

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-32718; File No. SR-OCC-2014-16]

### Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing of Proposed Rule Change To Apply Enhanced Post-Trade Price Reasonableness Checks on Confirmed Trades in Standardized Options and Futures Options To Increase the Likelihood That Erroneous Trades Will Be Identified and Voided

July 30, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 21, 2014, The Options Clearing Corporation (“OCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared by OCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

This proposed rule change will implement price reasonableness checks in connection with the reporting of confirmed trades in standardized options and futures options to OCC by an Exchange. The proposed rule change will promote OCC’s ability to protect itself and clearing members from the negative effects of clearing trades in standardized options and futures options that may contain erroneous premium information.

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

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

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

##### 1. Purpose

OCC is proposing to add an interpretation and policy concerning its administration of existing Article VI, Section 7(c) of the By-Laws and to implement price reasonableness checks in connection with the reporting of confirmed trades in standardized options and futures options to OCC by an Exchange under Article VI, Section 7 and Rule 401. Article VI, Section 7(c) provides that an Exchange may instruct OCC to disregard a confirmed trade previously reported to OCC for clearance and settlement under certain circumstances.<sup>3</sup> One such circumstance is a determination that “new or revised trade information was required to properly clear the transaction.” To promote OCC’s ability to protect itself and clearing members from the negative effects of clearing trades in standardized options and futures options that may contain erroneous premium information, OCC would apply to accepted trades a premium price threshold triggering further scrutiny of trades that exceed it.

##### Background

The Board of Directors and Risk Committee have been evaluating risk controls with respect to trades priced significantly away from current market prices and the risks they present to OCC.<sup>4</sup> OCC anticipates the proposed price reasonableness review process would be put in place while it also develops other post-trade risk controls for potential implementation.

##### Post-Trade Price Validation Process

Earlier this year, a trade data entry parameter in OCC’s systems that does not allow OCC to accept a trade having a premium price of more than \$9,999.99 per contract prevented OCC from accepting erroneous trades that resulted from a trading algorithm error of a customer of a clearing member. If the systems parameter had not prevented OCC from accepting the trades, the

settlement obligation for the clearing member for these trades alone could have exceeded \$800 million. This amount would have been in addition to any other settlement obligation of the clearing member.

In light of the incident, and to promote the protection of OCC and clearing members from erroneous trades, OCC’s Risk Committee directed OCC to perform an analysis of whether OCC should implement procedures regarding a reasonableness review for premium prices at some threshold level less than the current systems parameter of \$9,999.99 per contract. The parameter will also remain in place, however. OCC reviewed standardized option and futures option trade submissions from all Exchanges for a period of 141 business days from December 2, 2013 through June 24, 2014. Based on analysis of the data, OCC determined that it is appropriate to set a premium price limit of \$2,000 per contract because that premium threshold protects OCC and clearing members from erroneous trades that have the potential to cause significant settlement obligations while simultaneously not applying the post-trade price reasonableness check review to a material number of trades that may be valid. Of the nearly 179 million trades that OCC analyzed, only 30 would have triggered a price reasonableness check for exceeding the proposed \$2000 threshold.

Under the proposed process, receipt of a trade that exceeds the premium price limit would generate an automatic notice to alert OCC staff. After being accepted, the trade would be referred by OCC to the reporting Exchange for evaluation under the obvious error or other applicable rules of the Exchange. OCC estimates the trade identification and referral process should take less than an hour from initiation by OCC to full resolution by a reporting Exchange. While a trade is involved in the post-trade reasonableness check process, OCC would not report the position to clearing members or further process the trade. In the event the Exchange determines that the trade is good, it would notify OCC and the trade would continue through OCC’s clearing and reporting processes using the originally reported price. If the Exchange determines that the trade was in error or erroneously priced such that, as provided in Article VI, Section 7(c), new or revised trade information is required to properly clear the transaction, OCC expects the Exchange would instruct OCC to disregard or “bust” the trade. However, in the event the Exchange does not exercise its authority under its

<sup>3</sup> See Article VI, Section 7(c); see also Exchange Act Release No. 46734 (October 28, 2002), 67 FR 67229 (November 4, 2002)(SR-OCC-2002-18) (approving amendments to OCC’s By-Laws and Rules supporting the transition to near real-time reporting of matched trade information, including amendments to Article VI, Section 7 to allow instructions to OCC under certain conditions to disregard a matched trade).

