open-end management investment company under the Act. Applicants seek relief with respect to ten Funds (as defined below, and those Funds, the ''Initial Funds''). The Funds will operate as ActiveShares ETFs as described in the Reference Order.[2]

2. The Adviser, a New York limited liability company, will be the investment adviser to the Initial Funds. An Adviser (as defined below) will serve as investment adviser to each Fund. The Adviser is, and any other Adviser will be, registered as an investment adviser under the Investment Advisers Act of 1940 (''Advisers Act''). The Adviser may enter into sub-advisory agreements with other investment advisers to act as sub-advisers with respect to the Funds (each a ''Sub-Adviser''). Any Sub-Adviser will be registered under the Advisers Act.

3. The Distributor is a Delaware limited liability company and a broker-dealer registered under the Securities Exchange Act of 1934, as amended, and will act as the principal underwriter of Shares of the Funds. Applicants request that the requested relief apply to any distributor of Shares, whether affiliated or unaffiliated with the Adviser and/or Sub-Adviser (included in the term ''Distributor''). Any Distributor will comply with the terms and conditions of the Order.

Applicants' Requested Exemptive Relief

4. Applicants seek the requested Order under section 6(c) of the Act for an exemption from sections 2(a)(32), 5(a)(1), and 22(d) of the Act and rule 22c–1 under the Act, under sections 6(c) and 17(b) of the Act for an exemption from sections 17(a)(1) and 17(a)(2) of the Act, and under section 12(d)(1)(J) of the Act for an exemption from sections 12(d)(1)(A) and 12(d)(1)(B) of the Act. The requested Order would permit applicants to offer ActiveShares ETFs. Because the relief requested is the same as the relief granted by the Commission under the Reference Order and because the Adviser has entered into a licensing agreement with Precidian Funds LLC in order to offer ActiveShares ETFs,[3] the Order would incorporate by reference the terms and conditions of the Reference Order.

5. Applicants request that the Order apply to the Initial Funds and to any other existing or future open-end management investment company or series thereof that: (a) Is advised by the Adviser or any entity controlling, controlled by, or under common control with the Adviser (any such entity included in the term ''Adviser''); (b) operates as an ActiveShares ETF as described in the Reference Order; and (c) complies with the terms and conditions of the Order and of the Reference Order, which is incorporated by reference into the Order (each such company or series and any Initial Fund, a ''Fund'').[4]

6. Section 6(c) of the Act provides that the Commission may exempt any person, security or transaction, or any class of persons, securities or transactions, from any provisions of the Act, if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act. Section 17(b) of the Act authorizes the Commission to exempt a proposed transaction from section 17(a) of the Act if evidence establishes that the terms of the transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, and the transaction is consistent with the policies of the registered investment company and the general purposes of the Act. Section 12(d)(1)(J) of the Act provides that the Commission may exempt any person, security, or transaction, or any class of persons, securities or transactions, from any provision of section 12(d)(1) if the exemption is consistent with the public interest and the protection of investors. Applicants submit that for the reasons stated in the Reference Order the requested relief meets the exemptive standards under sections 6(c), 17(b) and 12(d)(1)(J) of the Act.

For the Commission, by the Division of Investment Management, pursuant to delegated authority.

Jill M. Peterson,

Assistant Secretary.

[FR Doc. 2019–24468 Filed 11–8–19; 8:45 am]

BILLING CODE 8011–01–P

[2] To facilitate arbitrage, an ActiveShares ETF disseminates a ''verified intraday indicative value'' or ''VIIV,'' reflecting the value of its portfolio holdings, calculated every second during the trading day. To protect the identity and weightings of its portfolio holdings, an ActiveShares ETF sells and redeems its Shares in creation units to authorized participants only through an unaffiliated broker-dealer acting on an agency basis.

[3] Aspects of the Funds are covered by intellectual property rights, including but not limited to those which are described in one or more patent applications.

[4] All entities that currently intend to rely on the Order are named as applicants. Any other entity that relies on the Order in the future will comply with the terms and conditions of the Order and of the Reference Order, which is incorporated by reference into the Order.

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–87476; File No. SR–OCC–2019–807]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Advance Notice Related to Proposed Changes to The Options Clearing Corporation's Rules, Margin Policy, Margin Methodology, Clearing Fund Methodology Policy, and Clearing Fund and Stress Testing Methodology To Address Specific Wrong-Way Risk

November 6, 2019.

Pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, entitled Payment, Clearing and Settlement Supervision Act of 2010 (''Clearing Supervision Act'') [1] and Rule 19b–4(n)(1)(i) [2] under the Securities Exchange Act of 1934 (''Act'' or ''Exchange Act''),[3] notice is hereby given that on October 10, 2019, the Options Clearing Corporation (''OCC'') filed with the Securities and Exchange Commission (''Commission'') an advance notice as described in Items I, II and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the advance notice from interested persons.

I. Clearing Agency's Statement of the Terms of Substance of the Advance Notice

This advance notice is submitted in connection with proposed enhancements to OCC's Rules, margin policy and methodology, Clearing Fund policy, and Clearing Fund and stress testing methodology to adopt new margin charges and other risk measures to address the specific wrong-way risk presented by certain cleared positions.

