UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding
File No. 3-20665

In the Matter of the Application of

LEK SECURITIES CORPORATION

For Review of Action Taken by The Options Clearing Corporation

THE OPTIONS CLEARING CORPORATION'S RESPONSE SEEKING DISMISSAL OF LEK SECURITIES CORPORATION'S APPLICATION FOR REVIEW UNDER EXCHANGE ACT SECTION 19(d)

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INTRODUCTION

The opening brief filed by Lek Securities Corporation ("LSC") confirms that the Commission lacks jurisdiction over its application for review. Though LSC gestures toward statutes and rules, its application and brief sing one note: the Commission should exercise jurisdiction here because LSC asserts the protective measures imposed by The Options Clearing Corporation ("OCC") "are based on erroneous information." LSC Ex. 4; LSC Br. at 3 ("[The protective measures] were imposed without a rational basis and are based on incorrect information."); *id.* at 4 ("premised on the same erroneous assumptions"); *id.* ("This alleged factual basis for the Protective Measures is simply false."); *id.* at 10; *id.* at 11 ("[T]he protective measures were imposed based on incorrect assumptions and an inaccurate understanding of LSC's operations."); *id.* at 12 ("false assumptions"). But jurisdiction under Section 19(d) is not created by unsupported assertions of a factual dispute about the basis for an otherwise non-reviewable action by an SRO.

As LSC recognizes, OCC has broad authority to establish, implement, maintain, and enforce a sound risk-management framework to manage the risks posed by clearing members. *See* LSC Ex. 4. Under that authority, OCC imposed protective measures—margin requirements and daily reporting obligations—to manage the risks created by LSC's own operational choices. Despite LSC's claims that these protective measures are "akin to a monetary penalty," LSC Br. at 3, the protective measures are risk management tools, not disciplinary sanctions that can be appealed to the Commission. Section 19(d) does not permit a clearing member to second guess an SRO's use of generally applicable and Commission-approved risk management tools. Even looking past LSC's improper attack on the application of OCC Rules, LSC has failed to carry its burden of establishing that its application falls within the Commission's limited jurisdiction under Section 19(d). The application should be dismissed for lack of jurisdiction.

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BACKGROUND

A. OCC's Risk Management Obligations Under the Exchange Act.

OCC is a clearing agency registered with the SEC pursuant to Section 17A of the Securities and Exchange Act of 1934 and as such it is also a self-regulatory organization ("SRO") subject to Section 19 of the Act. *See* 15 U.S.C. § 78q-1(b)(2). OCC is also designated by the Financial Stability Oversight Council as a systemically important financial market utility for the financial system of the United States. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. § 5462(4). As the central counterparty for all equity options listed on United States exchanges, and for the futures products and stock loan programs it supports, OCC becomes the buyer to every selling clearing member and the seller to every buying clearing member, guaranteeing that the obligations under the financial contracts will be honored regardless of the default of a clearing member. Accordingly, OCC's risk management processes are designed to protect OCC, other clearing members, and the public by placing the burden of risks presented by an individual clearing member primarily on that clearing member—not OCC, other clearing members, or the public.

Given OCC's systemic importance to the orderly functioning of financial markets, Exchange Act Section 17A(b)(3) requires that OCC rules must, among other things, be designed "to promote the prompt and accurate clearance and settlement of securities transactions," "to assure the safeguarding of securities and funds which are in [its] custody or control," and "in general, to protect investors and the public interest." Section 17A of the Exchange Act [15 U.S.C. § 78q-1(b)(3)]. In furtherance of these objectives, the SEC has implemented rules that require OCC to "establish, implement, maintain and enforce written policies and procedures" designed to manage the legal, credit, liquidity, operational, business, and other risks borne by it, and to manage its credit exposures to each clearing member, including by establishing a risk-

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based margin system that covers exposures to clearing members. *See* Rule 17Ad-22(e) [17 C.F.R. § 240.17Ad-22(e)]. Under Exchange Act Rule 17Ad-22(e)(3), OCC must specifically "maintain a sound risk management framework for comprehensively managing" these risks, which includes "risk management policies, procedures, and systems designed to identify, measure, monitor, and manage the range of risks that arise in or are borne by" OCC. [17 C.F.R. § 240.17Ad-22(e)(3)(i)]. These risk management policies and procedures are required to be subject to periodic review by OCC and approved annually by its board of directors. *Id.*

In addition, under Rule 17Ad-22(e)(4), OCC must "[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes," including by "[m]aintaining sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence." [17 C.F.R. § 240.17Ad-22(e)(4)(i)]. Exchange Act Rule 17Ad-22(e)(6) further requires OCC to cover "its credit exposures to [clearing members] by establishing a risk-based margin system that," among other things, "[c]onsiders, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market." [17 C.F.R. § 240.17Ad-22(e)(6)(i)]. And under Rule 17Ad-22(e)(18), OCC must "[e]stablish objective, risk-based, and publicly disclosed criteria for participation," "require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in [OCC], and monitor compliance with such participation requirements on an ongoing basis." [17 C.F.R. § 240.17Ad-22(e)(18)]. In sum, OCC is required by statute and the Commission's rules for a systemically important financial market utility like OCC to establish, implement, maintain, and enforce a robust risk management framework to protect itself, other OCC clearing members, and the public.

