum participation standards for Clearing Member are found in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and other publicly-disclosed supplemental documentation (together, "Participation Standards Documentation"). Under the Policy, OCC's Credit Risk Management and Member Services departments shall evaluate each Clearing Member applicant against the minimum standards of creditworthiness and for its overall financial condition and operational capabilities as provided in the Participation Standards Documentation. Such evaluation shall also consider the Counterparty's aggregation of exposure on an individual and related-entities level, as applicable, as well as any material exposure that may arise from tiered participation arrangements. The Credit Risk Management and Member Services departments shall document the results of this evaluation in a memorandum, including the Clearing Member applicant's ability to meet relevant participation standards, and report those results to OCC's Executive Chairman, Chief Operating Officer or Chief Administrative Officer for review and approval, where appropriate, or for recommendation to the Risk Committee or Board of Directors.[9]

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[9] Pursuant to Article V, Section 2 of the By-Laws, the Executive Chairman, Chief Operating Officer and Chief Administrative Officer each have delegated authority to approve Clearing Member applicants provided that (1) there is no recommendation to impose additional membership criteria in accordance with Article V of the By-Laws and (2) the Risk Committee is given not less than five days to determine the application should be reviewed at a meeting of the Risk Committee. Pursuant to Interpretation and Policy .06 to Article V, Section 1 of the By-Laws, the Risk Committee has the authority to impose additional requirements on Clearing

Commercial and Central Banks

OCC's minimum standards for asset custodians, settlement banks, letter of credit issuers and investment counterparties are found in OCC Rule 604 and relevant OCC procedures. The Credit Risk Management department shall coordinate with various departments (such as Collateral Services or Treasury) to evaluate each bank against the minimum standards of creditworthiness and for its overall financial condition and operational capabilities as provided in OCC Rule 604 and related OCC procedures. Such evaluation shall also consider the Counterparty's aggregation of exposure on an individual and related-entities level, as applicable, as well as whether OCC would be able to structure its custodial relationships in a manner that allows prompt access to its own and its Clearing Members' assets. The latter shall include holding assets at supervised and regulated institutions that adhere to generally accepted accounting practices, maintain safekeeping procedures, and have internal controls that fully protect these assets. Under the Policy, Credit Risk Management and either the Collateral Services or Treasury department, as applicable, shall document the results of its evaluation in a memorandum, including the bank's ability to meet relevant participation standards, and report those results to OCC's Executive Chairman, Chief Operating Officer or Chief Administrative Officer, each of which shall have the authority to approve new and expanded relationships with

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Member applicants, such as increased capital or margin requirements as well as restrictions on clearing activities. The Risk Committee also has the authority to approve waivers of certain clearing membership requirements under Article V, Section 1 of the By-Laws. Approvals of a Clearing Member business expansion by the Executive Chairman, Chief Operating Officer or Chief Administrative Officer are subsequently presented to the Risk Committee for ratification, except in limited circumstances detailed in Article V, Section 1.03(e) of the By-Laws.

asset custodians, settlement banks, letter of credit issuers, investment counterparties, and Liquidity Providers.

Liquidity Providers

Under the Policy, OCC maintains internal procedures outlining the minimum standards for Commercial Banks[10] and non-bank institutions acting as Liquidity Providers. OCC's Credit Risk Management and Treasury departments would be responsible for evaluating each Liquidity Provider against the minimum standards of creditworthiness and for its overall financial condition and operational capabilities as provided in the procedures. Because Liquidity Providers present both credit and liquidity risk to OCC, the due diligence around such institutions shall include a review of each lender's ability to perform their commitments as well as understand and manage their liquidity risks. Pursuant to the Policy, Credit Risk Management and Treasury shall document the results of its evaluation in a memorandum, including the Liquidity Provider's ability to meet relevant participation standards, and report those results to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, each of which shall have the authority to approve new and expanded relationships with Liquidity Providers.

FMUs

Under the Policy, OCC's maintains internal procedures outlining minimum standards for

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[10] Under the Policy, "Commercial Bank" is defined as a banking or depository institution that is not an operating arm of a Central Bank. Commercial bank relationships shall be governed by this Policy and all supporting bank-related procedures. Commercial Banks act as Liquidity Providers, asset custodians, settlement banks, letter of credit issuers, and investment counterparties on behalf of OCC.

FMUs. OCC's Business Operations and Credit Risk Management departments shall evaluate each FMU for its overall financial condition and operational capabilities as provided in the procedure. Pursuant to the Policy, before entering into any link arrangement, the Legal department shall assist the aforementioned business units to identify legal risks relating to rights and interests, collateral arrangements, settlement finality and netting arrangements, and financial and custody risks. The Business Operations, Credit Risk Management and Legal departments shall document the results of its evaluation in a memorandum, including the FMU's ability to meet relevant standards. All new and expanded FMU relationships shall be reviewed and approved by the Risk Committee and subsequently recommended for approval to the Board of Directors.

Measuring Counterparty Credit Risk

The CCRM Policy describes various ways in which OCC measures the credit risk posed by different Counterparties. With respect to Clearing Members, the CCRM Policy provides that OCC measures its credit exposures to Clearing Members under normal market conditions through the calculation of margin requirements and its credit exposures to Clearing Members under extreme but plausible conditions through stress testing and the calculation of Clearing Fund requirements, in accordance with applicable OCC policies. Margin, Clearing Fund and stress test results may be used by OCC's Financial Risk Management department ("FRM") to evaluate OCC's counterparty credit risk framework and inform Clearing Member surveillance processes.

With respect to Commercial Banks, Central Banks,[11] Liquidity Providers, and investment counterparties, OCC shall measure its credit exposures to these Counterparties by the balances generated from the various activities provided by these institutions in accordance with relevant internal procedures.

FMUs provide a range of services to OCC, including the Depository Trust Company ("DTC") as collateral custodian and provider of book order entry of securities transfers, Chicago Mercantile Exchange Inc. ("CME") and ICE Clear U.S. as cross-margin clearing organizations, and the National Securities Clearing Corporation ("NSCC") as a provider of securities settlement. Under the Policy, DTC credit exposures shall be measured by the collateral balances held and the value of securities lending/borrowing transactions facilitated. CME and ICE Clear U.S. credit exposures shall be measured by the projected margin impact in the event of suspension of a cross-margin program and, therefore, the absence of risk reducing positions cleared away from OCC. NSCC exposure shall be measured by the value of securities and cash to be settled in connection with the delivery obligations settled through NSCC.

