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Executive Vice President
General Counsel and Secretary

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Via Email (regs.comments@federalreserve.gov)

Robert deV. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Re: Docket No. R-1455: Proposed Amendments to Federal Reserve Board of Governors Regulation HH (RIN No. 7100-AD-94)

Dear Mr. deV. Frierson:

This letter is submitted by The Options Clearing Corporation (“OCC”) in response to the recent publication by the Board of Governors of the Federal Reserve System (the “Board”) of proposed amendments¹ to Regulation HH² implementing Section 806(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”).³ The Proposed Rules would authorize Federal Reserve Banks (“FRBs”) to establish and maintain accounts (“Accounts”) for, and provide services (“Services”) through those accounts to, financial market utilities that have been designated as systemically important (each, a “SIFMU”) by the Financial Stability Oversight Council (the “Council”). OCC supports adoption of the Proposed Rules, and we appreciate the opportunity to provide the following comments.

Background

Founded in 1973, OCC is currently the world’s largest equity derivatives clearing organization. OCC clears securities options, security futures and other securities contracts subject to the jurisdiction of the Securities and Exchange Commission (“SEC”), and commodity futures and options on commodity futures subject to the jurisdiction of the Commodity Futures Trading Commission (“CFTC”). OCC is registered with the SEC as a clearing agency pursuant to

¹ Financial Market Utilities, Notice of Proposed Rulemaking, 78 Fed. Reg. 14024 (March 4, 2013) (the “Proposed Rules”).

² 12 CFR Part 234.

³ Public Law 111–203, 124 Stat. 1376 (July 21, 2010).

Section 17A of the Securities Exchange Act of 1934⁴ and is registered with the CFTC as a derivatives clearing organization (“DCO”) pursuant to Section 5b of the Commodity Exchange Act.⁵ OCC clears all standardized options listed on the eleven U.S. national securities exchanges that trade options⁶ and, in its capacity as a DCO, clears CFTC-regulated futures products for six U.S. futures exchanges.⁷ OCC will also begin clearing over-the-counter options on securities indices in the near future, pending final regulatory approvals. OCC has operated safely and effectively for nearly 40 years – including through the market crises of 1987 and 2008 – mitigating systemic risk associated with derivatives trading.

On July 18, 2012, the Council designated OCC as a SIFMU. As such, OCC is subject to the enhanced supervisory and risk control system for SIFMUs established pursuant to Title VIII of Dodd-Frank. The SEC is OCC’s “Supervisory Agency” for purposes of Title VIII of Dodd-Frank, and OCC is subject to the regulations of the SEC implementing Title VIII.

Comments on the Proposed Rules

Soundness Standard

Section 234.6(b) of the Proposed Rules would require each FRB seeking to establish an Account for or provide Services to a SIFMU to ensure that doing so would “not create undue credit, settlement, or other risks to the [FRB].”⁸ Each FRB would be required to make a judgment that, among other things, the SIFMU is “in generally sound financial condition”⁹ and is “in compliance, based on information provided by the Supervisory Agency, with requirements imposed by its Supervisory Agency regarding financial resources, liquidity, participant default management, and other aspects of risk management[.]”¹⁰

We believe the Board should not adopt the subjective “general soundness” standard of subsection (b)(1) in addition to requiring each SIFMU to adhere to the financial and risk

⁴ 15 USC § 78q-1.

⁵ 7 USC § 7a-1.

⁶ OCC’s participant options exchanges include: BATS Exchange, Inc.; BOX Options Exchange, LLC; C2 Options Exchange, Inc.; Chicago Board Options Exchange, Inc.; International Securities Exchange, LLC; Miami International Securities Exchange, LLC; NASDAQ OMX BX, Inc.; NASDAQ OMX PHLX, LLC; The NASDAQ Stock Market LLC; NYSE Arca, Inc.; and NYSE MKT, LLC.

⁷ OCC’s participant futures exchanges include: CBCE Futures Exchange, LLC; ELX Futures L.P.; NASDAQ OMX Futures Exchange, Inc.; NYSE Life U.S. LLC; and OneChicago LLC.

⁸ Proposed Section 234.6(b), at 14028.

⁹ Proposed Section 234.6(b)(1), at 14028.