<sup>4</sup> See e.g., OCC Press Release, OCC and The U.S. Options Exchanges Adopt New Pre- and Post-Trade Risk Control Principles (May 21, 2014), [http://www.theocc.com/about/press/releases/2014/05\\_21.jsp](http://www.theocc.com/about/press/releases/2014/05_21.jsp). OCC intends that these principles will be the subject of additional proposed rule changes.

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

own rules to instruct OCC to disregard the trade pursuant to Article VI, Section 7(c), the trade would continue through OCC's clearing and reporting process using the originally reported price.

OCC will provide notice to market participants of the post-trade price reasonableness check process, and the process would be implemented upon regulatory approval. OCC believes this implementation timing is appropriate because OCC's Board instructed OCC to implement the post-trade risk control as quickly as practicable. OCC's decision to implement the process for price reasonableness checks and to set the premium price limit at the \$2,000 level also necessitates related systems changes and conforming changes to certain policies and procedures. Conforming changes to affected policies and procedures would include amendment of OCC's trade and position processing policy. Certain policies and procedures would also be updated to reflect aspects of the process for price reasonableness checks related to governance processes at OCC that are described in more detail below.

#### Ongoing Oversight of the Proposed Post-Trade Price Validation Process

The premium level at which the price reasonableness review process is triggered would be subject to adjustment or suspension under certain conditions. OCC would review the level on a quarterly basis for continued adequacy. In the event the maximum premium price traded over the prior quarter declines by a predetermined dollar amount or the average number of valid trades referred to reporting Exchanges exceeds a predetermined number of occurrences per quarter, OCC would be authorized to adjust the applicable premium level.<sup>5</sup> Establishment of such level and any modification thereof that may be made from time to time would be required to be reported to the Risk Committee. In addition, the Executive Chairman, President or Chief Operating Officer would be authorized to temporarily summarily suspend the then-applicable premium limit in the event that in excess of a predetermined number of valid trades are being referred to the reporting Exchanges for review; provided, however, that when the causes responsible for the temporary suspension are resolved the approved premium threshold would be reinstated. The Risk Committee, along with the Chief Risk and Compliance Officers,

would be advised of any such suspension. OCC believes these processes help ensure an appropriate level of management and Risk Committee oversight for the continued effectiveness of the proposed price reasonableness review process.

#### 2. Statutory Basis

OCC believes the proposed rule change is consistent with Section 17A(b)(3)(F) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"),<sup>6</sup> and the rules and regulations thereunder, including Rule 17Ad-22(d)(4),<sup>7</sup> because, by helping OCC protect itself and clearing members from confirmed trades in standardized options and futures options for which new or revised trade information may be required to properly clear the transaction, the proposed modifications would promote the prompt and accurate clearance and settlement of securities transactions, protect investors and the public interest and ensure that OCC has policies and procedures designed to "identify sources of operational risk and minimize those risks through the development of appropriate systems, controls, and procedures." The proposed rule change is not inconsistent with the existing rules of OCC, including any other rules proposed to be amended. OCC is notifying clearing members of the proposed rule change via an Information Memo.

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

OCC does not believe that the proposed rule change would impose any burden on competition.<sup>8</sup> The proposed post-trade price reasonableness review process that OCC would administer pursuant to Article VI, Section 7(c) would help identify erroneous trades reported to OCC by an Exchange for which clearing members would otherwise be responsible. OCC believes the proposed rule change would not unfairly inhibit access to OCC's services or disadvantage or favor any particular user in relationship to another user because the proposed premium price limit per contract and process for identifying standardized option and futures option transactions for review by reporting Exchanges would be applied uniformly to such transactions, regardless of the identity of the submitting Exchange or the clearing member for whose account the trade was reported.

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

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

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

#### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) By order approve or disapprove the proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

#### IV. Solicitation of Comments

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

##### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-OCC-2014-16 on the subject line.

##### Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.
- All submissions should refer to File Number SR-OCC-2014-16. 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 Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the

<sup>5</sup> Any such action by OCC regarding the premium level would also be subject to the regulatory process of filing a proposed rule change with the Commission.

