SECURITIES AND EXCHANGE COMMISSION

In the Matter of the The Options Clearing Corporation **For an Order Instituting Proceedings to Determine Whether to Approve or Disapprove** Proposed Rule Change to Revise The Options Clearing Corporation's Schedule of Fees (Rel. No. 34-82793; File No. SR-OCC-2018-004)	File No. SR-OCC-2018-004

THE OPTIONS CLEARING CORPORATION'S SUBMISSION IN SUPPORT OF THE PROPOSED RULE CHANGE TO REVISE ITS SCHEDULE OF FEES

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Statutes and Rules

Other Authorities

The Options Clearing Corporation ("OCC") respectfully submits this response to the Securities and Exchange Commission's Order, dated February 28, 2018 (the "Suspension Order"), suspending and instituting proceedings to determine whether to approve or disapprove of OCC's proposed rule change to revise its schedule of fees (the "Proposed Fee Schedule").

PRELIMINARY STATEMENT

OCC respectfully submits that the Commission should approve its Proposed Fee Schedule, which seeks a modest increase in its clearing fees by four tenths of a penny per contract per trade for trades up to 1,019 contracts. This fee increase is smaller than OCC clearing fee increases the Commission has approved in the past and is essential for OCC to comply with its regulatory obligations and to continue to fulfill its responsibilities as a systemically important financial market utility ("SIFMU").

For many years, OCC refunded all fees collected in excess of expenses, leaving virtually no resources for capital improvement. This artificially depressed fees—money that should have been retained and spent on improving and maintaining clearing systems and infrastructure was instead rebated to clearing members. The result, as the Commission knows, is that OCC must now devote considerable resources to enhance its technological, legal and compliance, and security capabilities. OCC has been collaborating with SEC staff on these matters and intends to satisfy all of its regulatory obligations.

These projects, of course, cost money. Before proposing any fee increase, OCC management spent a considerable amount of time projecting how much OCC would need to spend to fund its operations and pay for these additional projects and analyzing its historical and expected cash flows. Based on these projections and analyses, OCC then determined that its projected fee revenue in 2018 at existing rates would not be sufficient to pay for its operations and all of these

projects while maintaining the 25% Business Risk Buffer required under its Capital Plan, which has been in place since 2015.

Accordingly, OCC management recommended first to the Compensation and Performance Committee ("CPC") and then to the full Board of Directors that clearing fees should be increased as set forth in the Proposed Fee Schedule. Both the CPC and full Board *unanimously* accepted OCC's budget and approved the fee increase. And both the CPC and full Board are composed of a majority of directors who are not affiliated with Stockholder Exchanges. Notably, Clearing Members on the Board who voted in favor of the fee increase—and whose firms or customers will pay for it—outnumber Stockholder Exchanges by two to one.

Susquehanna International Group's ("SIG") self-serving criticisms of the Proposed Fee Schedule do not—and cannot—alter the fact that OCC established the Proposed Fee Schedule to raise sufficient resources to pay its expenses and satisfy its extensive regulatory obligations.[1] Indeed, the entire premise of SIG's position is that OCC deliberately fabricated and overinflated its projected expenses at the bidding of the Stockholder Exchanges in order to increase their dividends. SIG has no basis whatsoever for that assertion and it is not true. As the Commission knows, OCC has seen its expenses dramatically increase in recent years not because the Stockholder Exchanges are pushing OCC to spend more money, but because OCC is being required to make significant investments to satisfy its regulatory obligations. And a majority of independent directors (both on the CPC and full Board) reviewed and approved those expenses

[1] Comment of Susquehanna International Group, LLP in Response to the Options Clearing Corporation Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Revise The Options Clearing Corporation's Schedule of Fees, Release No. 34-82596 (Feb. 14, 2018) (SR-OCC-2018-004) ("SIG Comment Letter").

and the fee increases needed to pay for them. This has nothing to do with the Stockholder Exchanges.[2]

OCC's Proposed Fee Schedule therefore reflects "the equitable allocation of reasonable dues, fees, and other charges among its participants," as required by Section 17A(b)(3)(D).[3] Without the increased fees contemplated by the Proposed Fee Schedule, OCC cannot satisfy its regulatory obligations as a SIFMU nor comply with its own Capital Plan. And every day that passes where OCC is deprived of those necessary fee increases (which were intended to go into effect on March 1) makes the situation worse. OCC respectfully requests that the Commission approve its Proposed Fee Schedule as soon as possible.

FACTUAL BACKGROUND

I. OCC Established The Capital Plan To Satisfy Mandatory SEC Requirements Designed To Ensure That OCC Can Fulfill Its Essential Role As A SIFMU.