Monitoring and Managing Counterparty Credit Risk

The CCRM Policy also describes the manner in which OCC monitors and manages credit risk from its Counterparties. Under the Policy, OCC's monitoring and management of such risks

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[11] Under the Policy, "Central Bank" is defined as a bank serving as a bank for both depository institutions and a government, a regulator for financial institutions, and/or a nation's money manager. Central Banks act as asset custodians on behalf of OCC, and OCC uses access to accounts and services at a Central Bank, when available and where determined to be practical by the Board of Directors, to enhance its management of liquidity risk. Due to the inherently low credit risk presented by Central Banks, only limited monitoring activities would be performed pursuant to relevant OCC procedures.

is comprised of "Watch Level Reporting" processes in conjunction with other tools including margin adjustments, internal credit ratings, risk examinations, and monitoring of tiered participation arrangements and dormant Counterparties.

Watch Level Reporting Overview

Under the Policy, Counterparties are monitored by OCC's FRM, Business Operations, and Treasury departments for ongoing compliance with the minimum participation standards described above to identify any trends that might signal the deterioration of a Counterparty's ability to timely meet its obligations. When these trends are identified, Credit Risk Management shall report on a Counterparty through OCC's Watch Level Reporting processes, which are described in further detail below. As a Counterparty approaches or no longer meets minimum standards, FRM's monitoring heightens and, in the case of Commercial Banks and Clearing Members, increasingly rigorous protective measures may be imposed to limit or eliminate OCC's credit exposure.

Pursuant to the Policy, the Watch Level Reporting process shall be administered by OCC's Management Committee, which maintains approval authority of Watch Level parameter changes. The Watch Level Reporting process provides each of the Executive Chairman, Chief Operating Officer and Chief Administrative Officer with authority to take action to protect OCC given the facts and circumstances of the exposure presented by a Clearing Member or Commercial Bank. Under the Policy, Credit Risk Management shall provide monthly internal reporting to FRM summarizing the circumstances relating to a violation, additional risks observed and any corrective measure taken by any Clearing Member, Commercial Bank, or

FMU at or above Watch Level II (described below); and monthly reporting to OCC's Credit and Liquidity Risk Working Group, Management Committee and the Risk Committee of any Clearing Member or Commercial Bank at or above Watch Level III (described below).

Clearing Member Watch Level Reporting and Bank Watch Level Reporting

Pursuant to the CCRM Policy, the Clearing Member Watch Level Reporting process and Bank Watch Level Reporting process shall support initial and on-going participation standards by allowing OCC's Credit Risk Management department, with the support of other FRM business units, Business Operations and Treasury, to detect business-related concerns and/or financial or operational deterioration of a Counterparty in order to protect OCC and its Clearing Members against the potential default of a Clearing Member or Commercial Bank. Pursuant to the Policy, the Clearing Member Watch Level Reporting process and Bank Watch Level Reporting process shall be organized into four-tiered surveillance structures.

1. **Watch Level I.** Watch Level I is the lowest tier of severity and shall be used to categorize Clearing Members and Commercial Banks presenting minimal to very low credit risk. This level of violation shall be identified but not reported.
2. **Watch Level II.** This tier shall be used to categorize Clearing Members and Commercial Banks presenting low to lower moderate credit risk. This level of violation shall be identified and reported to internal personnel pursuant to FRM procedures.
3. **Watch Level III.** This tier shall be used to categorize Clearing Members and Commercial Banks potentially presenting upper moderate to substantial credit risk. Violations in this tier may indicate a Clearing Member or Commercial Bank that is below

early warning participation thresholds and may soon become non-compliant with OCC's minimum participation standards, as specified in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and internal OCC procedures. This level of violation shall be identified and reported to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, who shall have the authority to approve the imposition or waiver of protective measures. The Risk Committee shall be informed of these violations on a monthly basis.

4. **Watch Level IV.** Watch Level IV is the highest tier of severity and shall be used to categorize Clearing Members and Commercial Banks potentially presenting high to very high credit risk with a heightened probability of default. Violations in this tier may indicate a Clearing Member or Commercial Bank may imminently become or has already become non-compliant with OCC's minimum participation standards, as specified in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and internal OCC procedures. This level of violation shall be identified and reported to OCC's Credit and Liquidity Risk Working Group, with subsequent reporting to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, who shall have the authority to approve the imposition or waiver of protective measures, including the option to restrict business of or suspend the Clearing Member or Commercial Bank. The Risk Committee shall be promptly informed of these violations and a meeting of the Risk Committee may occur to discuss the event.

In addition, under the Policy, a Clearing Member reporting (1) aggregate uncollateralized

stress test exposure under normal market conditions less (2) the sum of base expected shortfall and stress test charges as computed under OCC's margin methodology, exceeding 75% of the Clearing Member's excess net capital shall be identified and reported on Watch Level II. When this exposure exceeds 100% of net capital, a Clearing Member shall be identified and reported on Watch Level III and shall be subject to a margin call for the amount of exposure exceeding net capital. A margin call shall be the standard form of protective measures for position risk monitoring and shall not require officer approval or further prompt escalation. However, Clearing Members may be reported to the Executive Chairman, Chief Operating Officer or Chief Administrative officer for consideration of additional protective measures.

FMU Watch Level Reporting

The FMU Watch Level Reporting process allows Credit Risk Management, with the support of other FRM business units and Business Operations, to detect business-related concerns and/or financial or operational deterioration of a FMU. Pursuant to the CCRM Policy, the FMU Watch Level Reporting process is organized into a two-tiered surveillance structure.

1. **Watch Level I.** Watch Level I is the lowest tier of severity and shall be used to categorize FMUs presenting minimal to very low credit risk. This level of violation shall be identified but not reported.
2. **Watch Level II.** Watch Level II is the highest tier of severity and shall be used to categorize FMUs presenting low to lower moderate credit risk. This level of violation shall be identified and reported.