The proposed amendments to OCC's Rules are included in Exhibit 5A of the filing. The proposed amendments to OCC's Margin Policy and Margins Methodology are included in Exhibits 5B and 5C, respectively. The proposed amendments to OCC's Clearing Fund Methodology Policy (''CFM Policy'') and Stress Testing and Clearing Fund Methodology Description (''Methodology Description'') are included in Exhibits 5D and 5E, respectively. Material proposed to be added to the Rules, Margin Policy and Margins Methodology as currently in effect is marked by underlining, and

[1] 12 U.S.C. 5465(e)(1).

[2] 17 CFR 240.19b–4(n)(1)(i).

[3] 15 U.S.C. 78a *et seq.*

material proposed to be deleted is marked in strikethrough text; however, the proposed Specific Wrong-Way Risk Add-On chapter of the Margins Methodology is presented without marking to improve readability as the entire chapter is newly proposed rule text.[4] Material proposed to be added to the CFM Policy and Methodology Description is marked by double underlining, and material proposed to be deleted is marked in double strikethrough text.[5]

The advance notice is available on OCC's website at *https://www.theocc.com/about/publications/bylaws.jsp.* All terms with initial capitalization that are not otherwise defined herein have the same meaning as set forth in the OCC By-Laws and Rules.[6]

II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Advance Notice

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

(A) Clearing Agency's Statement on Comments on the Advance Notice

Written comments were not and are not intended to be solicited with respect to the advance notice and none have been received. OCC will notify the Commission of any written comments received by OCC.

(B) Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing, and Settlement Supervision Act

Description of the Proposed Change

Background

As a central counterparty (''CCP''), OCC is exposed to wrong-way risk, which is the risk that arises when exposure to a counterparty is adversely correlated with the credit quality and probability of default of that counterparty. Specific wrong-way risk (''SWWR'') arises when an exposure to a participant is highly likely to increase when the creditworthiness of that participant is deteriorating.[7] For example, SWWR arises where a Clearing Member's cleared positions contain equity securities issued by the Clearing Member or its affiliates (*i.e.,* the Clearing Member Group) (such positions referred to herein as ''SWWR Equity positions'') as the equity issued by the Clearing Member Group may be assumed to have a price at or near zero in a default or bankruptcy scenario, and those positions (*e.g.,* equity used as a hedge, stock loans, options on equity, single-stock futures) may experience substantial losses. In addition, SWWR may arise where uncollateralized exchange-traded notes (''ETNs'') issued by a Clearing Member or its affiliates (''SWWR ETN positions'') are part of the Clearing Member's cleared positions (these positions, collectively with ''SWWR Equity positions,'' are hereinafter referred to as ''SWWR positions''). SWWR may also arise when a Clearing Member posts equity securities or ETNs issued by it or of its affiliates as margin collateral.

OCC currently accounts for SWWR as it relates to margin collateral by generally prohibiting a Clearing Member from pledging equities issued by it or one of its affiliates as margin collateral unless this pledge provides a hedge against a cleared position in the same account.[8] OCC does not, however, currently account for SWWR as it relates to cleared positions. As a result, OCC is proposing a new ''add-on'' charge [9] for its margin methodology, the System for Theoretical Analysis and Numerical Simulations (''STANS''),[10] and new stress test scenarios that may result in intra-day margin calls and, in more extreme cases, intra-month increases in the size of OCC's Clearing Fund [11] to address the wrong-way risk of OCC's cleared positions involving Clearing Member-issued securities. In addition, OCC proposes to introduce certain restrictions on stock lending activity related to SWWR positions.

Proposed Changes

OCC proposes to enhance its management of SWWR by: (1) Imposing certain restrictions on stock lending activity at OCC; (2) adopting a new SWWR margin add-on for STANS (''SWWR Add-on''); (3) introducing new stress test scenarios to capture the SWWR of cleared positions involving Clearing Member-issued ETNs beyond certain pre-defined thresholds; and (4) making other clarifying and conforming changes to the CFM Policy and Methodology Description. The proposed changes are intended to address the credit risks arising from SWWR positions at OCC. The proposed changes are described in detail below.

1. Prohibition on Lending Clearing Member/Affiliate-Issued Securities

OCC operates two programs for stock loan transactions: (1) The Stock Loan/Hedge Program and (2) the Market Loan Program (collectively, the ''Stock Loan Programs''). In the Stock Loan/Hedge Program, prospective Lending and Borrowing Clearing Members identify each other (independent of OCC), agree to bilaterally negotiated terms of the stock loan (in this case, a ''Hedge Loan''), and then send the details of the stock loan to the Depository Trust Company (''DTC'') designating the stock loan as a Hedge Loan for guaranty and clearance at OCC. The Lending Clearing Member then instructs DTC to transfer

[4] OCC also has filed a proposed rule change with the Commission in connection with the proposed changes. *See* SR–OCC–2019–010.

[5] OCC also filed with the Commission proposed rule change and advance notice filings concerning enhancements to its CFM Policy and Methodology Description, which are currently pending Commission review. *See* OCC filings SR–OCC–2019–009 and SR–OCC–2019–806. OCC has marked proposed changes to the CFM Policy and Methodology Description described herein in double marking to clearly differentiate those changes from other changes currently pending Commission review.