OCC, as the Commission knows, has been designated as a SIFMU by the Financial Stability Oversight Council.[4] This designation was made because OCC is "an integral part of the national market system for clearance and settlement, and its failure or service disruption could have cumulative negative effects on the U.S. options and futures markets, financial institutions,

[2] In its Comments, SIG takes issue with OCC's refusal to disclose to the public its highly confidential 2018 Corporate Budget and other confidential materials. As discussed in Part III *infra*, nothing in the APA or Exchange Act requires OCC or any other SRO to divulge confidential business information to commenters in order to make a fee change. It would represent a dramatic departure from Commission practice, would be fundamentally inconsistent with 17 C.F.R. § 200.83, and would impose a significant (and unsettling) burden on all SROs if SROs could not make changes to their fees without disclosing a detailed financial analysis, including a breakdown and supporting material for every expense they plan to incur, for public market participants to audit. SIG has plainly been afforded a meaningful opportunity to comment on the Proposed Rule Change (as evidenced by its submissions) and it is now within the purview of the Commission to evaluate the Proposed Rule Change based on the evidence submitted to it.

[3] 15 U.S.C. § 78q-1(b)(3)(D).

[4] Financial Stability Oversight Council 2012 Annual Report, Appendix A, https://www.treasury.gov/initiatives/fsoc/Pages/annual-report.aspx.

and the broader financial system."[5] In short, OCC "performs critical functions in the clearance and settlement process" and its services "increase the efficiency and speed of options trading and settlement as well as reduce members' operational expenses and counterparty credit risk."[6]

As a SIFMU, OCC is required to satisfy specific regulatory requirements promulgated by the Commission. OCC has no choice in the matter; these regulatory requirements are mandatory and govern its operations. Specifically, in 2016, the Commission adopted Rule 17Ad-22(e)(15), which contains explicit requirements designed to address the general business risks faced by OCC and other covered clearing agencies.[7] As the Commission explained, this Rule requires:

> [A] covered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that the covered clearing agency can continue operations and services as a going concern if those losses materialize.[8]

Accordingly, pursuant to Rule 17Ad-22(e)(15), OCC is required to satisfy two obligations: (i) OCC must maintain sufficient capital funded by equity "equal to the greater of either six months of [its] current operating expenses or the amount determined by the board of directors to be sufficient to ensure a recovery or orderly wind-down of critical operations and services of the

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[5] Order Setting Aside Action by Delegated Authority, Approving Proposed Rule Change Concerning The Options Clearing Corporation's Capital Plan and Denying Motions, Exchange Act Release No. 34-77112 (Feb. 11, 2016), 81 Fed. Reg. 8294, at 8294 (Feb. 18, 2016) ("2016 Approval Order").

[6] *Id.*

[7] 17 C.F.R. § 240.17Ad-22(e)(15).

[8] Definition of Covered Clearing Agency, Exchange Act Release No. 34-78963 (Sept. 28, 2016), 81 Fed. Reg. 70744, at 70750 (Oct. 13, 2016). This Rule comports with international standards. *See* Principle 15, *Principles for Financial Markets Infrastructure* ("PMFIs"), Bank for International Settlements and the International Organization of Securities Commissions ("A [Financial Market Infrastructure] should identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialise. Further, liquid net assets should at all times be sufficient to ensure a recovery or orderly wind-down of critical operations and services.").

covered clearing agency;" and (ii) OCC must have a viable plan "for raising additional equity should its equity fall close to or below" this amount.[9]

OCC adopted its Capital Plan to satisfy its regulatory obligations under Rule 17Ad-22(e)(15). Based on a "bottom up" analysis conducted by Oliver Wyman, an Ad Hoc Strategic Advisory Group (the "Advisory Group") of OCC's Board of Directors determined that OCC's existing capital reserves of $25 million were inadequate and that OCC needed to raise an additional $222 million of capital, plus implement a plan to obtain replenishment capital to the extent its capital were depleted.[10] Notably, seven of the Advisory Group's nine members were independent and not affiliated with the Stockholder Exchanges.

As the Commission knows, Rule 17Ad-22(e)(15) requires OCC to satisfy its capital requirements by maintaining capital "funded by equity." The only potential source of an additional equity capital infusion, therefore, was OCC's stockholders, the Stockholder Exchanges. OCC's Board of Directors also considered raising the required additional capital by raising fees and retaining after-tax earnings, but this would have reduced refunds to clearing members and ratcheted-up their fees, would have been highly inefficient from a tax perspective, and would not have obtained sufficient capital quickly enough to satisfy OCC's regulatory obligations based on OCC's expectations of the adoption date of the requirements at the time.