Other Tools for Monitoring and Managing Credit Risk

In addition to the Watch Level Reporting processes discussed above, the CCRM Policy discussed other tools and processes used by OCC to monitor and manage credit risks arising from its Counterparties. For example, in cases where ongoing monitoring of Clearing Members identifies circumstances impacting margin levels due to changing portfolio characteristics, market conditions, elevated Clearing Fund stress test results, upcoming holidays where trading is allowed but OCC is unable to call for additional margin deposits, and certain other situations, OCC shall have the authority to call for additional margin deposits or otherwise adjust margin requirements as further detailed in OCC's margin and Clearing Fund-related policies.

Under the Policy, OCC's Credit Risk Management department also maintains Internal Credit Ratings ("ICRs") which shall be incorporated into the Watch Level Reporting process and shall be designed to identify quarterly creditworthiness scores of Clearing Members and Commercial Banks. ICR reporting shall summarize the underlying cause of the ICR score, recent scoring trend and exposure introduced by a Clearing Member or Commercial Bank.

In addition, the Policy provides that Credit Risk Management shall perform examinations of the risk management frameworks, policies, procedures and practices of each Clearing Member no less than once in a three calendar year period focusing on the risks posed to OCC. For certain exams, Credit Risk Management may coordinate with external parties to realize operational efficiencies for both the Clearing Member and OCC.

The CCRM Policy also provides that OCC's Counterparty monitoring includes managing the material risks that arise from indirect participants through tiered participation arrangements. In particular, Credit Risk Management, supported by other FRM business units and Business

Operations, shall monitor the material risks that arise from indirect participants through tiered participation arrangements. Credit Risk Management (or other FRM business units, as appropriate) shall identify these tiered participation arrangements through standard monitoring processes when they present elevated risk to the Clearing Member or OCC. Furthermore, Clearing Member risk examinations shall seek to understand how direct participants identify, measure and manage the risks posed to OCC from indirect participants. In this regard, the CCRM Policy is designed to promote compliance with Rule 17Ad-22(e)(19) by addressing the material risks that may arise from indirect participants.[12]

Additionally, under the CCRM Policy, OCC shall monitor Clearing Members, Commercial Banks and investment counterparties during prolonged periods of inactivity, and Clearing Members shall be allowed to voluntarily enter a dormant state in order to reduce credit risk originating from unexpected trading activity. A dormant Clearing Member shall continuously adhere to all operational and financial standards and may reactivate its membership after submitting to an operational and financial review. OCC shall maintain sole discretion to terminate inactive Commercial Banks and investment counterparties in order to reduce credit risk.

Counterparty Credit Risk Termination

Finally, the CCRM Policy addresses the voluntary off-boarding of Counterparties. Under the Policy, voluntary off-boarding shall be performed in a manner designed to wind down

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12 17 CFR 240.17Ad-22(e)(19).

all credit exposures in an orderly fashion before a relationship is terminated.

B. Statutory Basis

Section 17A(b)(3)(F) of the Act[13] requires, among other things, that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible and, in general, to protect investors and the public interest. Through each of its respective sections, the CCRM Policy provides a framework that is designed to enable OCC to identify, evaluate, measure, monitor and manage potential credit risks posed by its Counterparties. In identifying these credit risks, the CCRM Policy details various ways in which OCC may be exposed to such risks. In evaluating counterparty credit risks, the CCRM Policy states that OCC evaluates each Counterparty against objective and risk-based minimum standards of creditworthiness, overall financial condition and operational capabilities. The Policy also provides detail on how OCC structures its custodial relationship to ensure it has prompt access to its own assets and Clearing Members' assets. In measuring counterparty credit risk, the CCRM Policy describes various ways in which OCC measures credit risk posed by different Counterparties, as well as the three main tools for managing credit risk posed by Clearing Members. In monitoring and managing counterparty credit risk, the CCRM Policy specifies the steps taken by OCC's internal units to monitor Counterparties, including by conducting examinations of Clearing Members' risk management frameworks and performing monthly Watch Level Reporting. The CCRM Policy's promotion of each aforementioned

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13 15 U.S.C. 78q-1(b)(3)(F).

activity ultimately inures to the protection of investors and the public interest, as well as the safeguarding of securities and funds in OCC's custody or control[14] in a manner consistent with Section 17A(b)(3)(F) of the Act.[15]

OCC also believes that that the CCRM Policy is consistent with several requirements under Rule 17Ad-22. For example, Rules 17Ad-22(e)(3) and (e)(4)[16] require a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, maintain a sound risk management framework for addressing credit risk, to effectively identify, measure, monitor, and manage credit risks that arise in or are borne by the covered clearing agency, including its credit exposures to participants and those arising from its payment, clearing, and settlement processes. OCC believes that the CCRM Policy is consistent with Rules 17Ad-22(e)(3) and (4)[17] because the CCRM Policy describes OCC's framework for comprehensively managing its credit risks. Specifically, the CCRM Policy describes the various processes by which OCC identifies, measures, monitors, and manages its credit exposures to participants and exposures arising from its payment, clearing, and settlement processes, including the Counterparty access and participation standards used by OCC to evaluate potential Counterparties, OCC's processes for measuring its Counterparty

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14 These activities, in turn, help ensure that OCC remains capable of continuing its operations and services in a manner that promotes the prompt and accurate clearance and settlement of securities transactions.

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

16 17 CFR 240.17Ad-22(e)(3) and (4).

17 Id.

exposures, and OCC's processes for monitoring and managing Counterparty exposures (particularly through the use of its Watch Level Reporting processes).

In addition, Rule 17Ad-22(e)(16)[18] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, safeguard the covered clearing agency's own and its participants' assets and minimize the risk of loss and delay in access to these assets. OCC believes that the access and participation requirements for Commercial and Central Banks outlined in the CCRM Policy enable it to appropriately evaluate each bank against relevant minimum standards of creditworthiness and for its overall financial condition and operational capabilities, and are therefore designed to minimize the risk of loss and delay in access to OCC's assets and its participants' assets in a manner consistent with Rule 17Ad-22(e)(16).[19]

Rule 17Ad-22(e)(18)[20] further requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, establish objective, risk-based, and publicly disclosed criteria for participation, which permit fair and open access and require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency, and monitor compliance with such participation requirements on an ongoing basis. OCC

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18 17 CFR 240.17Ad-22(e)(16).