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B. OCC's Statutorily-Mandated Risk Management Framework.

Consistent with its statutory obligations, OCC has implemented—and the SEC has approved under Exchange Act Section 19(b)—rules that enable OCC to address risks presented by its clearing members like LSC through various risk management tools. Critically, these rules are reviewed by the Commission and approved *only* when "consistent with" the requirements of the statute. Exchange Act Section 19(b)(2)(C)(i) [15 U.S.C. § 78s(b)(2)(C)(i)]. Three OCC rules are relevant here.

First, under OCC Rule 601(c), OCC "may fix the margin requirement for any account or any class of cleared contracts at such amount as it deems necessary or appropriate under the circumstances to protect the respective interests of Clearing Members, the Corporation, and the public." Second, OCC Rule 609(a) provides OCC the authority to "require the deposit of such additional margin ('intra-day margin') by any Clearing Member in any account at any time during any business day, as such officer deems advisable to reflect changes in," among other things, "the financial position of the Clearing Member, or otherwise to protect the Corporation, other Clearing Members or the general public." Third, OCC Rule 306 authorizes OCC to "require any Clearing Member at any time" to file such reports or financial statements in a form prescribed by OCC, including "for purposes of assessing whether the Clearing Member is meeting the financial requirements for clearing membership on an ongoing basis." These rules ensure that OCC fulfills its statutory obligations by providing OCC with the ability to adjust its risk management controls to address the unique risks that a particular clearing member may present.

In addition, OCC has adopted a Third Party Risk Management Framework—also approved by the SEC—that, among other things, describes how OCC conducts ongoing "Watch Level" reporting and monitoring of its clearing members' financial and operational risks and

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compliance with OCC's membership standards. Pursuant to this Framework, OCC may impose protective measures to limit or eliminate OCC's counterparty exposure, including "changes to margin requirements or composition," if a clearing member approaches or no longer meets minimum membership requirements. *See* Exchange Act Release No. 90406 (Nov. 12, 2020), 85 FR 73582, 73584–85 (Nov. 18, 2020) (SR-OCC-2020-014).[1]

C. OCC Fulfills Its Statutory Obligations By Imposing Protective Measures on Lek Securities.

By letter on October 15, 2021, OCC informed LSC that its Office of the Chief Executive Officer had "elected to impose protective measures" on LSC "due to recent and ongoing developments related to LSC's liquidity risk, operational risk and regulatory risk profiles." LSC Ex. 1. OCC explained that LSC's liquidity risk had "increased due to changes in its lines of credit," including "the phased reduction and ultimate termination of its line of credit with BMO Harris Bank," that its operational risks had increased "due to actions by other self-regulatory organizations in response to [its] heightened liquidity risks," and that its regulatory risks had also increased because OCC "received notice of FINRA's preliminary determination to recommend formal disciplinary action in connection with [LSC's] parent line of credit." *Id.* OCC noted that these developments were "on top of the heightened regulatory risk already present due to the 2019 SEC settlement and three-year engagement with an independent compliance monitor." *Id.*

Based on those developments, OCC implemented two protective measures. First, under OCC Rules 601 and 609, "to mitigate exposures observed in OCC's sufficiency and adequacy stress test shortfalls," OCC increased LSC's additional margin charge from 25% to 50%. *Id.*

[1] OCC's Third-Party Risk Management Policy is available on OCC's public website. *See* OCC, *Third-Party Risk Management Framework* (Dec. 28, 2020), https://www.theocc.com/getmedia/b29f51b3-d3a1-4878-932b-3c697de408f4/third-party-risk-management-framework.pdf.