As a result, OCC's Board of Directors adopted the Capital Plan, pursuant to which the Stockholder Exchanges immediately contributed a total of $150 million in equity capital to OCC and entered into agreements to provide OCC with a Replenishment Capital Commitment of up to an additional $200 million on a *pro rata* basis. This was a major capital investment and

[9] 17 C.F.R. § 240.17Ad-22(e)(15).

[10] For a more detailed description of these analyses and the two options considered by the Advisory Group and OCC Board, see OCC's Post-Remand Submission to the Commission in Support of the Re-Approval of the Capital Plan at 5-9 (Oct. 13, 2017) (SR-OCC-2015-02).

commitment by the Stockholder Exchanges, resulting in $150 million (and potentially $350 million) being tied up indefinitely on OCC's balance sheet. To compensate the Stockholder Exchanges for their illiquid investment and capital commitments, the Advisory Group negotiated an after-tax dividend that it concluded was fair and reasonable consideration for the Stockholder Exchanges' capital outlays and commitments. This after-tax dividend is calculated each year by first providing clearing members with a refund of 50% of OCC's earnings before tax and then issuing the after-tax amount of the remainder (*i.e.*, significantly less than 50% and thus significantly less than refunds to clearing members) as a dividend to the Stockholder Exchanges.

In addition, as part of the Capital Plan and to implement this compensation and refund structure, OCC adopted a Fee Policy, Refund Policy, and Dividend Policy, pursuant to which fees are reviewed (and adjusted when necessary) quarterly to cover OCC's projected operating expenses and to permit OCC to maintain a 25% Business Risk Buffer. The Business Risk Buffer is an amount of fee revenue that OCC targets above its anticipated operating expenses to allow for unexpected fluctuations in operating expenses, business capital needs, and regulatory capital requirements. SIG has repeatedly misrepresented the definition of this figure in an attempt to inflate its meaning. In its comment letter, SIG stated that "the Business Risk Buffer is 33% of its expense projection" and characterized OCC's description of its own Capital Plan as "false and grossly misleading."[11] To be clear, the Business Risk Buffer is met when OCC's net income (the difference between its projected revenue and operation expenses) is equal to 25% of OCC's forecasted revenue.[12]

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[11] SIG Comment Letter.

[12] Notice of Filing of an Advance Notice, as Modified by Amendment No. 1, Concerning a Proposed Capital Plan for Raising Additional Capital That Would Support The Options Clearing Corporation's Function as a Systemically Important Financial Market Utility, Release No. 34-74202 at 13-14 (Feb. 4, 2015) (SR-OCC-2014-813) ("Capital Plan").

Between February 2015 and February 2016, the Commission reviewed and approved the Capital Plan three separate times.[13] In so doing, the Commission found that the Plan was consistent with the requirements of the Exchange Act, including Sections 17A(b)(3)(A), 17A(b)(3)(D), 17A(b)(3)(F), and 17A(b)(3)(I).[14] The Commission concluded that the Capital Plan is designed "to allow OCC to continue its essential role by raising sufficient capital to cover business, operational, and pension risks" rather than "to enable the Stockholder Exchanges to monetize OCC's clearing monopoly."[15] The Commission also stated that it "does not believe that the Capital Plan operates to increase fees, inflate operating expenses or drive up transaction costs in a manner inconsistent with the protection of investors or the public interest."[16]

Several parties, including SIG, filed petitions for review of the Approval Order, challenging the action taken by delegated authority. Following review of these petitions, on August 8, 2017, the U.S. Court of Appeals for the D.C. Circuit remanded the Approval Orders to the Commission to further analyze whether the Capital Plan is consistent with the Exchange Act.[17] While the Commission further analyzes the Capital Plan, it remains in effect as originally approved by the Commission.[18]

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[13] *See* Notice of No Objection to Advance Notice Filing, Exchange Act Release No. 34-74387 (Feb. 26, 2015), 80 Fed. Reg. 12215 at 12220-12221 (Mar. 6, 2015) ("Notice of No Objection"); Order Approving Proposed Rule Change Concerning a Proposed Capital Plan for Raising Additional Capital That Would Support the Options Clearing Corporation's Function as a Systemically Important Financial Market Utility, Exchange Act Release No. 34-74452 (Mar. 6, 2015), 80 Fed. Reg. 13058, at 13068 (Mar. 12, 2015) ("2015 Approval Order"); Order Setting Aside Action by Delegated Authority, Approving Proposed Rule Change Concerning The Options Clearing Corporation's Capital Plan and Denying Motions, Exchange Act Release No. 34-77112 (Feb. 11, 2016), 81 Fed. Reg. 8294, at 8294 (Feb. 18, 2016).