19 Id.

20 17 CFR 240.17Ad-22(e)(18).

believes the CCRM Policy promotes compliance with Rule 17Ad-22(e)(18)[21] by ensuring that OCC has objective, risk-based and publicly disclosed criteria for participation requiring Clearing Members to have sufficient financial resources to meet their obligations to OCC. Moreover, the Policy outlines the Watch Level Reporting process used by OCC to monitor compliance with such participation requirements on an ongoing basis.

Rule 17Ad-22(e)(19)[22] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify, monitor, and manage the material risks to the covered clearing agency arising from arrangements in which firms that are indirect participants in the covered clearing agency rely on the services provided by direct participants to access the covered clearing agency's payment, clearing, or settlement facilities. OCC believes the Policy is designed to comply with Rule 17Ad-22(e)(19)[23] because it outlines the process by which OCC identifies and monitors the material risks arising from indirect participants through tiered participation arrangements, including through the use of risk examinations of its Clearing Members.

Finally, Rule 17Ad-22(e)(20)[24] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, identify, monitor, and manage risks related to any link the covered clearing agency

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21 Id.

22 17 CFR 240.17Ad-22(e)(19).

23 Id.

24 17 CFR 240.17Ad-22(e)(20).

establishes with one or more other clearing agencies or FMUs. OCC believes that the Policy promotes compliance with Rule 17Ad-22(e)(20)[25] because it outlines the standards OCC uses evaluate FMU Counterparties prior to entering into any link arrangement (including the evaluations OCC would perform relating to rights and interests, collateral arrangements, settlement finality and netting arrangements, and financial and custody risks that may arise due to such link arrangement) and the processes by which OCC measures and monitors the risks arising from such FMU Counterparties (including its FMU Watch Level Reporting process).

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

Section 17A(b)(3)(I) of the Act[26] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. OCC does not believe that the proposed rule change would impact or impose any burden on competition. The proposed rule change addresses the framework by which OCC manages counterparty credit risk arising from its business, as set forth in the CCRM Policy. Because any individual Counterparty under the CCRM Policy is equally subject to the aspects of the counterparty credit risk framework that apply to it based on the type of Counterparty that it represents (i.e., direct and indirect participants, Liquidity Providers, asset custodians, settlement banks, letter of credit issuers, investment counterparties, clearing agencies and FMUs) and the

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25 Id.

26 15 U.S.C. 78q-1(b)(3)(I).

related counterparty credit risks that are posed to OCC by that type of Counterparty the proposed rule change would not provide any Counterparty with a competitive advantage over any other similar Counterparty. Further, the proposed rule change would not affect Clearing Members' or other Counterparties' existing access to OCC's services or impose any new or different direct burdens on Clearing Members or other Counterparties.

For the foregoing reasons, OCC believes that the proposed rule change is in the public interest, would be consistent with the requirements of the Act applicable to clearing agencies, and would not impact or impose a 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 none have been received.

Item 6. Extension of Time Period for Commission Action

Not applicable.

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)

Not applicable.

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

Not applicable.

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

Not applicable.

Item 11. Exhibits

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

Exhibit 5 Counterparty Credit Risk Management Policy

CONFIDENTIAL TREATMENT IS REQUESTED FOR EXHIBIT 5

PURSUANT TO SEC RULE 24b-2

SIGNATURES

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:_____
Justin W. Byrne
Vice President, Regulatory Filings

EXHIBIT 1A

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-[_____]; File No. SR-OCC-2017-009)

October 12, 2017

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change Related to The Options Clearing Corporation's Counterparty Credit Risk Management Policy

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on October 12, 2017, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared primarily by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency's Statement of the Terms of Substance of the Proposed Rule Change

This proposed rule change by OCC would formalize OCC's Counterparty Credit Risk Management Policy ("CCRM Policy" or "Policy"), which promotes compliance with multiple requirements applicable to OCC under Rule 17Ad-22, including Rules 17Ad-22(e)(3) concerning frameworks for the comprehensive management of risks, (e)(4) concerning credit risk management, (e)(16) concerning the safeguarding of assets, (e)(18) concerning risk-based participation criteria, (e)(19) concerning risks form indirect

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

2 17 CFR 240.19b-4.

participants, and (e)(20) concerning linkages.[3] The CCRM Policy is included as confidential Exhibit 5.

The proposed rule change does not require any changes to the text of OCC's By-Laws or Rules. All terms with initial capitalization that are not otherwise defined herein have the same meaning as set forth in the OCC By-Laws and Rules.[4]

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

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

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

(1) Purpose

Background

As a central counterparty providing clearance, settlement, and risk management services, OCC is exposed to and must manage a range of risks, including credit risk. The purpose of the CCRM Policy is to outline OCC's overall approach to identify, measure, monitor, and manage its exposures to direct and indirect participants, Liquidity

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3 17 CFR 240.17Ad-22(e)(3), (4), (16), (18), (19), and (20).

4 OCC's By-Laws and Rules can be found on OCC's public website: http://optionsclearing.com/about/publications/bylaws.jsp.

Providers,[5] asset custodians, settlement banks, letter of credit issuers, investment counterparties, other clearing agencies, and financial market utilities ("FMUs")[6] (each a "Counterparty") arising from its payment, clearing, and settlement processes. OCC notes that the CCRM Policy is part of a broader framework used by OCC to manage credit risk, including OCC's By-Laws, Rules, and other policies and procedures that are designed collectively to ensure that OCC appropriately manages counterparty credit risk and to promote compliance with Rule 17Ad-22.[7]

The CCRM Policy would be maintained by OCC to promote compliance with a number of rules adopted under Section 17A of the Securities Exchange Act of 1934, as amended ("Act"),[8] and the Payment, Clearing, and Settlement Supervision Act of 2010 ("Clearing Supervision Act").[9] In particular, the Policy is designed to address certain aspects of Rules 17Ad-22(e)(3) concerning frameworks for the comprehensive management of risks, (e)(4) concerning credit risk management, (e)(16) concerning the safeguarding of assets, (e)(18) concerning risk-based participation criteria, (e)(19) concerning risks form indirect participants, and (e)(20) concerning linkages.[10]

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5 Under the CCRM Policy, "Liquidity Provider" is defined as a Commercial Bank or a non-banking institution – generally a pension fund – that provides a committed liquidity facility to OCC.