¹⁰ Proposed Section 234.6(b)(2), at 14028.

management standards of its own Supervisory Agency, which we support. Each Supervisory Agency is in the best position to adopt specific financial and risk management standards for the SIFMUs it regulates and to ensure that each such SIFMU complies with those standards. In OCC's case, the SEC has established risk management standards for clearing agencies that are designated as SIFMUs.¹¹ The SEC Standards were developed with the consultation of both the Council and the Board, as required by Title VIII of Dodd-Frank. We believe it is highly unlikely that there could be a scenario in which OCC would be in compliance with the SEC Standards, but not be in "generally sound financial condition" for purposes of Proposed Rule 234.6(b)(1). If such a scenario were possible, the proper way to address it would be to reconsider the SEC Standards, and not to require OCC to adhere to an additional, subjective standard.

Furthermore, we are concerned that the imposition of an additional subjective standard could, particularly in times of market stress, undermine confidence by creating confusion among market participants about what compliance, in addition to compliance with SEC Standards, is required of OCC, and whether OCC remains eligible to rely on the Accounts and Services provided by the FRBs. This confusion could inject unnecessary risk into the financial system. Use of a subjective standard would also make it difficult for a SIFMU to monitor its own compliance and make course corrections if the SIFMU's compliance staff detects deviations from those standards. If the Board believes a SIFMU's eligibility to continue to benefit from Accounts and Services provided by an FRB requires adherence to heightened standards, the Board should make those standards explicit in the final rules. Only clearly stated, verifiable requirements will enable market participants to evaluate the risk, if any, of OCC losing access to FRB Accounts and Services, and allow OCC to adjust its financial and risk management policies and procedures to ensure such continued access. Accordingly, we respectfully request that the Board (i) delete subsection 234.6(b)(1) from its final rule and (ii) clarify in the final rules that the Board's authority under subsection 234.6(b)(3) to set further standards for access for FRB Accounts and Services will be implemented in a transparent and objective manner. At the same time, we believe the Board should consider adding a provision giving the Board discretion to instruct an FRB to continue to provide services to a SIFMU in times of severe market stress without regard to the SIFMU's compliance with other requirements if the Board determines that such action is necessary to avoid a crisis of confidence in the financial system.

Termination of Accounts/Services

Section 234.6(e) of the Proposed Rules would allow the Board to direct an FRB "to impose limits, restrictions, or other conditions on the availability or use of [an Account] or [S]ervice by a [SIFMU], including directing the [FRB] to terminate the use of a particular [S]ervice or to close the [A]ccount."¹² OCC is currently evaluating how it may utilize Accounts and Services in an effort to decrease its reliance on commercial banks and further improve its own risk management practices through diversification of key functions. In conducting this evaluation, OCC must

¹¹ See Clearing Agency Standards, Final Rule, 77 Fed. Reg. 66220 (November 2, 2012) (the "SEC Standards").

¹² Proposed Rules at 14028.

consider the extent to which it will be able to rely on the continued availability of Accounts and Services in times of market stress, and the extent to which OCC's members will have comfort in that availability.

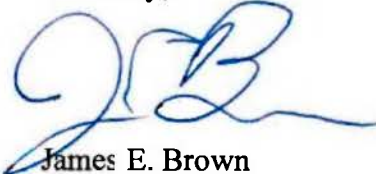
When establishing account relationships with commercial banks, OCC has the opportunity to negotiate terms it deems appropriate to reasonably ensure its ability to continue to rely on its commercial banks at such times. Thus, OCC has some ability to put in place measures designed to ensure that commercial bank accounts and services will remain available in times of market stress. The possibility that Accounts and Services may be terminated during periods in which those Accounts and Services are most important to OCC and difficult for OCC replace will be an important factor in OCC's determination of how to use the Accounts and Services.

Accordingly, we believe it is important that the Board carefully consider the impact a decision to require termination of Accounts or Services would have on a SIFMU before any such decision is made. While we appreciate that the FRBs should have the ability to terminate Accounts and Services in circumstances that pose more risk to the FRBs than would arise out of continuing to maintain the Accounts and Services, market stability demands a clear statement by the Board in the final Rule that (i) termination will be based on clearly defined standards, (ii) a decision to terminate will consider not only risks of continuing to maintain the Accounts and Services, but also the systemic effects of terminating them and (iii) in the event of such termination, the FRB will cooperate with the applicable SIFMU to provide for a transition to private sector services that is as smooth and seamless as is reasonably possible.

Conclusion

OCC appreciates the opportunity to comment on the Proposed Rules. We would be pleased to provide the Board with any additional information or analysis the Board may find useful in addressing our comments. If you have questions on the contents of this letter, feel free to contact me at (312) 322-6855 or jbrown@theocc.com.

Sincerely,



James E. Brown

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