[14] 15 U.S.C. § 78q-1(b)(3)(A); 15 U.S.C. § 78q-1(b)(3)(F); 15 U.S.C. § 78q-1(b)(3)(D); 15 U.S.C. § 78q-1(b)(3)(I).

[15] 2016 Approval Order, 81 Fed. Reg. at 8300.

[16] *Id.* at 8301.

[17] *Susquehanna Int'l Grp., LLP v. SEC*, 866 F.3d 442, 451 (D.C. Cir. 2017).

[18] *See id*.

II. The Proposed Fee Schedule Was Set In Accordance With OCC's Fee Policy And Was Approved By A Majority Of Independent And Disinterested Directors Representing Clearing Members And Other Fee Payers.

Pursuant to OCC's Fee Policy, OCC management reviews its projected operating expenses and revenues on a quarterly basis to determine whether its projected fees are sufficient to cover its projected operating expenses while maintaining the required Business Risk Buffer.

To meet the requirements of the Capital Plan, the difference between revenue and expenses (net income) must equal at least 25% of revenue. If net income is *less* than 25% of projected revenue, then OCC must increase its projected revenue by increasing clearing fees.[19] Conversely, if net income is *greater* than 25% of projected revenue, OCC can decrease its clearing fees and/or refund the excess to clearing members. Since the adoption of the Capital Plan, OCC has done both. For example, on March 1, 2016, OCC reduced clearing fees on average by 19%, and has recently announced a special refund of $25.7 million for 2017 clearing fees in addition to its regular refund of approximately $53 million.[20]

OCC has followed this same approach ever since the Capital Plan went into effect three years ago. During that time, OCC has adjusted its Fee Schedule four times (prior to the current proposal), all based on the same approach and all without fanfare. In each instance, OCC adjusted its fees to obtain a sufficient amount of projected revenue to cover its projected expenses plus the Business Risk Buffer. And, in each instance, OCC's proposed fee changes were reviewed carefully by OCC management and OCC's Board of Directors and its subcommittees, who scrutinized OCC's proposed budget and expenses closely to make sure they are appropriate given

[19] Capital Plan at 13-14.

[20] Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Revise The Options Clearing Corporation's Schedule of Fees, Release No. 34-77041 (SR-OCC-2016-001) (Feb. 3, 2016); Press Release, "OCC Declares Nearly $80 Million Clearing Member Refund for 2017," (March 1, 2018), https://www.theocc.com/about/newsroom/releases/2018/March-1-OCC-Declares-Nearly-80-Million-Clearing-Member-Refund-for-2017.jsp.

that an overwhelming majority of the Board represents those who will be responsible for paying the fees—not the Stockholder Exchanges.

Every step of this process is guided by disinterested management and directors who have no incentive to inflate or otherwise distort OCC's revenue and expense projections. Pursuant to the OCC Board of Directors Charter and Corporate Governance Principles, nine of the Board's 20 directors must represent OCC clearing members ("Member Directors"), five must be unaffiliated ("Public Directors"), one director must represent OCC management ("Management Director"), **and only five of twenty directors represent OCC's Stockholder Exchanges** ("Exchange Directors").[21] And, before any proposed fee changes reach the full Board, they are prepared by OCC management and reviewed by Board committees that likewise are comprised of a majority of disinterested members that are independent from the Stockholder Exchanges. Thus, contrary to SIG's unfounded suggestion otherwise, OCC's Stockholder Exchanges have no ability to inflate OCC's expenses nor the resulting clearing fees, and no one who actually controls how expenses and fees are determined has any incentive to do so.

OCC followed this same approach to determine the Proposed Fee Schedule. In December 2017, as part of its quarterly review of projected revenues and expenses, OCC management, led by its Chief Financial Officer, reviewed OCC's budget for 2018. As the Commission knows, for many years, OCC refunded all fees collected in excess of expenses, leaving virtually no resources for capital improvement. OCC has thus been placed in the position of now being required to identify and address any and all perceived shortcomings (which have been identified in close collaboration with the SEC staff) in its technological, legal and compliance, and security capabilities.

[21] The Options Clearing Corporation Board of Directors Charter and Corporate Governance Principles at 4, https://www.theocc.com/components/docs/about/corporate-information/board_of_directors_charter.pdf.

OCC must now obtain the necessary funds to pay for all of these capital and operational improvements. And it must do so within the parameters of the Capital Plan, which was adopted in order to comply with Rule 17Ad-22(e)(15). OCC has no other choice. It cannot be required to spend money to improve its systems and controls while, at the same time, being denied the ability to raise that money through the only means it has—clearing fees.