6 Under the CCRM Policy, "Financial Market Utility" is defined as a derivatives clearing organization partnering with OCC to provide a cross-margin program; a clearing agency providing settlement services of securities arising from the exercise, assignment or maturity of options or futures; or the Depository providing book-entry securities transfers and asset custodian services.

7 17 CFR 240.17Ad-22.

8 15 U.S.C. 78q-1.

9 12 U.S.C. 5461 et. seq.

10 17 CFR 240.17Ad-22(e)(3), (4), (16), (18), (19), and (20).

Counterparty Credit Risk Management Policy

OCC's CCRM Policy outlines the key components of OCC's framework for identifying, measuring, monitoring, and managing OCC's exposures to its Counterparties. This framework includes: (1) the identification of credit risk, (2) Counterparty access and participation standards, (3) the measurement of its Counterparty exposures, (4) the monitoring and managing of Counterparty exposures, and (5) voluntary termination of Counterparty relationships. Each of these components is described in more detail below.

Identification of Credit Risk

The CCRM Policy identifies various ways in which credit risk originates from the failure of a Counterparty to perform. With respect to a Clearing Member, the CCRM Policy details a number of different ways in which OCC may be exposed to credit risk. This includes the potential failure of a Clearing Member to pay for purchased options, to meet expiration-related settlement obligations, or to make certain mark-to-market variation payments or initial margin deposits. It also includes the potential insufficiency of a defaulting Clearing Member's margin and Clearing Fund deposits in a liquidation scenario. Other sources of credit risk identified in the CCRM Policy include the inability of OCC to access collateral (e.g., cash or securities) from a custodian or investment counterparty that is needed to facilitate a liquidation, or a failure by an issuer of a letter of credit to honor its corresponding obligations. The CCRM Policy also identifies that certain relationships with other FMUs, such as cross-margining programs and cash market settlement services, represent critical linkages that may present certain degrees of credit exposure based on the terms and design of the linkage. The CCRM Policy also

notes that OCC may face additional risks from Counterparties, such as the potential failure of a Liquidity Provider to honor a borrowing request.

Counterparty Access and Participation Standards

Under the CCRM Policy, OCC's management of Counterparty credit risks begins with an initial evaluation process intended to ascertain that Counterparties meet certain minimum financial and operational standards and are considered as having a low probability of defaulting on their obligations prior to engaging or effecting any new transactions or expansion of business with OCC. To accomplish this objective, OCC shall evaluate each Counterparty against established minimum standards of creditworthiness, overall financial condition, and operational capabilities. Pursuant to the Policy, the standards used to evaluate Counterparties shall be objective, risk-based, and publicly-disclosed in order to permit fair and open access. These standards shall be developed independently for Clearing Members, Commercial and Central Banks, investment counterparties, Liquidity Providers and FMUs, accounting for differences in their regulatory reporting and overall business operations.

Clearing Membership Standards

OCC's minimum participation standards for Clearing Member are found in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and other publicly-disclosed supplemental documentation (together, "Participation Standards Documentation"). Under the Policy, OCC's Credit Risk Management and Member Services departments shall evaluate each Clearing Member applicant against the minimum standards of creditworthiness and for its overall financial condition and operational capabilities as provided in the Participation Standards Documentation. Such

evaluation shall also consider the Counterparty's aggregation of exposure on an individual and related-entities level, as applicable, as well as any material exposure that may arise from tiered participation arrangements. The Credit Risk Management and Member Services departments shall document the results of this evaluation in a memorandum, including the Clearing Member applicant's ability to meet relevant participation standards, and report those results to OCC's Executive Chairman, Chief Operating Officer or Chief Administrative Officer for review and approval, where appropriate, or for recommendation to the Risk Committee or Board of Directors.[11]

Commercial and Central Banks

OCC's minimum standards for asset custodians, settlement banks, letter of credit issuers and investment counterparties are found in OCC Rule 604 and relevant OCC procedures. The Credit Risk Management department shall coordinate with various departments (such as Collateral Services or Treasury) to evaluate each bank against the minimum standards of creditworthiness and for its overall financial condition and

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[11] Pursuant to Article V, Section 2 of the By-Laws, the Executive Chairman, Chief Operating Officer and Chief Administrative Officer each have delegated authority to approve Clearing Member applicants provided that (1) there is no recommendation to impose additional membership criteria in accordance with Article V of the By-Laws and (2) the Risk Committee is given not less than five days to determine the application should be reviewed at a meeting of the Risk Committee. Pursuant to Interpretation and Policy .06 to Article V, Section 1 of the By-Laws, the Risk Committee has the authority to impose additional requirements on Clearing Member applicants, such as increased capital or margin requirements as well as restrictions on clearing activities. The Risk Committee also has the authority to approve waivers of certain clearing membership requirements under Article V, Section 1 of the By-Laws. Approvals of a Clearing Member business expansion by the Executive Chairman, Chief Operating Officer or Chief Administrative Officer are subsequently presented to the Risk Committee for ratification, except in limited circumstances detailed in Article V, Section 1.03(e) of the By-Laws.

operational capabilities as provided in OCC Rule 604 and related OCC procedures. Such evaluation shall also consider the Counterparty's aggregation of exposure on an individual and related-entities level, as applicable, as well as whether OCC would be able to structure its custodial relationships in a manner that allows prompt access to its own and its Clearing Members' assets. The latter shall include holding assets at supervised and regulated institutions that adhere to generally accepted accounting practices, maintain safekeeping procedures, and have internal controls that fully protect these assets. Under the Policy, Credit Risk Management and either the Collateral Services or Treasury department, as applicable, shall document the results of its evaluation in a memorandum, including the bank's ability to meet relevant participation standards, and report those results to OCC's Executive Chairman, Chief Operating Officer or Chief Administrative Officer, each of which shall have the authority to approve new and expanded relationships with asset custodians, settlement banks, letter of credit issuers, investment counterparties, and Liquidity Providers.