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

[7] *See* Securities Exchange Act Release No. 78961 (September 28, 2016), 81 FR 70786, 70816, n. 317 (October 13, 2016) (S7–03–14) (''Standards for Covered Clearing Agencies''). *See also* Committee on Payment and Settlement Systems and Technical Committee of the International Organization of Securities Commissions, *Principles for financial market infrastructures* (Apr. 16, 2012), available at *http://www.bis.org/publ/cpss101a.pdf.*

[8] *See* OCC Rule 604, Interpretation and Policy .16.

[9] Under OCC's Margin Policy, OCC may collateralize certain exposures through the use of add-on charges.

[10] *See* Securities Exchange Act Release No. 53322 (February 15, 2006), 71 FR 9403 (February 23, 2006) (SR–OCC–2004–20). A detailed description of the STANS methodology is available at *http://optionsclearing.com/risk-management/margins/.*

[11] Under OCC's existing stress testing and Clearing Fund methodology, OCC runs on a daily basis a set of stress test scenarios designed to measure the exposure of the Clearing Fund to the portfolios of individual Clearing Member Groups and determine whether any such exposure is sufficiently large as to necessitate OCC calling for additional resources so that OCC continues to maintain sufficient financial resources to guard against potential losses under a wide range of stress scenarios, including extreme but plausible market conditions (''Sufficiency Scenarios,'' and such scenarios collectively constituting ''Sufficiency Stress Tests''). *See* Securities Exchange Act Release No. 83714 (July 26, 2018), 83 FR 37570 (August 1, 2018) (SR–OCC–2018–803) and Securities Exchange Act Release No. 83735 (July 27, 2018), 83 FR 37855 (August 2, 2018) (SR–OCC–2018–008). Under OCC Rule 609, the CFM Policy, and the Methodology Description, if a Sufficiency Stress Test identifies exposures that exceed 75% of the current Clearing Fund requirement less deficits (the ''75% threshold'' or ''Sufficiency Stress Test Threshold 1''), OCC may require additional margin deposits from the Clearing Member Group(s) driving the breach. If a Sufficiency Stress Test identifies exposures that exceed 90% of the current Clearing Fund, OCC would perform an intra-month resizing of the Clearing Fund. *Id.*

a specified number of shares of Eligible Stock [12] to the account of the Borrowing Clearing Member, and the Borrowing Clearing Member instructs DTC to transfer the appropriate amount of cash collateral to the account of the Lending Clearing Member. In the Market Loan Program, stock loans are initiated through the matching of bids and offers that are either agreed upon by the Market Loan Clearing Members or matched anonymously through a Loan Market (such stock loans being ''Market Loans''). In order to initiate a Market Loan, the Loan Market sends a matched transaction to OCC, which in turn sends two separate but linked settlement instructions to DTC to effect the movement of Eligible Stock and cash collateral between the accounts of the Market Loan Clearing Members through OCC's account at DTC.

Regardless of whether a transaction is initiated under the Stock Loan/Hedge Program or Market Loan Program, OCC novates the transaction and becomes the lender to the Borrowing Clearing Member and the borrower to the Lending Clearing Member. As the principal counterparty to the Borrowing and Lending Clearing Members, OCC guarantees the return of the full value of cash collateral to a Borrowing Clearing Member and guarantees the return of the Loaned Stock (or value of that Loaned Stock) to the Lending Clearing Member.[13] As noted above, OCC may be exposed to SWWR in its Stock Loan Programs where Clearing Members lend equity securities or ETNs issued by the Clearing Member or its affiliates. Specifically, the lending of Clearing Member or Member Affiliate-issued equity or ETNs creates a long exposure and liability in the case when a Clearing Member defaults and its own or affiliated equity or ETN declines.

OCC proposes to mitigate SWWR in its Stock Loan Programs by prohibiting Clearing Members from lending any Eligible Stock issued by such Clearing Member or any affiliate of such Clearing Member. The proposed restriction would apply to both SWWR Equity positions and SWWR ETN positions. OCC does not believe that the proposed restriction on lending SWWR Equity positions would have a material impact on Clearing Members in the Stock Loan Programs as Clearing Members do not typically engage in lending of their own equity securities and borrowers typically do not accept equity securities issued by their lending counterparty.[14] The proposed restrictions on lending SWWR ETN positions would, however, impact a very small segment of Clearing Members that lend SWWR ETNs.[15] OCC believes that the impact of the proposed changes would be limited by the fact that, unlike listed options, Clearing Members are able to lend SWWR positions on an uncleared basis outside of OCC. The proposed restrictions on lending activity in the Stock Loan Programs would not prevent Clearing Members from lending equities or ETNs issued by the Clearing Member or any affiliate of such Clearing Member on a bilateral basis if members wish to do so.

The proposed prohibition on lending Clearing Member or Member Affiliate-issued Eligible Stock would be included in new OCC Rules 2202(f) and 2202A(f) for the Stock Loan/Hedge Program and Market Loan Program, respectively. OCC would also make conforming changes to its Margin Policy and Margins Methodology to reflect the newly proposed restrictions in stock lending activity.

The proposed change would only apply to stock lending activity as of the time of implementation of the proposed change. The proposed change would not be applied retroactively to existing open positions, and Clearing Members with open stock loans involving Clearing Member or Member Affiliate-issued Eligible Stock would not be forced to terminate those existing positions. Any SWWR stock lending positions in existence as of the implementation of the proposed change would be subject to the SWWR charges described below until such positions are closed out through the normal course stock loan termination process.