To that end, OCC engaged in a collaborative effort between its Finance, Project Management, and IT departments to identify the resources that it would need in 2018 to fulfill its regulatory obligations. This included:

- Adding 8 full-time employees in Compliance and 6 in Legal to help deliver a comprehensive end-to-end legal framework;
- Adding 17 full-time employees in Security Services;
- Adding 19 full-time employees to fully operationalize business transformation and drive superior execution; and
- Dedicating 7 full-time employees to begin the replacement of OCC's Encore system.

In addition to these resources, among other things, OCC was set to incur other employee cost increases from the full year impact of 2017 hiring, incur expenses as a result of its planned office relocation, and incur increases in IT costs driven mostly by requirements for data storage, software licenses in support of strategic projects, and new IT systems.

In total, OCC projected that expenses would increase by approximately 15%, to $347.6 million. Based on projected trading volume, this meant that to cover expenses and maintain the Business Risk Buffer, OCC would need to obtain $463.5 million in revenues in 2018. Management calculated that it could achieve those revenues if OCC implemented a fee increase of four-tenths of a penny per contract per trade starting March 1, 2018. This fee increase, to $0.0540 per contract per trade, is reflected in the Proposed Fee Schedule.

All of the additional expenses driving the required fee increase were explained in detail in OCC's 2018 Corporate Budget. Far from containing conclusory statements, as SIG wrongly suggests, OCC's 2018 Corporate Budget contains pages and pages of detailed financial analysis—including a roll forward of OCC's 2017 forecast broken down by expense category to show each area of expense increase, a list showing exactly where additional headcount would be added, and an item-by-item comparison of the 2018 Budget to the 2017 forecast for all IT costs, professional fees, and employee costs. And, if the Commission requires additional information about any of its projected expenses, OCC would be pleased to provide it and address any questions the Commission might have.

OCC's 2018 Corporate Budget—on which OCC based its 2018 expense forecast and the Proposed Fee Schedule—was prepared by OCC management without any influence from the Stockholder Exchanges. On December 12, 2017, OCC management presented its 2018 Corporate Budget to the Compensation and Performance Committee ("CPC"), a majority of which is composed of Management or Public Directors.[22] After a discussion of Management's projections, the CPC *unanimously* approved the 2018 Corporate Budget and the Proposed Fee Schedule.[23] Also on December 12, 2017, the Audit Committee met to review its portion of the 2018 Corporate Budget. Five committee members attended, all of which were Public Directors, Management Directors, or Member Directors.[24] None of the Exchange Directors attended this meeting of the Audit Committee. On December 13, 2017, the Technology Committee met to review the IT portion of the 2018 Corporate Budget. Five committee members attended the

[22] 2018 Corporate Budget (Ex. 1); Meeting Minutes of the Regular Meeting of the Compensation and Performance Committee of the Options Clearing Corporate (Dec. 12, 2017) (Ex. 2).
[23] *Id.* at 4.
[24] Meeting Minutes of the Regular Meeting of the Audit Committee of the Options Clearing Corporate (Dec. 12, 2017) (Ex. 3).

meeting, including one Public Director, one Management Director, and three Member Directors.[25] In sum, three different committees reviewed and approved OCC's 2018 Corporate Budget, and none of them is controlled by the Stockholder Exchanges.

On December 13, 2017, OCC's Board of Directors met and approved the 2018 Corporate Budget and Proposed Fee Schedule.[26] Eighteen Directors attended that meeting, including eight of nine Member Directors, four of five Exchange Directors, all five Public Directors, and one Management Director. That is, the number of Member Directors—who represent the firms who will actually pay OCC's higher fees—outnumbered Exchange Directors by two to one. OCC's CFO presented the 2018 Corporate Budget to the Board and explained that the year-over-year expense growth of 15% was attributable to the full year employee expense from 2017, increased technology costs, and a reduction of professional fees.[27] OCC's CFO further explained that, to pay for these increased expenses, the CPC accepted Management's recommendation of a fee increase from $0.050 to $0.054. Under this recommendation, the fee for trades with contracts greater than 1,100 remained at $55 per trade, and OCC also lowered the trade size where the $55 per trade cap applies from 1,100 contracts to 1,019 contracts so that no one ever pays in excess of this $55 per trade cap. Following this presentation, the Board, including the fourteen non-Exchange Directors in attendance, unanimously approved the 2018 Corporate Budget and Proposed Fee Change.

[25] Meeting Minutes of the Regular Meeting of the Technology Committee of the Options Clearing Corporate (Dec. 13, 2017) (Ex. 4).
[26] Meeting Minutes of the Regular Meeting of the Board of Directors of the Options Clearing Corporate (Dec. 13, 2017) (Ex. 5).
[27] Ex. 5 at 12.