Liquidity Providers

Under the Policy, OCC maintains internal procedures outlining the minimum standards for Commercial Banks[12] and non-bank institutions acting as Liquidity Providers. OCC's Credit Risk Management and Treasury departments would be responsible for evaluating each Liquidity Provider against the minimum standards of

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12 Under the Policy, "Commercial Bank" is defined as a banking or depository institution that is not an operating arm of a Central Bank. Commercial bank relationships shall be governed by this Policy and all supporting bank-related procedures. Commercial Banks act as Liquidity Providers, asset custodians, settlement banks, letter of credit issuers, and investment counterparties on behalf of OCC.

creditworthiness and for its overall financial condition and operational capabilities as provided in the procedures. Because Liquidity Providers present both credit and liquidity risk to OCC, the due diligence around such institutions shall include a review of each lender's ability to perform their commitments as well as understand and manage their liquidity risks. Pursuant to the Policy, Credit Risk Management and Treasury shall document the results of its evaluation in a memorandum, including the Liquidity Provider's ability to meet relevant participation standards, and report those results to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, each of which shall have the authority to approve new and expanded relationships with Liquidity Providers.

FMUs

Under the Policy, OCC's maintains internal procedures outlining minimum standards for FMUs. OCC's Business Operations and Credit Risk Management departments shall evaluate each FMU for its overall financial condition and operational capabilities as provided in the procedure. Pursuant to the Policy, before entering into any link arrangement, the Legal department shall assist the aforementioned business units to identify legal risks relating to rights and interests, collateral arrangements, settlement finality and netting arrangements, and financial and custody risks. The Business Operations, Credit Risk Management and Legal departments shall document the results of its evaluation in a memorandum, including the FMU's ability to meet relevant standards. All new and expanded FMU relationships shall be reviewed and approved by the Risk Committee and subsequently recommended for approval to the Board of Directors.

Measuring Counterparty Credit Risk

The CCRM Policy describes various ways in which OCC measures the credit risk posed by different Counterparties. With respect to Clearing Members, the CCRM Policy provides that OCC measures its credit exposures to Clearing Members under normal market conditions through the calculation of margin requirements and its credit exposures to Clearing Members under extreme but plausible conditions through stress testing and the calculation of Clearing Fund requirements, in accordance with applicable OCC policies. Margin, Clearing Fund and stress test results may be used by OCC's Financial Risk Management department ("FRM") to evaluate OCC's counterparty credit risk framework and inform Clearing Member surveillance processes.

With respect to Commercial Banks, Central Banks,[13] Liquidity Providers, and investment counterparties, OCC shall measure its credit exposures to these Counterparties by the balances generated from the various activities provided by these institutions in accordance with relevant internal procedures.

FMUs provide a range of services to OCC, including the Depository Trust Company ("DTC") as collateral custodian and provider of book order entry of securities transfers, Chicago Mercantile Exchange Inc. ("CME") and ICE Clear U.S. as cross-margin clearing organizations, and the National Securities Clearing Corporation

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13 Under the Policy, "Central Bank" is defined as a bank serving as a bank for both depository institutions and a government, a regulator for financial institutions, and/or a nation's money manager. Central Banks act as asset custodians on behalf of OCC, and OCC uses access to accounts and services at a Central Bank, when available and where determined to be practical by the Board of Directors, to enhance its management of liquidity risk. Due to the inherently low credit risk presented by Central Banks, only limited monitoring activities would be performed pursuant to relevant OCC procedures.

("NSCC") as a provider of securities settlement. Under the Policy, DTC credit exposures shall be measured by the collateral balances held and the value of securities lending/borrowing transactions facilitated. CME and ICE Clear U.S. credit exposures shall be measured by the projected margin impact in the event of suspension of a cross-margin program and, therefore, the absence of risk reducing positions cleared away from OCC. NSCC exposure shall be measured by the value of securities and cash to be settled in connection with the delivery obligations settled through NSCC.

Monitoring and Managing Counterparty Credit Risk

The CCRM Policy also describes the manner in which OCC monitors and manages credit risk from its Counterparties. Under the Policy, OCC's monitoring and management of such risks is comprised of "Watch Level Reporting" processes in conjunction with other tools including margin adjustments, internal credit ratings, risk examinations, and monitoring of tiered participation arrangements and dormant Counterparties.

Watch Level Reporting Overview

Under the Policy, Counterparties are monitored by OCC's FRM, Business Operations, and Treasury departments for ongoing compliance with the minimum participation standards described above to identify any trends that might signal the deterioration of a Counterparty's ability to timely meet its obligations. When these trends are identified, Credit Risk Management shall report on a Counterparty through OCC's Watch Level Reporting processes, which are described in further detail below. As a Counterparty approaches or no longer meets minimum standards, FRM's monitoring heightens and, in the case of Commercial Banks and Clearing Members, increasingly

rigorous protective measures may be imposed to limit or eliminate OCC's credit exposure.

Pursuant to the Policy, the Watch Level Reporting process shall be administered by OCC's Management Committee, which maintains approval authority of Watch Level parameter changes. The Watch Level Reporting process provides each of the Executive Chairman, Chief Operating Officer and Chief Administrative Officer with authority to take action to protect OCC given the facts and circumstances of the exposure presented by a Clearing Member or Commercial Bank. Under the Policy, Credit Risk Management shall provide monthly internal reporting to FRM summarizing the circumstances relating to a violation, additional risks observed and any corrective measure taken by any Clearing Member, Commercial Bank, or FMU at or above Watch Level II (described below); and monthly reporting to OCC's Credit and Liquidity Risk Working Group, Management Committee and the Risk Committee of any Clearing Member or Commercial Bank at or above Watch Level III (described below).

Clearing Member Watch Level Reporting and Bank Watch Level Reporting

Pursuant to the CCRM Policy, the Clearing Member Watch Level Reporting process and Bank Watch Level Reporting process shall support initial and on-going participation standards by allowing OCC's Credit Risk Management department, with the support of other FRM business units, Business Operations and Treasury, to detect business-related concerns and/or financial or operational deterioration of a Counterparty in order to protect OCC and its Clearing Members against the potential default of a Clearing Member or Commercial Bank. Pursuant to the Policy, the Clearing Member

Watch Level Reporting process and Bank Watch Level Reporting process shall be organized into four-tiered surveillance structures.