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This additional margin charge is calculated as a percentage of LSC's margin requirement at OCC, which OCC calculates based on the minimum expected liquidating value of LSC's accounts. *Id.* Second, under OCC Rule 306, OCC required that LSC "provide daily end-of-day liquidity sources and uses reporting covering all available bank lines of credit, parent lines of credit, securities financing, unencumbered cash-on-hand, etc." *Id.* OCC did not assert that LSC had violated any OCC Rule or that the protective measures were being imposed through OCC's disciplinary process. *See id.* One week later, LSC sent OCC a request "under OCC Rule 305(c)" for review of the protective measures. LSC Ex. 2. OCC responded to inform LSC that it "is not entitled to a hearing under Rule 305 or otherwise under the [Exchange Act] to review the use of these risk management tools." LSC Ex. 3. This application followed. LSC Ex. 4.[2]

LEGAL STANDARD

The Commission, like a federal court, has limited jurisdiction. It "lack[s] jurisdiction where Congress has not expressly authorized it." *Jonathan Edward Graham*, Exchange Act Release No. 89237, 2020 WL 3820988, at *3 (July 7, 2020) (Commission opinion). And just like a federal court, the Commission must presume that an action "lies outside this limited jurisdiction." *Kokkonen v. Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 377 (1994); *see John Boone Kincaid III*, Exchange Act Release No. 87384, 2019 WL 5445514, at *4 (Oct. 22, 2019); *cf. Sharemaster v. SEC*, 847 F.3d 1059, 1068 (9th Cir. 2017) (explaining that the Commission has justified its "live-sanction" requirement by "analogizing to doctrines application to Article III courts" and that "it is reasonable for the Commission to assume that Congress legislated against

[2] LSC's application sought a stay of the protective measures. In a letter to the SEC, OCC explained that LSC's request should be denied because its application was invalid and the request was "both procedurally improper and substantively baseless." LSC Ex. 5 n.1. The Commission denied the requested stay, holding that LSC had not "raised a serious legal question on the merits," including whether the Commission had jurisdiction under Section 19(d). *See Lek Securities Corp.*, Exchange Act Release No. 93837, File No. 3-20665 (Dec. 20, 2021).

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the backdrop of mootness and standing doctrines in defining the scope of the Commission's quasi-judicial review authority."). The party asserting jurisdiction bears the burden of overcoming this presumption and establishing jurisdiction. *See Graham*, 2020 WL 3820988, at *3 ("Because [applicant] has not established that Exchange Act Section 19(d) authorizes us to exercise jurisdiction to review his claims, we dismiss his application for review."); *see also Kokkonen*, 511 U.S. at 377. The lack of any other avenue to review or "the alleged importance or necessity" of review of an SRO's action "does not confer jurisdiction" under Section 19(d). *John Boone Kincaid III*, 2019 WL 5445515, at *4; *Graham*, 2020 WL 3820988, at *4.

ARGUMENT

LSC's application improperly seeks to challenge under Section 19(d) OCC's use of protective measures pursuant to OCC Rules that have been approved by the Commission and that OCC has implemented to comply with regulatory requirements, as described in detail above, that are imposed on OCC by the Exchange Act and Commission rules thereunder. As LSC concedes in its application, OCC has the authority under its rules to implement protective measures "under circumstances that would protect the interests and financial positions of Clearing Members, the Corporation and the public," and "can adjust its margin requirement measures as it deems necessary and appropriate." LSC Ex. 4. But LSC says OCC has no power to implement *these* protective measures because they "are based on erroneous information." *Id*. Not so—and LSC cites no authority permitting a challenge to OCC's risk-management protective measures. Instead, LSC attempts to recharacterize the protective measures as an action that "prohibits or limits any person in respect to access to services offered by such organization or member" or "imposes a[] final disciplinary sanction," to try to wedge its petition into the jurisdiction granted the Commission under Section 19(d). [15 U.S.C. § 78s(d)(1)]. But the protective measures OCC

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imposed for risk management reasons neither limit LSC's access to OCC's services nor sanction LSC for any disciplinary violation, so Section 19(d) simply does not apply.

I. Section 19(d) Does Not Authorize a Collateral Attack on the Application of OCC Rules 601, 609, and 306.

LSC improperly seeks to use Section 19(d) to challenge the application of OCC Rules. As explained above, Section 17A(b)(3) and Rule 17Ad-22(e) require OCC to manage the risk arising from its participants so that OCC may ensure the obligations under the financial contracts that OCC clears and settles will be honored even in certain clearing member default scenarios. *See* [15 U.S.C. § 78q-1(b)(3)]; [17 C.F.R. § 240.17Ad-22(e)]. And OCC fulfilled its statutory obligations by adopting Rules that give it the appropriate authority to address idiosyncratic risks presented by clearing members. *See* OCC Rule 601(c) (permitting OCC to "fix the margin requirement for *any account* or any class of cleared contracts at such amount *as it deems necessary or appropriate under the circumstances*" (emphasis added)); OCC Rule 609(a) (giving OCC authority to "require the deposit of such additional margin ('intra-day margin') by *any* Clearing Member in *any account* at *any time* during *any* business day" (emphasis added)); OCC Rule 306 (authorizing OCC to "require *any* Clearing Member at *any time*" to file such reports or financial statements to assess whether the member is meeting financial requirements for clearing membership). The Commission approved these OCC rules through its regulatory review and public comment process required under the Exchange Act. *See, e.g.,* Exchange Act Section 19(b)(2)(C)(i) [15 U.S.C. § 78s(b)(2)(C)(i)].