2. SWWR Add-on

OCC proposes to adopt a new margin add-on (*i.e.,* the SWWR Add-on) to address SWWR from cleared positions involving Clearing Member and affiliate issued equities and ETNs. The SWWR Add-on would be calculated for each margin tier account of a Clearing Member Group having positions related to either publicly traded equities or ETNs issued by the Clearing Member Group and would cover all types of positions (equity used as collateral, equity and ETN options, single-stock futures). The proposed SWWR Add-on is comprised of three main components: (1) ''SWWR Equity Charge,'' (2) ''SWWR ETN Charge,'' and (3) ''SWWR Residual.'' Each of these components is discussed below.

a. SWWR Equity Charge

Under the proposal, when a Clearing Member defaults, it is assumed that the price of any equity security issued by the Clearing Member Group would fall to zero. As a result, OCC would calculate the SWWR Equity Charge by assuming that a Clearing Member's and its affiliates' equity securities would be priced at zero and value all cleared positions accordingly (*i.e.,* all stocks, single stock futures, call options, and put options would be valued at zero) to provide full protection for the risk of potential market exposure to products on a Clearing Member Group's own equity in a default or bankruptcy scenario. In each margin account, the profit and loss (''P&L'') of SWWR Equity positions would be calculated as the difference of the theoretical value of such securities (*i.e.,* zero) and the closing price of the position multiplied by the net quantity.[16] Moreover, any potential gain from the SWWR positions would be excluded by flooring the SWWR Equity Charge at zero.[17] As a result, OCC believes that the proposed SWWR Equity Charge would adequately cover the SWWR arising from a Clearing Member's SWWR Equity positions.

[12] OCC's By-Laws define ''Eligible Stock'' to mean, in part, any security that is eligible for lending in the Stock Loan/Hedge Program and the Market Loan Program. *See* Article I, Section 1.E(3) of the OCC By-Laws. Eligible Stock may include ETNs issued by OCC's Clearing Members.

[13] Under the Market Loan Program, OCC also provides a limited guaranty of dividend and rebate payments.

[14] As of the start of September 2019, OCC had 107 Clearing Members, of which 64 have member or affiliate-issued securities eligible for lending in the Stock Loan Programs. OCC analyzed SWWR Equity lending activity for its Clearing Members from January 2018 through the beginning of September 2019. During this period, less than 10 Clearing Members had stock lending activity in SWWR Equity positions, and loans of SWWR Equity positions constituted less than three percent of each of those Clearing Members' average notional stock lending activity for the period.

[15] OCC analyzed SWWR ETN lending activity for its Clearing Members from January 2018 through the beginning of September 2019. Only 11 of OCC's 107 Clearing Members have member or affiliate issued ETNs. During this period, less than 10 Clearing Members had stock lending activity for SWWR ETN positions. For the majority of these Clearing Members, lending in SWWR ETN positions constituted approximately 13 percent or less of each of those Clearing Members' average notional stock lending activity for the period. For Clearing Members that averaged higher notational lending activity, OCC has observed significant reductions in this activity over recent months.

[16] Because SWWR of equity-related positions would be fully covered as part of margins, these positions would be removed from Clearing Fund shortfall calculations under OCC's stress testing and Clearing Fund methodology. Accordingly, OCC proposes to revise its Methodology Description to reflect the exclusion of SWWR Equity positions from the synthetic accounts used in OCC's stress testing.

[17] For example, suppose the P&L from the SWWR equity price going to 0 for all SWWR equity-related positions were a loss of $1 million. The SWWR Equity Charge in this case would be $1 million. If the P&L were a gain of $1 million, the SWWR Equity Charge would be $0.

b. SWWR ETN Charge

In addition to SWWR that arises from equity securities issued by a Clearing Member or its affiliates, OCC is also exposed to SWWR from open positions related to the uncollateralized ETNs issued by a Clearing Member/Group, which are adversely correlated with the credit quality of that Clearing Member Group. These ETNs are generally equivalent to unsecured senior debt issued by the Clearing Member/Group. While a Clearing Member default can be triggered by its failure to meet other obligations, the firm may or may not default on its ETNs. Hence, the recovery rate for ETNs is uncertain and could be between 0% and 100%.

To address SWWR presented by ETNs issued by a Clearing Member/Group, OCC proposes to calculate an SWWR ETN Charge as part of the SWWR Add-on. OCC notes that, unlike SWWR Equity positions, for which it is assumed that the price of any equity security issued by the Clearing Member Group would fall to zero, the recovery rate for ETNs would not necessarily fall to zero. As a result, the proposed SWWR ETN Charge would utilize an industry standard recovery rate assumption designed to reflect the credit risk associated with such ETN positions.[18] OCC would also adopt additional stress test scenarios to monitor and measure SWWR ETN position exposures and allow for OCC to call for additional financial resources from its Clearing Members when certain thresholds are breached. These SWWR stress test scenarios are discussed in further detail below.