PROCEDURAL HISTORY

On January 19, 2018, OCC filed with the Commission the Proposed Fee Schedule (for implementation as of March 1, 2018) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 and Rule 19b-4 thereunder. Pursuant to Section 19(b)(3)(A) of the Act, the Proposed Fee Schedule was immediately effective upon filing. The Proposed Fee Schedule was published for comment in the Federal Register on February 2, 2018.[28]

Only one commenter objected to the Proposed Fee Schedule, SIG. On February 14, 2018, SIG submitted a comment arguing that the proposed fee increase contemplated by the Proposed Fee Schedule was "exorbitant," and was the product of a "conflict of interest" in which "the OCC Shareholder Exchanges are incented to overestimate its expenses, because such overestimation increases the Business Risk Buffer amount, which is the source of the Shareholder Exchange dividends."[29] OCC submitted a response to SIG's comment, explaining that the increase in light of the significantly increased expenses faced by OCC to satisfy its regulatory obligations as a SIFMU.[30]

On February 28, 2018, the Commission issued an order suspending the Proposed Fee Schedule and instituting proceedings to determine whether it should be approved or disapproved.[31] OCC offers this submission to further demonstrate that the Proposed Fee Schedule satisfies the requirements of Section 17A(b)(3)(D) of the Act, was the product of a thorough and

[28] Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Revise the Options Clearing Corporation's Schedule of Fees, Release No. 82596 (Jan. 30, 2018), 83 Fed. Reg. 4944 (Feb. 2, 2018) (SR-OCC-2018-004) ("Notice").
[29] SIG Comment Letter.
[30] OCC Response to SIG Comment Letter (Feb. 28, 2018) (SR-OCC-2018-004).
[31] Suspension of and Order Instituting Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change to Revise the Options Clearing Corporation's Schedule of Fees, Release No. 82793 (Feb. 28, 2018), 88 Fed. Reg. 9562 (March 6, 2018) (SR-OCC-2018-004) ("Suspension Order").

disinterested process by both the OCC Board and Management, and as a result, should be approved by the Commission.

ARGUMENT

I. The Proposed Fee Schedule Satisfies The Requirements of Section 17A(b)(3)(D) of the Exchange Act.

Under the Proposed Fee Schedule, OCC proposes to charge $0.054 per contract per trade, up to 1,019 contracts. For trades of contracts above that amount OCC charges a flat fee of $55 per trade. This represents an increase of four tenths of one cent per contract per trade above its existing $0.050 fee, which is what OCC has charged since October 3, 2016, pursuant to the last proposed fee schedule filed with the Commission.

OCC's Proposed Fee Schedule complies with Section 17A(b)(3)(D) of the Exchange Act because it provides for "the equitable allocation of reasonable dues, fees, and other charges among its participants."[32] Because all clearing members are charged the same amount under the Proposed Fee Schedule, there can be no question that fees are allocated equitably and SIG does not contend otherwise.

OCC's Proposed Fee Schedule is also reasonable. Several facts make this clear.

First, as discussed above, the Proposed Fee Schedule was the product of a robust forecasting process where OCC management projected its expenses for 2018 and then determined how to set the Proposed Fee Schedule to pay for those expenses and retain a 25% Business Risk Buffer. A self-regulatory organization ("SRO") setting fees to pay for its projected expenses plus a risk buffer designed to satisfy its regulatory obligations is plainly reasonable.

The amount that OCC proposes to charge for the clearing services is also reasonable, and SIG does not point to any facts suggesting otherwise. OCC provides a valuable

[32] 15 U.S.C. § 78q-1(b)(3)(D).

service for which it is entitled to compensation. And to the extent that its fee revenues turn out to be higher than its actual expenses plus the Business Risk Buffer, those fees may be refunded to clearing members (as they have in the past).

Second, OCC's projected expenses (and hence the resulting fees to pay for them) were carefully considered and reviewed not only by OCC management, but also by the full OCC Board of Directors and three committees of directors. Neither the Board nor those committees is in any way beholden to or dominated by the Stockholder Exchanges. To the contrary, they are composed predominantly of clearing members and public directors—not the Stockholder Exchanges. This is especially important here because it is the clearing members (or their customers) who bear the additional expense of higher clearing fees, and they unanimously voted in favor of OCC's 2018 Budget Plan and Proposed Fee Schedule. If OCC's non-stockholder directors believed that OCC's planned expenditures were unnecessary, they would certainly have voted against a fee increase to pay for them since they have a direct economic interest in that decision and it was *against* that economic interest to vote for a fee increase. That they did not vote against the proposed fee increase speaks volumes.