LSC does not dispute OCC has broad authority to establish, implement, maintain, and enforce a sound risk-management framework to manage the risks posed by clearing members. *See* LSC Ex. 4 (acknowledging that "OCC's Rules provide that OCC can adjust its margin requirement calculation as it deems necessary and appropriate"). Nor does it dispute that the

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protective measures were taken pursuant to OCC's authority under Rules 601(c), 609(a) and 306. Indeed, LSC acknowledges that OCC Rules 601 and 609 "can be implemented under circumstances that would protect the interests and financial positions of Clearing Members, the Corporation and the Public." *See id*.

Instead, LSC mounts a collateral attack on OCC's application of its Rules with nothing more than a mere assertion that OCC exercised its authority "based on erroneous information." *Id.* But jurisdiction under Section 19(d) is not created by unsupported assertions of a factual dispute about the basis for an otherwise non-reviewable action by an SRO within the SRO's discretion. LSC acknowledges that OCC exercised its discretion under its Rules based on stated factual bases. *See* LSC Br. at 2. LSC's application thus claims nothing more than that OCC exercised discretion authorized under its rules, took actions expressly provided for in its rules, and did so for reasons explicitly contemplated by the rules. LSC expressly disavows any claim that OCC acted in bad faith, LSC Br. at 12, and it provides no support for its conclusory assertion that there was some unexplained factual dispute depriving OCC of a rational basis for its determination.

At bottom, LSC cannot use Section 19(d) to collaterally attack the application of OCC Rules. As LSC recognizes in its application, OCC has broad authority to address risks presented by clearing members. *See* LSC Ex. 4. For good reason: The risks presented by clearing members to OCC, other clearing members, and the public are dynamic. OCC's risk management controls and protective measures protect OCC, its clearing members, and the public from present risks and potential future losses. In short, the protective measures are responsive, risk-management measures that OCC must use to satisfy its obligations under the Exchange Act and

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react in light of changing facts and circumstances. Section 19(d) thus affords LSC no ability to challenge the application of these OCC Rules.

II. Lek Securities Has Failed to Carry Its Burden of Establishing that Its Application Falls Within the Commission's Limited Jurisdiction Under Section 19(d) of the Exchange Act.

Even looking past LSC's improper attack on the application of OCC Rules, it has failed to establish that its application falls within the Commission's limited jurisdiction under Section 19(d). Section 19(d)(2) of the Exchange Act grants the Commission jurisdiction "to review" "[a]ny action with respect to which [an SRO] is required by [19(d)(1)] to file notice." 15 U.S.C. § 78s(d)(2). And Section 19(d)(1) of the Exchange Act requires an SRO to "file notice" when an SRO takes action against a member that "prohibits or limits any person in respect to access to services offered by such organization or member" or "imposes any final disciplinary sanction on any member." 15 U.S.C. § 78s(d)(1). LSC therefore must show that OCC has taken an action that "limits [its] access to services offered" by OCC or "imposes a[] final disciplinary sanction" on LSC. *Id.* On both, LSC has failed to carry its burden.

A. The Protective Measures Do Not Limit Lek Securities' Access to Services Offered by OCC.

The protective measures imposed by OCC do not limit LSC's access to services. To understand what is a limit on access to OCC's services, "[w]e start, of course, with the statutory text." *BP Am. Prod. Co. v. Burton*, 549 U.S. 84, 91 (2006). Unless otherwise defined, the statute's words are interpreted as taking their "ordinary, contemporary, common meaning." *Perrin v. United States*, 444 U.S. 37, 42 (1979). In common parlance, "access" means "the right to enter, approach, or use; admittance." *Webster's New World Dictionary* (2d ed. 1974); *see also* Merriam-Webster Online ("permission, liberty, or ability to enter [or] approach"); *Graham*, 2020 WL 3820988, at *3. Thus, to fall within this statutory language, LSC needed to show that the

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protective measures limit its right to enter, approach, or use "fundamentally important" services offered by OCC that are "central to [OCC's] function." *See Graham*, 2020 WL 3820988, at *3. It has not done so.

Based on the liquidity, operational, and regulatory risk presented by LSC, OCC imposed on LSC two protective measures. LSC's brief focuses on only one: OCC's decision to increase its additional margin charge from 25% to 50% pursuant to OCC Rules 601 and 609.[3] *See generally* LSC Br.; LSC Ex. 1. But right-sizing a margin charge does not limit LSC's right to enter, obtain, or use OCC services. OCC provides—and LSC utilizes—clearing and settlement services. The margin charge sets the terms by which LSC *uses* these services—it does not limit LSC's right to enter or to use these services.