c. SWWR Residual

To ensure that OCC appropriately calculates margins to capture SWWR Equity and SWWR ETN position exposures, OCC proposes to include an SWWR Residual component in SWWR Add-on. Under the proposal, OCC would continue to calculate base STANS margin requirements for Clearing Members with SWWR positions including SWWR Equity and SWWR ETN positions under its current methodology (*i.e.,* without assuming that all SWWR Equity positions fall to a value of zero and without assuming all SWWR ETN positions are valued at the recovery rate times their current price).[19] OCC would then also calculate a residual STANS margin with the SWWR Equity and SWWR ETN positions removed since for SWWR their P&L would be captured through the SWWR Equity and SWWR ETN Charges. The SWWR Residual would then be the difference between the residual margin and the base margin. If the sum of the SWWR Equity Charge, SWWR ETN Charge and SWWR Residual would result in a net credit to the Clearing Member,[20] then the SWWR Residual would be adjusted to ensure that OCC always uses a more conservative measure that captures the greater of either the base STANS margin or the residual STANS margin plus the SWWR Equity and SWWR ETN Charges.[21]

3. Enhancements to Sufficiency Stress Test Scenarios for ETNs

OCC proposes to revise its CFM Policy and Methodology Description to introduce new stress test scenarios designed to capture SWWR exposures for Clearing Member-issued ETNs that are not accounted for in the SWWR ETN Charge and that exceed certain thresholds of OCC's Clearing Fund (''SWWR Sufficiency Scenarios'').[22] Under the proposal, certain Sufficiency Scenarios [23] would be evaluated with Clearing Member-issued ETNs declining to zero within the respective Clearing Member's accounts. Such scenarios would include, but would not be limited to, the 1987 ''Black Monday'' market event on a Cover 1 basis and the two most extreme moves from the 2008 historical market event on a Cover 2 basis.

SWWR Sufficiency Scenarios would value Clearing Member-issued ETNs at a price of zero within their own accounts capturing impacts to any cleared positions tied to those ETNs. Calls, equities, and single-stock futures would all be valued at zero and puts would be valued at their strike price. For these scenarios, margin assets for shortfall calculations would not be adjusted by the SWWR ETN Charge. In addition, other scenarios may be created that embed the SWWR Equity risk by not excluding positions related to the Clearing Member Group's own equity but using an equity price of zero to value all related products.

In the event an SWWR Sufficiency Scenario identifies exposures that exceed 75% of the current Clearing Fund requirement less deficits, OCC may require additional margin deposits from the Clearing Member Group(s) driving the breach. If an SWWR Sufficiency Stress Scenario identifies exposures that exceed 90% of the current Clearing Fund, OCC would perform an intra-month resizing of the Clearing Fund. The proposed change would enable OCC to more accurately measure its credit risks as they relate to SWWR and better test the sufficiency of its overall financial resources and would allow OCC to call for additional financial resources when SWWR ETN position exposures exceed certain thresholds of OCC's Clearing Fund. As a result of these proposed enhancements, OCC believes it would have sufficient financial resources to cover the SWWR associated with SWWR ETN positions if such positions were to be liquidated for less than the assumed recovery rate.

OCC notes that, under its current CFM Policy, in the event results of a daily Sufficiency Stress Test over the final

[18] ETNs issued by a Clearing Member Group would still be stressed in OCC's Clearing Fund as only a part of the credit risk is covered by the SWWR ETN Charge. Additionally, any credit from margin assets would be adjusted by the direct charges related to the risk of the equity and ETNs issued by each Clearing Member Group.

[19] STANS margin requirements are comprised of the sum of several components, each reflecting a different aspect of risk. The base component of the STANS margin requirement for each account is obtained using a risk measure known as 99% Expected Shortfall. The Expected Shortfall component is established as the estimated average of potential losses higher than the 99% value at risk threshold. The term ''value at risk'' or ''VaR'' refers to a statistical technique that, generally speaking, is used in risk management to measure the potential risk of loss for a given set of assets over a particular time horizon. This base component is then adjusted by the addition of a stress test component, which is obtained from consideration of the increases in 99% Expected Shortfall that would arise from market movements that are especially large and/or in which various kinds of risk factors exhibit perfect or zero correlations in place of their correlations estimated from historical data (''Dependence Add-on''), or from extreme adverse idiosyncratic movements in individual risk factors to which the account is particularly exposed (''Concentration Add-on'').

[20] For example, where a customer of a Clearing Member has net short positions referencing that Clearing Member's issued equities, such positions may actually present so-called ''right-way risk'' whereby the position would result in a gain or margin credit for that account as the credit quality of the Clearing Member deteriorates.

[21] For example, suppose that there are no SWWR ETN positions and the Expected Shortfall of a portfolio including all positions was a $10 million loss and the Expected Shortfall with the SWWR Equity-related positions removed was a greater loss of $11 million. In this case, the SWWR Residual would be −$1 million. If the Expected Shortfall with the SWWR Equity-related positions removed was reduced to a loss of $9 million then the SWWR Residual would depend on the SWWR Equity Charge: If the SWWR Equity Charge was more negative than −$1 million, then the SWWR Residual would be +$1 million; if the SWWR Equity Charge was $0, then SWWR Residual would be $0; and if SWWR Equity Charge was between $0 and −$1 million (*e.g.,* −$0.4 million), then SWWR Residual would be positive and the opposite value of SWWR Equity Charge (*e.g.,* +$0.4 million). Thus, the sum of the SWWR Equity Charge, SWWR ETN Charge, and SWWR Residual cannot be positive.