1. **Watch Level I.** Watch Level I is the lowest tier of severity and shall be used to categorize Clearing Members and Commercial Banks presenting minimal to very low credit risk. This level of violation shall be identified but not reported.
2. **Watch Level II.** This tier shall be used to categorize Clearing Members and Commercial Banks presenting low to lower moderate credit risk. This level of violation shall be identified and reported to internal personnel pursuant to FRM procedures.
3. **Watch Level III.** This tier shall be used to categorize Clearing Members and Commercial Banks potentially presenting upper moderate to substantial credit risk. Violations in this tier may indicate a Clearing Member or Commercial Bank that is below early warning participation thresholds and may soon become non-compliant with OCC's minimum participation standards, as specified in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and internal OCC procedures. This level of violation shall be identified and reported to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, who shall have the authority to approve the imposition or waiver of protective measures. The Risk Committee shall be informed of these violations on a monthly basis.
4. **Watch Level IV.** Watch Level IV is the highest tier of severity and shall be used to categorize Clearing Members and Commercial Banks potentially presenting high to very high credit risk with a heightened probability of default. Violations

in this tier may indicate a Clearing Member or Commercial Bank may imminently become or has already become non-compliant with OCC's minimum participation standards, as specified in Article V of OCC's By-Laws, Chapters II and III of OCC's Rules, and internal OCC procedures. This level of violation shall be identified and reported to OCC's Credit and Liquidity Risk Working Group, with subsequent reporting to the Executive Chairman, Chief Operating Officer or Chief Administrative Officer, who shall have the authority to approve the imposition or waiver of protective measures, including the option to restrict business of or suspend the Clearing Member or Commercial Bank. The Risk Committee shall be promptly informed of these violations and a meeting of the Risk Committee may occur to discuss the event.

In addition, under the Policy, a Clearing Member reporting (1) aggregate uncollateralized stress test exposure under normal market conditions less (2) the sum of base expected shortfall and stress test charges as computed under OCC's margin methodology, exceeding 75% of the Clearing Member's excess net capital shall be identified and reported on Watch Level II. When this exposure exceeds 100% of net capital, a Clearing Member shall be identified and reported on Watch Level III and shall be subject to a margin call for the amount of exposure exceeding net capital. A margin call shall be the standard form of protective measures for position risk monitoring and shall not require officer approval or further prompt escalation. However, Clearing Members may be reported to the Executive Chairman, Chief Operating Officer or Chief Administrative officer for consideration of additional protective measures.

<u>FMU Watch Level Reporting</u>

The FMU Watch Level Reporting process allows Credit Risk Management, with the support of other FRM business units and Business Operations, to detect business-related concerns and/or financial or operational deterioration of a FMU. Pursuant to the CCRM Policy, the FMU Watch Level Reporting process is organized into a two-tiered surveillance structure.

1. **Watch Level I.** Watch Level I is the lowest tier of severity and shall be used to categorize FMUs presenting minimal to very low credit risk. This level of violation shall be identified but not reported.
2. **Watch Level II.** Watch Level II is the highest tier of severity and shall be used to categorize FMUs presenting low to lower moderate credit risk. This level of violation shall be identified and reported.

Other Tools for Monitoring and Managing Credit Risk

In addition to the Watch Level Reporting processes discussed above, the CCRM Policy discussed other tools and processes used by OCC to monitor and manage credit risks arising from its Counterparties. For example, in cases where ongoing monitoring of Clearing Members identifies circumstances impacting margin levels due to changing portfolio characteristics, market conditions, elevated Clearing Fund stress test results, upcoming holidays where trading is allowed but OCC is unable to call for additional margin deposits, and certain other situations, OCC shall have the authority to call for additional margin deposits or otherwise adjust margin requirements as further detailed in OCC's margin and Clearing Fund-related policies.

Under the Policy, OCC's Credit Risk Management department also maintains Internal Credit Ratings ("ICRs") which shall be incorporated into the Watch Level

Reporting process and shall be designed to identify quarterly creditworthiness scores of Clearing Members and Commercial Banks. ICR reporting shall summarize the underlying cause of the ICR score, recent scoring trend and exposure introduced by a Clearing Member or Commercial Bank.

In addition, the Policy provides that Credit Risk Management shall perform examinations of the risk management frameworks, policies, procedures and practices of each Clearing Member no less than once in a three calendar year period focusing on the risks posed to OCC. For certain exams, Credit Risk Management may coordinate with external parties to realize operational efficiencies for both the Clearing Member and OCC.

The CCRM Policy also provides that OCC's Counterparty monitoring includes managing the material risks that arise from indirect participants through tiered participation arrangements. In particular, Credit Risk Management, supported by other FRM business units and Business Operations, shall monitor the material risks that arise from indirect participants through tiered participation arrangements. Credit Risk Management (or other FRM business units, as appropriate) shall identify these tiered participation arrangements through standard monitoring processes when they present elevated risk to the Clearing Member or OCC. Furthermore, Clearing Member risk examinations shall seek to understand how direct participants identify, measure and manage the risks posed to OCC from indirect participants. In this regard, the CCRM Policy is designed to promote compliance with Rule 17Ad-22(e)(19) by addressing the material risks that may arise from indirect participants.[14]

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14 17 CFR 240.17Ad-22(e)(19).

Additionally, under the CCRM Policy, OCC shall monitor Clearing Members, Commercial Banks and investment counterparties during prolonged periods of inactivity, and Clearing Members shall be allowed to voluntarily enter a dormant state in order to reduce credit risk originating from unexpected trading activity. A dormant Clearing Member shall continuously adhere to all operational and financial standards and may reactivate its membership after submitting to an operational and financial review. OCC shall maintain sole discretion to terminate inactive Commercial Banks and investment counterparties in order to reduce credit risk.

Counterparty Credit Risk Termination

Finally, the CCRM Policy addresses the voluntary off-boarding of Counterparties. Under the Policy, voluntary off-boarding shall be performed in a manner designed to wind down all credit exposures in an orderly fashion before a relationship is terminated.[15]

(2) Statutory Basis

Section 17A(b)(3)(F) of the Act[16] requires, among other things, that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible and, in general, to protect investors and the public interest. Through each of its respective sections, the CCRM Policy provides a framework that is designed to enable OCC to identify, evaluate, measure, monitor and manage potential credit risks posed by its Counterparties. In identifying these credit risks, the CCRM Policy details various ways in which OCC may be exposed to such risks. In evaluating counterparty credit risks, the CCRM Policy states that OCC

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15 17 CFR 240.17Ad-22(e)(19).