For this reason, OCC's authority to set margin requirements for each of its members is not among those measures that fall within the limitations and restrictions on clearing activity for which OCC's Rules *do* provide clearing members a right to appeal. OCC Rule 305(c), approved by the SEC under Exchange Act Section 19(b), limits a clearing member's right to appeal to actions taken by an authorized OCC officer pursuant to Rule 305. This rule sets out seven categories of OCC action that clearing members may appeal, including an action prohibiting or limiting "opening purchase transactions or opening writing transactions," requiring a clearing member to "reduce or eliminate existing unsegregated long positions or short positions" in its accounts, and requiring a clearing member "to reduce or eliminate existing stock loan positions

[3] Though LSC's application purports to challenge Rule 306, LSC fails to mention Rule 306 or the protective measure requiring LSC to provide daily end-of-day liquidity sources and uses reporting in the Argument section of its brief. *See* LSC Br. 5–13. For that reason, this argument has been waived. *See, e.g.*, *Anthony Field*, Exchange Act Release No. 4028, 2015 WL 728005, at *19 n.115 (Feb. 20, 2015) ("[A]rguments for reversal not made in the opening brief are waived."). Even if the Commission were to find that LSC did not waive this argument, it fails

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or stock borrow positions." OCC Rule 305(a).[4] The protective measures here—requiring LSC to deposit additional margin and provide additional liquidity reporting (*i.e.*, email to OCC a document LSC already prepares for other purposes)—do not fall within these types of prohibitions and limitations.[5]

Indeed, LSC's principal argument concedes that these protective measures do not limit its ability to access OCC's services. LSC says that these protective measures "constrain" its access to OCC's services, but just a sentence later LSC admits that the protective measures in fact "[e]ffectively . . . limit *the volume of customer transactions* that LSC can clear and settle through OCC." LSC Br. at 6 (emphasis added). Thus, as LSC recognizes, it has access to—*i.e.*, the right to use—OCC's clearing and settlement services. LSC simply wants the terms of its use to be different. LSC's position, moreover, is unworkable and has no limiting principle. Under LSC's reading, *any* margin charge "limits" a clearing member's "access to services offered" by OCC.[6] That is because *any* margin charge, no matter how small, would flunk LSC's test: it would "limit

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for the same reasons as LSC's challenge to the protective measure under Rules 601 and 609. *See* § 2.

[4] OCC had previously imposed stock loan restrictions on LSC under Rule 305. LSC appealed these restrictions to the Risk Committee and then filed an application for review with the SEC. As LSC admitted in its voluntary motion to dismiss, OCC lifted the protective measure, rendering its application moot. *Lek Securities Corp.*, Exchange Act Release No. 93281, File No. 3-20619 (Dec. 17, 2021).

[5] A clearing member may also appeal a suspension of its clearing membership under OCC Rule 1110. However, the protective measures do not constitute a suspension of LSC's membership under Rule 1102.

[6] In other words, *each* of OCC's 105 clearing members could file *tomorrow* an application under Section 19(d) challenging the margin requirements OCC has imposed on it. And under LSC's view, the Commission would have jurisdiction. That is incorrect. As LSC's unworkable position shows, the purported limitations it complains of are inherent in (and an essential part of) the services OCC provides to *all* clearing members—not a limitation on access to its services. *See, e.g.*, Rule 17Ad-22(e)(4) [17 C.F.R. § 240.17Ad-22(e)(4)(i)].

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the volume of customer transactions that [a clearing member] can clear and settle through OCC." LSC Br. at 6. Nothing in the statute's text supports that reading.

Nor does the structure of Section 19 of the Exchange Act. *See Mellouli v. Lynch*, 575 U.S. 798, 809 (2015) ("Statutes should be interpreted 'as a symmetrical and coherent regulatory scheme.'"). Under Section 19(f), if the Commission concludes that an SRO's Section 19(d) limitation violates the Exchange Act, the Commission must provide a two-part remedy. First, it must "set aside the action" of the SRO. 15 U.S.C. § 78s(f). Second, it must "grant [the aggrieved] person access to [the SRO's] services." *Id.* But here, the Commission could not grant LSC access to OCC's clearing and settling services; LSC already has access to those services—it has a right to use (and does use) them. In fact, it is only when LSC is *using* those services that it must—like every other OCC clearing member—satisfy its margin requirements.