[22] OCC notes that it may also develop additional Informational Scenarios to monitor SWWR; however, these Informational Scenarios would not be used to call for additional financial resources from Clearing Members.

[23] *See supra* note 1111.

five business days preceding the monthly Clearing Fund sizing exceed 90% of the projected Clearing Fund size for the upcoming month, the Clearing Fund size is set such that the peak Sufficiency Stress Test draw is no greater than 90% of the Clearing Fund size. OCC proposes to revise the CFM Policy to provide that OCC generally does not intend to mutualize exposures resulting from the proposed SWWR Sufficiency Scenarios and therefore SWWR Sufficiency Scenarios would not be included for purposes of this anti-procyclicality measure. The proposed change is generally aligned with OCC's intention to appropriately charge individual Clearing Members based on the SWWR they bring to OCC.

4. Other Clarifying and Conforming Changes to CFM Policy and Methodology Description

In addition to the proposed changes described above, OCC would revise the CFM Policy and Methodology Description to provide that, with respect to stress test portfolio construction, SWWR single-name equity positions would be removed from stress test portfolios as they are fully collateralized in margins. Additionally, the Methodology Description would be revised to provide that when adding STANS margin asset amounts to scenario gains and losses, the SWWR Equity Charge, SWWR ETN Charge, and certain other Add-ons from STANS margin asset amounts are excluded.

Finally, OCC would revise its Methodology Description to clarify that for Idiosyncratic Scenarios,[24] the four riskiest names used to calculate idiosyncratic stress test exposures would exclude any equity issued by the Clearing Member's own firms and make other clarifying, non-substantive changes to the Methodology Description concerning stress testing price shocks for products with multiple risk factors and Idiosyncratic Scenarios that are unrelated to the proposal described herein.

Clearing Member Outreach

To inform Clearing Members of the proposed changes, OCC has provided an overview of the proposed changes to the Financial Risk Advisory Council (''FRAC''), a working group comprised of exchanges, Clearing Members and indirect participants of OCC. OCC has also performed direct outreach to Clearing Members that would be most impacted by the proposed changes. To-date, OCC has not received any material objections or concerns in response to this outreach.

Implementation Timing

OCC expects to implement the proposed changes within sixty (60) days after the date that OCC receives all necessary regulatory approvals for the proposed changes. OCC will announce the implementation date of the proposed change by an Information Memorandum posted to its public website at least two (2) weeks prior to implementation.

Expected Effect on and Management of Risk

The proposed changes are designed to enhance OCC's overall framework for managing credit risk and reduce the overall level of risk presented to and presented by OCC. OCC believes that prohibiting Clearing Members from lending their own or Member Affiliate-issued securities in the Stock Loan Programs and introducing the proposed SWWR Add-on charge would improve OCC's ability to manage the credit risks presented by its Clearing Members' SWWR positions and would reduce the risk that OCC's financial resources would be insufficient in the event of a Clearing Member default. As a result, the proposed change is designed, in general, to enhance OCC's framework for measuring and managing its credit risks so that it can continue to provide prompt and accurate clearance and settlement of securities and derivatives transactions in the event of a Clearing Member default.

In addition, OCC believes that introducing new SWWR Sufficiency Scenarios designed to capture SWWR exposures for Clearing Member-issued ETNs that are not accounted for in the SWWR ETN Charge would provide OCC with a more comprehensive approach to managing OCC's credit risks as they relate to SWWR ETN positions. The proposed change would enable OCC to more accurately measure its credit risks and better test the sufficiency of its overall financial resources and would allow OCC to call for additional financial resources when those exposures exceed certain thresholds of OCC's Clearing Fund.

OCC also proposes a number of other clarifying and conforming changes to its CFM Policy and Methodology Description required to implement the proposed SWWR Add-on and SWWR Sufficiency Scenarios described herein and to more clearly describe OCC's stress testing practices. OCC believes that these changes would enhance OCC's overall framework for measuring and managing its credit risks so that it can continue to provide prompt and accurate clearance and settlement of securities in the event of a Clearing Member default.

Consistency With the Payment, Clearing and Settlement Supervision Act

The stated purpose of the Clearing Supervision Act is to mitigate systemic risk in the financial system and promote financial stability by, among other things, promoting uniform risk management standards for systemically important financial market utilities and strengthening the liquidity of systemically important financial market utilities.[25] Section 805(a)(2) of the Clearing Supervision Act[26] also authorizes the Commission to prescribe risk management standards for the payment, clearing and settlement activities of designated clearing entities, like OCC, for which the Commission is the supervisory agency. Section 805(b) of the Clearing Supervision Act[27] states that the objectives and principles for risk management standards prescribed under Section 805(a) shall be to:

- promote robust risk management;
- promote safety and soundness;
- reduce systemic risks; and
- support the stability of the broader financial system.

OCC believes that the proposed changes described herein are consistent with the objectives and principles of Section 805(b) of the Clearing Supervision Act[28] and the risk management standards adopted by the Commission in Rule 17Ad–22 under the Act for the reasons set forth below.[29]

OCC believes the proposed changes are consistent with the objectives and principles of Section 805(b) of the Clearing Supervision Act.[30] The proposed changes are designed to improve OCC's overall framework for managing SWWR brought by its Clearing Members. OCC believes that prohibiting Clearing Members from

[24] OCC has proposed in separate proposed rule change and advance notice filings to adopt a new set of stress scenarios to be used in the monthly sizing of OCC's Clearing Fund that are designed to capture the risks of extreme moves in individual or small subsets of securities (''Idiosyncratic Scenarios''). These Idiosyncratic Scenarios would consider the four single-name securities with the worst P&L in a Clearing Member's portfolio. *See supra* note 5.