SIG—the only commenter challenging the Proposed Fee Schedule—should not be heard to second guess the decisions of clearing members (and disinterested parties) serving on OCC's Board. And, while SIG might point to significant expense growth in recent years, that does not mean that OCC's expense projections are wrong. For years, clearing members like SIG enjoyed low fees and high refunds. As the Commission is well aware, OCC is now being required to make substantial investments in its technological, legal and compliance, and security capabilities. This costs money and OCC now must increase its fees to pay for the necessary resources to satisfy its regulatory obligations.

These projects are very real and quite expensive. They are not fabricated as SIG suggests, nor the result of some nefarious scheme by the Stockholder Exchanges to increase their dividends. If OCC is denied the resources to pay for them, they cannot be completed with the result that all of OCC's members will be harmed.

Third, OCC is *required* by its Fee Policy and Capital Plan "to set its fees at a level that utilizes a Business Risk Buffer of 25%."[33] That is exactly what OCC did. The resulting Proposed Fee Schedule is therefore necessary for OCC to satisfy its obligations as a SIFMU. Without it, OCC would fall short of its obligations under the Capital Plan and Rule 17Ad-22(e)(15). As such, the Proposed Fee complies with the requirement that clearing agencies' fees be reasonable and should be approved.

This is also completely consistent with the objectives of the Capital Plan. Nothing in the Capital Plan, in any of OCC's related filings, or in the Exchange Act or the rules promulgated thereunder guarantees participants such as SIG low clearing fees in perpetuity. To the contrary, the Commission stated that it "does not believe that the Capital Plan operates to increase fees, inflate operating expenses or drive up transaction costs **in a manner inconsistent with the protection of investors or the public interest**."[34] As this statement implies, there are instances in which an increase in fees is consistent with, and even mandated by, the protection of investors and the public interest.

Simply put, OCC needs the resources to pay for several critical programs that are underway. These are necessary to improve the integrity and efficiency of its operations, and fulfill its regulatory obligations. SIG's self-serving submissions—none of which its fellow market participants has endorsed and those serving on the OCC Board rejected—only serve to undermine

[33] Capital Plan at 16.
[34] 2016 Approval Order, 81 Fed. Reg. at 8301 (emphasis added).

OCC's efforts (working closely with the Commission) to address these concerns. This runs directly contrary to the objectives of Section 17A to promote the "public interest, the protection of investors, [and] the prompt and accurate clearance and settlement of securities transactions and the safeguarding of securities and funds."[35]

II. Delaying Implementation of the Proposed Fee Schedule Further Places OCC In An Untenable Position.

The amount that OCC has budgeted to spend on capital and operational improvement projects is not going to decrease. If anything, OCC's expenses this year have only increased due to unanticipated developments.

By suspending OCC's Proposed Fee Schedule, OCC will now collect less revenue in 2018 than it would have had its proposed fees been implemented on March 1. If the Proposed Fee Change were implemented on March 1, as originally intended, OCC would have at least nine months' of higher fees to cover daily operating expenses plus 25% of revenue as required by the Business Risk Buffer. However, the same Proposed Fee Change implemented on June 1 only provides OCC with six months of higher fees. Thus, OCC has three months of higher operating expenses with no corresponding increase in revenue. Although SIG points to increased trading volume early this year, the increase in volume is more than offset by the lower amount of fees per trade that OCC is able to collect as a result of the Suspension Order.

This puts OCC in an untenable position. OCC is required to spend a significant amount of money to satisfy its regulatory obligations. But OCC cannot spend money that it does not have. The longer the Proposed Fee Schedule is delayed, the worse this situation gets. Ultimately, OCC may have to abandon projects that it cannot afford, or raise fees even higher in order to make sure it can afford them.

[35] 15 U.S.C. § 78q-1(1)(b)(1).

OCC respectfully submits that the Commission should resolve the Catch-22 in which OCC has been put, lift the Suspension Order as soon as possible, and approve the Proposed Fee Schedule.

III. The Commission Should Not Alter Settled Practice By Requiring OCC To Disclose Publicly Its Confidential Business Records In Order To Obtain Approval For Changes To Its Fee Schedule.

When OCC submitted the Proposed Rule Change, it followed exactly the same procedure, and provided the same level of information necessary for public comment, as it and other SROs have provided for prior proposed rule changes impacting fees charged to market participants. OCC described the terms of substance covered by the Proposed Rule Change, set forth the purpose for the Proposed Rule Change, and set forth the statutory basis for the Proposed Rule Change. Consistent with the Administrative Procedure Act ("APA") and the Exchange Act, public comment was invited and one commenter (SIG) provided a comment about the Proposed Rule Change. That single comment prompted this proceeding.

In addition to its public submissions, OCC has also supplied the Commission a copy of its 2018 Corporate Budget and other confidential information so that the Commission may evaluate whether the Proposed Rule Change complies with the Exchange Act. OCC is also submitting additional confidential materials, including OCC Board and committee minutes, in further support of the Proposed Rule Change.