Without any support from the text or structure, LSC resorts to misquoting the Commission's adopting release for its rules under Section 19(d). *See* LSC Br. at 6. LSC contends "the Commission indicated that it would expect to review both disciplinary actions and 'other kinds of *administrative* actions' that are 'quite similar.'" LSC Br. at 5–6 (emphasis added). That is incorrect. In adopting Rule 19d-1, the Commission actually noted that "'disciplinary actions' include (for reporting purposes) other kinds of *adjudicatory* action which, while not treated by the Act in precisely the same framework as disciplinary matters, are, as a practical matter, quite similar."[7] Thus, contrary to LSC's contention, nowhere did the Commission say it expected non-adjudicatory administrative actions to be "disciplinary actions" reviewable under Section 19(d). Rather, the Commission explained that the term "disciplinary

[7] *See* Exchange Act Release No. 13726 (July 14, 1977), 42 FR 36410, 36412 (Aug. 15, 1977) (emphasis added).

actions *include[s]* . . . other kinds of *adjudicatory* action." *Id.* (emphasis added). LSC does not contend that the protective measures were the result of an adjudicatory action by OCC.

LSC finally turns to decisions by the Commission, but all miss the mark because they look nothing like the routine risk-management actions taken by OCC. LSC starts with *Securities Industry and Financial Markets Association* ("*SIFMA*"), where SIFMA challenged rule changes by two SROs that allowed the SROs to charge for certain exchange data previously made available at no cost. Exchange Act Release No. 1921, File No. 3-15350, 2014 SEC LEXIS 3906 (Oct. 20, 2014). But the court of appeals reversed, holding that "Section 19(d) is not available as a means to challenge the reasonableness of generally-applicable fee rules." *NASDAQ Stock Market, LLC v. SEC*, 961 F.3d 421, 424 (D.C. Cir. 2020). So too here: risk-adjusted margin requirements are a generally-applicable tool that OCC uses with *each* of its clearing members.

LSC tries to wriggle within the court's language noting that, "for a fee rule to be challengeable under Section 19(d), it must, *at a minimum*, be targeted at specific individuals or entities." *Id.* at 427–28 (emphasis added); *see* LSC Br. at 7 (arguing that the margin charges "specifically target LSC"). But again, *each* OCC clearing member has margin charges that OCC imposes based on the risk level presented by each clearing member. The margin charges thus do not target LSC: OCC issues margin reports to each of its 105 clearing members each business day, and it often increases margin requirements based on the idiosyncratic risks a clearing member presents pursuant to stated policies and practices. *See* OCC Rule 609 (permitting OCC to require the deposit of additional margin "by any Clearing Member . . . at any time during any business day"); OCC's Third-Party Risk Management Policy, *supra* note 1 (providing that OCC monitors all its clearing member relationships and may act to protect OCC, including by "changes to margin requirements or composition"). And in any event, LSC misreads the

language from *SIFMA*. The Commission noted that, for it to exercise jurisdiction under Section 19(d), a fee rule must—"at minimum"—target a specific party. In other words, targeting is necessary but not sufficient for the Commission to exercise jurisdiction under Section 19(d).

LSC next points to *William J. Higgins*, where the Commission reasoned that the NYSE had limited access to services when it denied two members permission to install telephones to communicate from the exchange floor to non-members located off-floor. *William J. Higgins*, Exchange Act Release No. 24429, 1987 WL 757509, at *2 (May 6, 1987). But there the Commission recognized that it had jurisdiction and "must set aside any SRO action that imposes a limitation on access *when the action is not taken pursuant to a rule of the SRO*." *Id.* at *14 (emphasis added). Years earlier, the Commission had stated that, "in the absence of a rule prohibiting non-member telephone access to the trading floor, such access constitutes a service which could be offered by members to non-members." *Id.* at *5. Thus, unlike here, *see* OCC Rule 601 and 609, the SRO in *Higgins* took action without authority under its own rules. And in any event, OCC's action setting margin requirements looks nothing like the action in *Higgins*, which summarily and completely denied non-members telephone access to the floor.

For much the same reasons, LSC fares no better with *Consolidated Arbitration Applications*, Exchange Act Release No. 89495, 2020 WL 4569083 (Aug. 6, 2020). There, though FINRA's corporate charter stated that one of its functions was "[t]o promote self-discipline among members, and to investigate and adjust grievances between the public and members and between members," it denied persons from FINRA member firms "access to FINRA's arbitration forum to seek expungement of prior adverse arbitration awards arising from customer disputes." *Id.* at *1–2. Once again, the wholesale denial of access to an arbitration forum looks nothing like OCC's actions here: LSC still has access to OCC's clearing and settling

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services—it just wants a lower margin requirement. LSC's final case is inapposite for the same reasons. *See Int'l Power Grp., Ltd.*, Exchange Act Release No. 66611, 2012 SEC LEXIS 844, at *16–18 (Mar. 15, 2012) (appealing from DTC's decision to "suspend indefinitely book-entry clearing and settlement services to its Participants with respect to IPWG's common stock," which "affect[ed] all transactions in [the] suspended securities").