[25] 12 U.S.C. 5461(b).

[26] 12 U.S.C. 5464(a)(2).

[27] 12 U.S.C. 5464(b).

[28] *Id.*

[29] 17 CFR 240.17Ad–22. *See* Securities Exchange Act Release Nos. 68080 (October 22, 2012), 77 FR 66220 (November 2, 2012) (S7–08–11) (''Clearing Agency Standards''); 78961 (September 28, 2016), 81 FR 70786 (October 13, 2016) (S7–03–14) (''Standards for Covered Clearing Agencies''). OCC is a ''covered clearing agency'' as defined in Rule 17Ad–22(a)(5) and therefore must comply with the requirements of Rule 17Ad–22(e).

[30] 12 U.S.C. 5464(b).

lending their own or Member Affiliate-issued securities in the Stock Loan Programs and introducing the proposed SWWR Add-on charge would enhance OCC's ability to manage the credit risks presented by its Clearing Members' SWWR positions and would reduce the risk that OCC's financial resources would be insufficient in the event of a Clearing Member default. In addition, OCC believes that introducing new SWWR Sufficiency Scenarios designed to capture SWWR exposures for Clearing Member-issued ETNs that are not accounted for in the SWWR ETN Charge would provide OCC with a comprehensive approach to managing OCC's credit risks as they relate to SWWR ETN positions. The proposed change would enable OCC to more accurately measure its credit risks and better test the sufficiency of its overall financial resources and would allow OCC to call for additional financial resources when those exposures exceed certain thresholds of OCC's Clearing Fund. OCC also proposes a number of other clarifying and conforming changes to its CFM Policy and Methodology Description required to implement the proposed SWWR Add-on and SWWR Sufficiency Scenarios described herein and to more clearly describe OCC's stress testing practices. Accordingly, OCC believes the proposed changes are designed to promote robust risk management, promote safety and soundness, reduce systemic risks, and support the stability of the broader financial system.

OCC also believes the proposed changes are consistent with the risk management standards adopted by the Commission in Rule 17Ad–22 under the Act. Rule 17Ad–22(b)(2) [31] requires a registered clearing agency that performs CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to, in part, use margin requirements to limit its credit exposures to participants under normal market conditions and use risk-based models and parameters to set such margin requirements. In addition, Rules 17Ad–22(e)(6)(i) and (v) [32] require a covered clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to cover its credit exposures to its participants by establishing a risk-based margin system that, at a minimum: (1) Considers and produces margin levels commensurate with the risks and particular attributes of each relevant product, portfolio, and market, and (2) uses an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products.

The proposed changes to OCC's margin and Clearing Fund policies and methodologies to adopt the SWWR Add-on would utilize a risk-based model designed to limit OCC's credit exposures to Clearing Members that present SWWR exposure to OCC through the clearing of Clearing Member-issued equity and ETN positions. OCC believes the proposed SWWR Add-on is reasonably designed to produce margin levels commensurate with the risks and particular attributes SWWR Equity and ETN positions and would use an appropriate method for measuring credit exposure that accounts for relevant product risk factors such as SWWR.

The proposed SWWR Add-on would include both an SWWR Equity Charge and SWWR ETN Charge to address the SWWR attributes and exposures presented to OCC by each type of product. For example, the SWWR Equity Charge assumes that when a Clearing Member defaults the price of any equity security issued by the Clearing Member Group would fall to zero. As a result, OCC would calculate the SWWR Equity Charge by assuming that a Clearing Member's and its affiliates' equity securities would be priced at zero and value all cleared positions accordingly to provide full protection for the risk of potential market exposure to products on a Clearing Member Group's own equity in a default or bankruptcy scenario. Moreover, the SWWR Add-on charge would include an SWWR Residual component to ensure that OCC takes the more conservative of the base STANS margin requirement or margin requirements including the SWWR Equity Charge (particularly in circumstances where using the SWWR Equity Charge would result in a net credit to the Clearing Member).

In addition, OCC would adopt an SWWR ETN Charge to address the SWWR presented by Clearing Member-issued ETNs. ETNs have different characteristics than equity securities and more closely reflect those characteristics of other unsecured debt obligations. For example, if a Clearing Member defaults that does not necessarily imply that it will automatically default on its ETNs. Therefore, ETNs are not necessarily valued at 0 and in fact may retain 100% of their value and be exposed to normal market risk. OCC proposes to measure the risk of these positions using an industry standard recovery rate assumption designed to calculate a margin charge that reflects the expected credit risk associated with such ETN positions. The potential market risk of the ETNs would still be covered by including ETNs in regular margin calculations, whereas the SWWR Equity positions are assumed to be heading towards bankruptcy and necessarily valued near 0 in a default situation.