16 15 U.S.C. 78q-1(b)(3)(F).

evaluates each Counterparty against objective and risk-based minimum standards of creditworthiness, overall financial condition and operational capabilities. The Policy also provides detail on how OCC structures its custodial relationship to ensure it has prompt access to its own assets and Clearing Members' assets. In measuring counterparty credit risk, the CCRM Policy describes various ways in which OCC measures credit risk posed by different Counterparties, as well as the three main tools for managing credit risk posed by Clearing Members. In monitoring and managing counterparty credit risk, the CCRM Policy specifies the steps taken by OCC's internal units to monitor Counterparties, including by conducting examinations of Clearing Members' risk management frameworks and performing monthly Watch Level Reporting. The CCRM Policy's promotion of each aforementioned activity ultimately inures to the protection of investors and the public interest, as well as the safeguarding of securities and funds in OCC's custody or control[17] in a manner consistent with Section 17A(b)(3)(F) of the Act.[18]

OCC also believes that that the CCRM Policy is consistent with several requirements under Rule 17Ad-22. For example, Rules 17Ad-22(e)(3) and (e)(4)[19] require a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, maintain a sound risk management framework for addressing credit risk, to effectively identify, measure, monitor, and manage credit risks that arise in or are borne by the covered clearing

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17 These activities, in turn, help ensure that OCC remains capable of continuing its operations and services in a manner that promotes the prompt and accurate clearance and settlement of securities transactions.

18 15 U.S.C. 78q-1(b)(3)(F).

19 17 CFR 240.17Ad-22(e)(3) and (4).

agency, including its credit exposures to participants and those arising from its payment, clearing, and settlement processes. OCC believes that the CCRM Policy is consistent with Rules 17Ad-22(e)(3) and (4)[20] because the CCRM Policy describes OCC's framework for comprehensively managing its credit risks. Specifically, the CCRM Policy describes the various processes by which OCC identifies, measures, monitors, and manages its credit exposures to participants and exposures arising from its payment, clearing, and settlement processes, including the Counterparty access and participation standards used by OCC to evaluate potential Counterparties, OCC's processes for measuring its Counterparty exposures, and OCC's processes for monitoring and managing Counterparty exposures (particularly through the use of its Watch Level Reporting processes).

In addition, Rule 17Ad-22(e)(16)[21] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, safeguard the covered clearing agency's own and its participants' assets and minimize the risk of loss and delay in access to these assets. OCC believes that the access and participation requirements for Commercial and Central Banks outlined in the CCRM Policy enable it to appropriately evaluate each bank against relevant minimum standards of creditworthiness and for its overall financial condition and operational capabilities, and are therefore designed to minimize the risk of loss and

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20 Id.

21 17 CFR 240.17Ad-22(e)(16).

delay in access to OCC's assets and its participants' assets in a manner consistent with Rule 17Ad-22(e)(16).[22]

Rule 17Ad-22(e)(18)[23] further requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, establish objective, risk-based, and publicly disclosed criteria for participation, which permit fair and open access and require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency, and monitor compliance with such participation requirements on an ongoing basis. OCC believes the CCRM Policy promotes compliance with Rule 17Ad-22(e)(18)[24] by ensuring that OCC has objective, risk-based and publicly disclosed criteria for participation requiring Clearing Members to have sufficient financial resources to meet their obligations to OCC. Moreover, the Policy outlines the Watch Level Reporting process used by OCC to monitor compliance with such participation requirements on an ongoing basis.

Rule 17Ad-22(e)(19)[25] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify, monitor, and manage the material risks to the covered clearing agency arising from arrangements in which firms that are indirect participants in the covered clearing agency rely on the services provided by direct participants to access the covered clearing agency's payment, clearing, or settlement facilities. OCC believes the Policy is designed

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22 Id.

23 17 CFR 240.17Ad-22(e)(18).

24 Id.

25 17 CFR 240.17Ad-22(e)(19).

to comply with Rule 17Ad-22(e)(19)[26] because it outlines the process by which OCC identifies and monitors the material risks arising from indirect participants through tiered participation arrangements, including through the use of risk examinations of its Clearing Members.

Finally, Rule 17Ad-22(e)(20)[27] requires a covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to, among other things, identify, monitor, and manage risks related to any link the covered clearing agency establishes with one or more other clearing agencies or FMUs. OCC believes that the Policy promotes compliance with Rule 17Ad-22(e)(20)[28] because it outlines the standards OCC uses evaluate FMU Counterparties prior to entering into any link arrangement (including the evaluations OCC would perform relating to rights and interests, collateral arrangements, settlement finality and netting arrangements, and financial and custody risks that may arise due to such link arrangement) and the processes by which OCC measures and monitors the risks arising from such FMU Counterparties (including its FMU Watch Level Reporting process).

The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended.

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

Section 17A(b)(3)(I) of the Act[29] requires that the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the

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26 Id.

27 17 CFR 240.17Ad-22(e)(20).

28 Id.

29 15 U.S.C. 78q-1(b)(3)(I).

purposes of the Act. OCC does not believe that the proposed rule change would impact or impose any burden on competition. The proposed rule change addresses the framework by which OCC manages counterparty credit risk arising from its business, as set forth in the CCRM Policy. Because any individual Counterparty under the CCRM Policy is equally subject to the aspects of the counterparty credit risk framework that apply to it based on the type of Counterparty that it represents (i.e., direct and indirect participants, Liquidity Providers, asset custodians, settlement banks, letter of credit issuers, investment counterparties, clearing agencies and FMUs) and the related counterparty credit risks that are posed to OCC by that type of Counterparty the proposed rule change would not provide any Counterparty with a competitive advantage over any other similar Counterparty. Further, the proposed rule change would not affect Clearing Members' or other Counterparties' existing access to OCC's services or impose any new or different direct burdens on Clearing Members or other Counterparties.

For the foregoing reasons, OCC believes that the proposed rule change is in the public interest, would be consistent with the requirements of the Act applicable to clearing agencies, and would not impact or impose a burden on competition.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

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

III. Date of Effectiveness of the Proposed Rule Change 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 the proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

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

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-OCC-2017-009 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-OCC-2017-009. 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 that are filed

with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for 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 such filing also will be available for inspection and copying at the principal office of OCC and on OCC's website at http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_17_009.pdf.

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-2017-009 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.[30]

Robert W. Errett
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:_____

30 17 CFR 200.30-3(a)(12).

EXHIBIT 5

[Redacted Pursuant to Rule 24b-2]

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