LSC has failed to carry its burden of establishing that OCC's imposition of an increased margin charge limits its access to services offered by OCC. And to the extent there is any doubt about that (though there is not), OCC's interpretation of its own rules is afforded substantial deference. *See Heath v. SEC*, 586 F.3d 122, 138–39 (2d Cir. 2009) (collecting cases and acknowledging its "obligation to afford some level of deference to [SROs] interpretation of [its own] rules"); *cf. Fogel v. Chestnutt*, 533 F.2d 731, 753 (2d Cir. 1975) (Friendly, J.) ("[A]n exchange has a substantial degree of power to interpret its own rules."), *cert. denied*, 429 U.S. 824 (1976). Accordingly, the Commission lacks jurisdiction to grant LSC's application for review on that ground.

B. The Protective Measures Do Not Constitute Final Disciplinary Sanctions.

The protective measures imposed by OCC also do not constitute a final disciplinary sanction on LSC. "Section 19(d) grants [the Commission] jurisdiction to review only those disciplinary actions in which a final disciplinary sanction is imposed." *Sky Capital LLC*, Exchange Act Release No. 55828, 2007 WL 1559228, at *3 (May 30, 2007). "[A] disciplinary action is an action that responds to an alleged violation of an SRO rule or Commission statute or rule, or an action in which a punishment is sought or intended." *Eric David Wanger*, Exchange Act Release No. 79008, 2016 WL 5571629, at *3 (Sept. 30, 2016) (cleaned up); *see* OCC Rule 1201(a) (providing that, in imposing disciplinary sanctions, OCC "may censure, suspend, expel or limit the activities, functions or operations of any Clearing Member *for any violation* of the

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By-Laws and Rules or its agreements with [OCC]" (emphasis added)). Here, LSC has failed to show that OCC imposed these protective measures as a "punishment" or that they were imposed in response to a "violation" by LSC of OCC's by-laws or rules.

OCC has not found that LSC committed any violation and has not imposed any disciplinary sanction or punishment. As explained above, consistent with its regulatory requirements, OCC has applied its Rules, policies, and procedures—many approved by the SEC—to increase margin requirements addressing idiosyncratic risks presented by a clearing member. Thus, the margin requirements imposed on LSC—just like those imposed on other clearing members—are not a sanction for any violation. Rather, the margin requirements are risk management tools that form part of OCC's core statutory duty to "establish, implement, maintain and enforce" a "sound risk management framework for comprehensively managing," among other things, "credit and liquidity risks . . . that arise in or are borne by [OCC]." Rule 240.17Ad-22(e)(3) [17 C.F.R. § 240.17Ad-22(e)(3)].

Indeed, the SEC has charged OCC to "[e]ffectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by" requiring its clearing members to maintain—with a "high degree of confidence"—"sufficient financial resources to cover [OCC's] credit exposure to each participant." Rule 17Ad-22(e)(4) [17 C.F.R. § 240.17Ad-22(e)(4)]. And OCC "effectively . . . manage[s]" its credit exposures, *id.*, by fixing the margin requirements for its clearing members, OCC Rule 601(c). Thus, as OCC explained in its October 15, 2021 letter, OCC increased LSC's margin charge "to mitigate exposures observed in OCC's sufficiency and adequacy stress test shortfalls"—not because LSC committed a violation. LSC Ex. 1.

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LSC's position once again has no limiting principle and completely disregards OCC's statutory obligations. LSC says that "OCC here made an assessment of purported wrongdoing" by LSC. LSC Br. at 9. Not so. As explained in its letter imposing these protective measures, OCC simply "observed [its] sufficiency and adequacy stress test shortfalls" and chose to use routine risk management tools to manage the range of risks presented by "recent and ongoing developments related to [LSC's] liquidity risk, operational risk and regulatory risk profiles." LSC Ex. 1; *see* Rule 17Ad-22(e)(3) [17 C.F.R. § 240.17Ad-22(e)(3)]. LSC's entire application and brief rest on the mistaken view that the effects of complying with protective measures imposed under OCC Rules are akin to disciplinary sanctions for *violating* OCC rules. There is no basis in the text or the structure of this regulatory scheme to equate the two and thereby bring this case within the Commission's jurisdiction.