For these reasons, OCC believes the proposed SWWR Add-on would enhance OCC's margin system by providing for a risk-based model that: (1) Sets margin requirements designed to limit OCC's SWWR exposures to its participant; (2) considers and produces margin levels commensurate with the risks and particular attributes SWWR positions cleared by OCC; and (3) uses an appropriate method for measuring such SWWR exposures consistent with the requirements of Rules 17Ad–22(b)(2), (e)(6)(i) and (e)(6)(v).[33]

Rules 17Ad–22(e)(4)(iii) and (vi) [34] require that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by: (1) Maintaining additional financial resources at the minimum to enable it to cover a wide range of foreseeable stress scenarios that include, but are not limited to, the default of the participant family that would potentially cause the largest aggregate credit exposure for the covered clearing agency in extreme but plausible market conditions and (2) testing the sufficiency of its total financial resources available to meet these minimum financial resource requirements. OCC believes that introducing new SWWR Sufficiency Scenarios designed to capture SWWR exposures for Clearing Member-issued ETNs that are not accounted for in the SWWR ETN Charge would enable OCC to more accurately measure its credit risks and better test the sufficiency of its overall financial resources, particularly in stressed marked conditions. The proposed change would also allow OCC to call for additional financial resources when those exposures exceed certain thresholds of OCC's Clearing Fund. The proposed change is therefore designed to enhance OCC's overall framework for measuring and managing its credit risks and would reduce the risk that OCC's financial resources would be

[31] 17 CFR 240.17Ad–22(b)(2).

[32] 17 CFR 240.17Ad–22(e)(6)(i) and (v).

[33] 17 CFR 240.17Ad–22(b)(2), (e)(6)(i), and (e)(6)(v).

[34] 17 CFR 240.17Ad–22(e)(4)(iii) and (vi).

insufficient in the event of a Clearing Member default consistent with Rules 17Ad–22(e)(4)(iii) and (vi).[35]

Rule 17Ad–22(e)(4) [36] generally requires that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes. By prohibiting Clearing Members from lending Eligible Stock issued by the Clearing Member or any affiliate of such Clearing Member, OCC would mitigate the SWWR that currently exists in its Stock Loan Programs and thereby reduce the risk that OCC's financial resources would be insufficient in the event such a Clearing Member would default. OCC believes the proposed change is therefore reasonably designed to help OCC manage the credit risks associated with SWWR Equity and SWWR ETN positions in the Stock Loan Programs and is therefore consistent with Rule 17Ad–22(e)(4).[37]

III. Date of Effectiveness of the Advance Notice and Timing for Commission Action

The proposed change may be implemented if the Commission does not object to the proposed change within 60 days of the later of (i) the date the proposed change was filed with the Commission or (ii) the date any additional information requested by the Commission is received. OCC shall not implement the proposed change if the Commission has any objection to the proposed change.

The Commission may extend the period for review by an additional 60 days if the proposed change raises novel or complex issues, subject to the Commission providing the clearing agency with prompt written notice of the extension. A proposed change may be implemented in less than 60 days from the date the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the proposed change and authorizes the clearing agency to implement the proposed change on an earlier date, subject to any conditions imposed by the Commission.

OCC shall post notice on its website of proposed changes that are implemented. The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

IV. Solicitation of Comments

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

Electronic Comments

- Use the Commission's internet comment form (*http://www.sec.gov/rules/sro.shtml*); or
- Send an email to *rule-comments@sec.gov.* Please include File Number SR–OCC–2019–807 on the subject line.

Paper Comments

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

All submissions should refer to File Number SR–OCC–2019–807. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (*http://www.sec.gov/rules/sro.shtml*). Copies of the submission, all subsequent amendments, all written statements with respect to the advance notice that are filed with the Commission, and all written communications relating to the advance notice between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the self-regulatory organization.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR–OCC–2019–807 and should be submitted on or before November 27, 2019.

By the Commission.

Jill M. Peterson,

Assistant Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–87475; File No. SR–OCC–2019–806]

Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Advance Notice Related to Proposed Changes to The Options Clearing Corporation's Rules, Clearing Fund Methodology Policy, and Clearing Fund and Stress Testing Methodology

November 6, 2019.

Pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, entitled Payment, Clearing and Settlement Supervision Act of 2010 (''Clearing Supervision Act'') [1] and Rule 19b–4(n)(1)(i) [2] under the Securities Exchange Act of 1934 (''Exchange Act'' or ''Act''),[3] notice is hereby given that on October 10, 2019, the Options Clearing Corporation (''OCC'') filed with the Securities and Exchange Commission (''Commission'') an advance notice as described in Items I, II and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the advance notice from interested persons.

I. Clearing Agency's Statement of the Terms of Substance of the Advance Notice

This advance notice is submitted in connection with proposed enhancements to OCC's Clearing Fund and stress testing rules and methodology designed to: (1) Incorporate a new set of stress test scenarios to be used in the monthly sizing of OCC's Clearing Fund that are designed to capture the risks of extreme moves in individual or small subsets of securities; (2) enhance OCC's stress testing methodology for modeling certain volatility index futures; (3) modify OCC's methodology for allocating Clearing Fund contribution requirements to standardize the margin risk component of the allocation formula for all Clearing Members; (4) adopt an additional threshold for notifying senior management of intra-

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[35] *Id.*

[36] 17 CFR 240.17Ad–22(e)(4).

[37] *Id.*

[1] 12 U.S.C. 5465(e)(1).

[2] 17 CFR 240.19b–4(n)(1)(i).

[3] 15 U.S.C. 78a *et seq.*