OCC, however, is not required to disclose confidential information about its operations, future plans, and financial position to market participants. These business records contain detailed financial information and analyses, risk analyses, internal records, and discussions of business decisions that clearly fall within the scope of information entitled to confidential treatment under FOIA pursuant to 5 U.S.C. § 552(b)(4) ("FOIA Exemption 4") and under

Commission rules, *see* 17 C.F.R. § 200.83. This information would have highly detrimental consequences that could impact OCC's essential business functions if released to the public.

Nothing in the APA nor the Exchange Act requires this unprecedented result. The APA requires agencies to provide the public with notice of proposed rules and "give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments with or without opportunity for oral presentation."[36] This opportunity for public comment must be a "meaningful opportunity."[37] But providing the public the meaningful opportunity to comment on a proposed rule does not require the agency (or SRO) to disclose all materials or data it reviewed (or provided) in the course of rulemaking, particularly when such materials are confidential under the very same law.[38] As the courts have recognized, federal agencies may rely on confidential information without requiring the disclosure of that confidential information.[39] And, as evidenced by SIG's comment letter and its submission in response to the Commission's Suspension Order, SIG (and others) plainly have been afforded the required "meaningful opportunity" to comment.

This makes sense. The Commission is the reviewing agency, and it must make a reasoned decision based on the evidence presented to it regarding the Proposed Fee Schedule. SIG can provide comments, as it has done, but it is not entitled to OCC's confidential information and the Commission cannot substitute SIG's judgment for that of the Commission. Contrary to SIG's assertions, this is completely consistent with OCC's statements to the Commission in connection

[36] 5 U.S.C. § 553(c).
[37] *Gerber v. Norton*, 294 F.3d 173, 179 (D.C. Cir. 2002); *see also Rural Cellular Ass'n v. F.C.C.*, 588 F.3d 1095, 1101 (D.C. Cir. 2009) (finding that "nothing else is required" when the F.C.C. issued a notice, considered the submitted comments, and only issued an order once the required rulemaking process was complete).
[38] *FBME Bank Ltd. v. Lew*, 125 F. Supp. 3d 109, 119 n.2 (D.D.C. 2015) (holding that the agency was not required to provide classified information or even unclassified summaries of the classified information when the notice "adequately summarized the conclusions [the agency] drew from the classified evidence.")).
[39] *Id.* (quoting *Al Haramain Islamic Found., Inc. v. U.S. Dep't of Treasury*, 686 F.3d 965, 983 (9th Cir. 2012).)

with the Capital Plan—in which OCC emphasized that Commission review of fee changes would be a check on any abuse and there would also be "an opportunity for Clearing Members and other market participants to object to any proposed changes."[40] That is what happened here—SIG has objected and the Commission is reviewing OCC's Proposed Fee Schedule. OCC did not, and would not, promise to make its sensitive confidential information available to market participants as part of this process.

Moreover, it would set a terrible precedent if an SRO like OCC were required to disclose publicly a detailed financial analysis, including a breakdown and supporting material for every expense it plans to incur, in order to obtain approval to change its fee schedule. This would represent a dramatic departure from Commission practice and would impose a significant burden on OCC and SROs generally. Indeed, SIG's own co-Petitioners challenging the Capital Plan have taken precisely the same approach in their own fee filings, with the same level of information as OCC, as OCC did in the Proposed Rule Change.[41]

No SRO should need to face the Hobson's choice between revealing its confidential information and forgoing fee increases needed to fund projected expenses. Nor should any SRO be required to subject its financials to a line-by-line audit, as SIG proposes here, of all its operating expenses and revenue forecasts. This will create an impossible burden for SROs (who, again, are regulated by the Commission, not by market participants) and result in costly delays (which, again, has happened here). SIG's invitation for the Commission to

[40] Letter from James E. Brown, Executive Vice President, General Counsel and Secretary, Options Clearing Corporation, to Brent J. Fields, File No. SR-OCC-2015-02, at 11 (Feb. 5, 2015).
[41] *See, e.g.*, Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend the BOX Volume Rebate, Release No. 34-82655 (SR-BOX-2018-03) (Feb. 8, 2018); Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend the Fee Schedule of Miami Intl. Securities Exchange, LLC, Release No. 34-82673 (SR-MIAX-2018-02) (Feb. 8, 2018).

change longstanding and widely accepted industry and SEC practice in this manner will lead to greater instability in the financial markets and should be rejected.

CONCLUSION

For the reasons discussed above, OCC respectfully requests that the Commission approve its Proposed Rule Change, and accompanying Proposed Fee Schedule, as soon as possible.

Dated: March 27, 2018

Respectfully submitted,

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