The only decision LSC cites to support its position in fact provides no support at all. LSC Br. at 9 (citing *Morgan Stanley & Co., Inc.*, Exchange Act Release No. 34-39459, 1997 SEC LEXIS 2598 (Dec. 17, 1997)). There, Morgan Stanley argued that the Commission had jurisdiction under Section 19(d) to review the National Association of Securities Dealers (NASD) denial of its request for an exemption from a two-year prohibition on engaging in municipal securities business in a state. *Id.* at *7. But the Commission dismissed the application for review, holding that it did not have jurisdiction under Section 19(d), because NASD's denial "did not impose 'a punishment or sanction'" and thus "was not a disciplinary action" under the Exchange Act. *Id.* at *8. "In a disciplinary action," the Commission explained, "a sanction is imposed following a determination of wrongdoing." *Id.* But NASD made "no determination" or "finding" of "wrongdoing." *Id.* In other words, NASD "did not make any assessment of whether [a Morgan Stanley employee's] contribution was wrongful." *Id.* at *7. Rather, when

NASD denied the request for an exemption, it "merely exercise[ed] the discretionary authority granted it under the rule." *Id.*

So too here. OCC did not make any "assessment" of whether LSC committed any "wrongdoing." *See* LSC Ex. 1. It merely exercised its discretionary authority pursuant to its obligation to monitor and manage risk. OCC Rule 601(c), 609; Rule 17Ad-22(e)(3) [17 C.F.R. § 240.17Ad-22(e)(3)]. Thus, the Commission lacks jurisdiction under Section 19(d) here for the same reasons it lacked jurisdiction in *Morgan Stanley*. *Cf. Fogel*, 533 F.2d at 753; *Shultz v. SEC*, 614 F.2d 561, 571 (7th Cir. 1980) ("[B]ecause these are rules of the Exchange, the Exchange should be allowed discretion in determining their meaning.").

LSC's contrary position find no support in the text or the Commission's precedent and is unworkable. *See* LSC Br. at 10 ("The harm done to the member should be critical to the determination" of whether OCC imposed a "final disciplinary sanction."); *id.* at 13 (claiming, without citation, that "Congress intended the Commission to have broad authority to review SRO actions that are detrimental to members of the SRO"). For decades, the Commission has reiterated that an "SRO action is not reviewable merely because it adversely affects the applicant." *E.g.*, *Graham*, 2020 WL 3820988 at *4 (cleaned up); *see also Joseph Dillon & Co.*, Exchange Act Release No. 43523, 2000 WL 1664016 (Nov. 6, 2000) (Commission opinion). If OCC were obligated to notify the SEC of every risk management action taken against a clearing member, then any margin call or request for information directed at a clearing member would become an event subject to such a notice and potential challenge, leading to a proliferation of

notices from the OCC to the SEC and flooding the SEC with applications asking it to second guess the OCC's administration of its own rules.[8]

Finally, LSC's pleas that OCC's action imposes "onerous burdens and significant costs," LSC Br. at 10, provide no support for exercising jurisdiction under Section 19(d). *John Boone Kincaid III*, 2019 WL 5445514, at *4 ("[T]he alleged importance or necessity of our review does not confer jurisdiction where we have determined Congress has not authorized it: we will not review [an SRO] action simply because an applicant claims 'extraordinary circumstances' or 'compelling reasons.'"); *Allen Douglas Sec., Inc.*, Exchange Act Release No. 50513, 2004 WL 2297414, at *2 n.14 (Oct. 12, 2004) (explaining that the Commission has refused to consider the importance or significance of SRO action "as a basis for review where the appeal did not satisfy the jurisdictional requirements set forth in Section 19(d)"). OCC's specific application of its Commission-approved risk management framework is not subject to further review upon a participant's petition under Section 19(d). *See Graham*, 2020 WL 3820988, at *4 ("The lack of a mechanism for the relief [sought] does not confer jurisdiction . . . where Congress has not authorized it."). Accordingly, the Commission should follow the text and its precedent and conclude that the protective measures here do not constitute a final disciplinary sanction.

[8] Section 19(d) places the burden on the SRO to notify the SEC when the SRO's internal review process is complete and the sanction or disciplinary action becomes final. *Id.* If OCC were obligated to notify the SEC of *every* routine risk management action taken, any margin call or request for information directed to a clearing member would become an event subject to such notice and potential challenge. That would bury OCC in notices to be submitted to the SEC: OCC issues margin reports to each of its approximately 105 clearing members *each business day*, and *each* of these routine margin reports would be (in LSC's view) potentially subject to review by the Commission. Section 19(d) does not countenance such a waste of resources. Rather, the Exchange Act delegated such risk management functions to OCC, subject to the Commission's review and approval of OCC's rules.

CONCLUSION

For the foregoing reasons, the Commission should dismiss LSC's application for lack of jurisdiction under Section 19(d) of the Exchange Act.

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Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to the Commission's Rule of Practice 420(f), I hereby certify that I have omitted or redacted any sensitive personal information, as defined by Rule of Practice 420(e)(2), from this filing.

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CERTIFICATE OF SERVICE

I hereby certify that on February 23, 2022, I caused a true and correct copy of the foregoing to be electronically filed using the Commission's Electronic Filings in Administrative Proceedings (eFAP) system. I further certify that I caused a true and correct copy of the foregoing to be served by electronic mail on the following:

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