<sup>6</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>7</sup> 17 CFR 240.17Ad-22(d)(4).

<sup>8</sup> 15 U.S.C. 78q-1(b)(3)(I).

submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site 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 OCC and on OCC's Web site at [http://www.theocc.com/components/docs/legal/rules\\_and\\_bylaws/sr\\_occ\\_14\\_16.pdf](http://www.theocc.com/components/docs/legal/rules_and_bylaws/sr_occ_14_16.pdf). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-OCC-2014-16 and should be submitted on or before August 26, 2014.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72705; File No. SR-MSRB-2014-05]

### Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change Consisting of Proposed Amendments to Rule G-3, on Professional Qualification Requirements, Regarding Continuing Education Requirements

July 29, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 22, 2014, the Municipal Securities Rulemaking Board (the "MSRB" or "Board") filed with the Securities and Exchange Commission (the "SEC" or "Commission") the proposed rule

change as described in Items I, II, and III below, which Items have been prepared by the MSRB. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The MSRB is filing with the Commission a proposed rule change consisting of proposed amendments to Rule G-3, on professional qualification requirements (the "proposed rule change").<sup>3</sup> The effective date of the proposed rule change will be January 1, 2015.

The text of the proposed rule change is available on the MSRB's Web site at [www.msrb.org/Rules-and-Interpretations/SEC-Filings/2014-Filings.aspx](http://www.msrb.org/Rules-and-Interpretations/SEC-Filings/2014-Filings.aspx), at the MSRB's principal office, and at the Commission's Public Reference Room.

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

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

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

###### 1. Purpose

The purpose of the proposed rule change is to improve the Firm Element continuing education requirement of MSRB Rule G-3(h)(ii) by requiring brokers, dealers and municipal securities dealers (collectively, "dealers") to conduct annual municipal securities training for registered representatives who regularly engage in, and municipal securities principals who regularly supervise, municipal securities activities. While the MSRB has intended, from the inception of the rule, that dealers consider the scope of their municipal securities activities and

regulatory developments in preparing their annual training plan, the rule does not specifically require dealers to train registered persons on municipal securities issues. The proposed rule change would require such training for a select group of registered persons who are regularly engaged in or supervise municipal securities activities.

###### Background

In 1993, a self-regulatory organization ("SRO") task force<sup>4</sup> was created to study and develop recommendations regarding continuing education in the securities industry. The task force issued a report calling for a formal, two-part continuing education program consisting of: (i) A Regulatory Element requiring securities industry professionals to obtain periodic and uniform training in regulatory matters, and (ii) a Firm Element requiring firms to provide ongoing training to employees to ensure they have up to date knowledge of job and securities product-related subjects.

On February 8, 1995 the SEC approved SRO rule changes based on the task force's recommendations.<sup>5</sup> In approving the SRO rule changes, the SEC stated that these SROs "may require their members, either individually or as part of a group, to provide specific training in any areas the SROs deem necessary."<sup>6</sup> The SEC added that "[a]s the program evolves, it is expected that educational standards will be defined by the SROs for products and services where heightened regulatory concerns exist."<sup>7</sup> Since approval of the continuing education rules, SROs have amended their continuing education rules as industry and market practices evolved.

###### Current Firm Element Continuing Education Requirement

Currently, MSRB Rule G-3(h)(ii)(B)(1) requires dealers to maintain a continuing and current education program for their covered registered persons to enhance their securities knowledge, skill and professionalism. Under Rule G-3(h)(ii)(A), covered registered persons are limited to those registered representatives who have direct contact with customers in the conduct of a dealer's securities sales, trading and investment banking

<sup>4</sup> The task force included representatives from six SROs, including the MSRB, and industry representatives.

<sup>5</sup> See SEC Release No. 34-35341 (Feb. 8, 1995), 60 FR 8426 (Feb. 14, 1995), File No. SR-MSRB-94-17 (approving MSRB Rule G-3(h), on continuing education requirements).

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>9</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Certain portions of Rule G-3, including the title, are the subject of proposed amendments that are currently pending SEC approval and will not be effective until 60 days following the date of such approval. See SEC Release No. 34-72425 (Jun. 18, 2014); 79 FR 35829 (Jun. 24, 2014); File No. SR-MSRB-2014-04.