8011-01

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-84565; File No. SR-ODD-2018-01]

Self-Regulatory Organizations; The Options Clearing Corporation; Order Granting Approval of Accelerated Delivery of Supplement to the Options Disclosure Document Reflecting the Inclusion of Disclosure Regarding Foreign Currency Index Options and Implied Volatility Index Options, Certain Contract Adjustment Disclosures, and T+2 Settlement

November 9, 2018.

On October 24, 2018, the Options Clearing Corporation ("OCC") submitted to the Securities and Exchange Commission ("Commission"), pursuant to Rule 9b-1 under the Securities Exchange Act of 1934 ("Act"),[1] five preliminary copies of a supplement to amend the options disclosure document ("ODD") to include disclosure regarding foreign currency index options and implied volatility index options, certain contract adjustment disclosures, and T+2 settlement ("October 2018 Supplement").[2] On October 25, 2018, the Commission received from the OCC five definitive copies of the October 2018 Supplement.[3]

The October 2018 Supplement consists of three parts. Part I addresses foreign currency index options and implied volatility index options. It amends and restates the April 2015 Supplement[4] in its entirety and includes additional changes to take into account a recently approved proposed rule change allowing the listing of a new implied volatility index option.[5] The

1 17 CFR 240.9b-1.

2 See email from Marcie Pomper, Corporate Assistant, OCC, to Sharon Lawson and David Michehl, Division of Trading and Markets ("Division"), Commission, dated October 24, 2018.

3 See letter from Karen Bilek, Vice President and Counsel, OCC, to Sharon Lawson, Senior Special Counsel, Division, Commission, dated October 24, 2018. The October 2018 Supplement also makes certain technical, non-substantive amendments to the ODD.

4 https://www.sec.gov/rules/sro/occ/occarchive/occarchive2015.shtml#odd.

5 See infra note 10.

April 2015 Supplement was never distributed to options customers. The OCC issued an information memo on May 22, 2015[6] to inform its clearing members and investors that the April 2015 Supplement would be amended and replaced in its entirety in order to accommodate other implied volatility index options proposed for trading by a different participant options exchange. Part I of the October 2018 Supplement serves as that replacement. Part II of the October 2018 Supplement addresses additional contract adjustment disclosures. Part III of the October 2018 Supplement provides for the change in settlement from T+3 to T+2.

The October 2018 Supplement accommodates the introduction of options on foreign currency indexes and implied volatility options whose exercise settlement value is calculated differently than that of existing implied volatility options.

Currently, the ODD states that indexes that may underlie options include stock indexes, variability indexes, strategy-based indexes, dividend indexes, and relative performance indexes. In April 2013, the Commission approved a proposed rule change by the International Securities Exchange, LLC ("ISE") to list options on the Dow Jones FXCM Dollar Index.[7] The October 2018 Supplement amends disclosures in the ODD to add foreign currency indexes as a type of index that can underlie an option, in order to accommodate the trading of options on the Dow Jones FXCM Dollar Index and similarly structured foreign currency indexes.[8] Specifically, the October 2018 Supplement adds new disclosure regarding the characteristics of foreign currency index options and their special risks. In addition, the supplement adds an example of the

6 See OCC Information Memo No. 36788 available at https://www.theocc.com.

7 See Securities Exchange Act Release No. 69365 (April 11, 2013), 78 FR 23321 (April 18, 2013) (SR-ISE-2013-14).

8 The October 2018 Supplement is intended to accommodate the trading of options on foreign currency indexes that reflect the value of one currency, often the U.S. dollar, against a basket of foreign currencies. Foreign currency indexes are calculated using exchange rates.

calculation of a foreign currency index. The supplement also amends disclosures in the ODD to accommodate the fact that components of foreign currency indexes are foreign currencies rather than securities (e.g., by referring to "components" of an index rather than "constituent securities" of an index).

The ODD currently contains general disclosures on the characteristics and risks of trading standardized options on variability indexes. The ODD states that variability indexes are indexes intended to measure the implied volatility, or the realized variance or volatility, of specified stock indexes or specified securities. In January 2014, the Commission approved a proposed rule change by the ISE to list options on the Nations VolDex Index.[9] In October 2018, the Commission approved a proposed rule change by the Miami International Securities Exchange, LLC to list options on the SPIKES Index.[10]

The October 2018 Supplement amends disclosures in the ODD regarding implied volatility index options to accommodate the listing of options on the Nations VolDex Index, the SPIKES Index and other similarly structured implied volatility indexes.[11] Specifically, the October 2018 Supplement amends the discussion of implied volatility index options by including disclosure regarding exercise settlement value calculations that use the mid-point of the bid and offer of the index components or actual trade prices and the risks of the different calculation methodologies. The supplement also provides disclosure regarding the types of options that can

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9 See Securities Exchange Act Release No. 71365 (January 22, 2014), 79 FR 4512 (January 28, 2014) (SR-ISE-2013-42).

10 See Securities Exchange Act Release No. 84417 (October 12, 2018), 83 FR 52865 (October 18, 2018) (SR-MIAX-2018-14).

11 The exercise settlement value for the Nations VolDex Index is calculated using the mid-point of the NBBO for the component options of the index while the SPIKES Index uses a "price dragging" technique when determining the ongoing price for each individual option used in the calculation of the index. Most other index settlement values are calculated using transaction prices of the index components.

be used to calculate implied volatility indexes (i.e., out-of-the-money option series and hypothetical at-the-money option series; options with certain expiration months or weeks; number of days the options have until expiration).

The October 2018 Supplement also amends the ODD to reflect that adjustments to some of the terms of options contracts, to account for certain events, such as certain dividend distributions or other corporate actions that affect the underlying security or other underlying interest, will be made by the OCC rather than an adjustment panel of the Securities Committee.[12] Adjustment determinations were previously made by adjustment panels that consisted of two representatives of each U.S. options market on which a series is traded and one representative of the OCC, who voted only to break a tie. Determinations as to whether to adjust outstanding options in response to a particular event, and, if so, in what manner, are now made solely by the OCC taking into consideration policies established by representatives of each of the U.S. options markets on which the effected option trades and a representative of OCC. Panels, however, consisting of representatives of each of the U.S. options markets on which the affected series of options is traded and one representative of the OCC retain their function and authority under other provisions of the OCC's rules to fix exercise settlement amounts and cash settlement amounts in certain circumstances. The Supplement amends references to these panels, eliminating potential confusion with the Securities Committee, which will continue to determine the appropriateness of adopting prospective policy changes or clarifications. The October 2018 Supplement includes additional clarification and examples regarding how certain adjustments may affect an option's value and deletes certain obsolete language.

Finally, the October 2018 Supplement makes changes necessary to reflect that the regular

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12 See Securities Exchange Act Release No. 69977 (July 11, 2013), 78 FR 42815 (July 17, 2013) (SR-OCC-2013-05).

exercise settlement date for physical delivery stock options has moved from the third business date following exercise (T+3) to the second business date following exercise (T+2).

The October 2018 Supplement is intended to be read in conjunction with the more general ODD, which discusses the characteristics and risks of options generally.[13]

Rule 9b-1(b)(2)(i) under the Act[14] provides that an options market must file five copies of an amendment or supplement to the ODD with the Commission at least 30 days prior to the date definitive copies are furnished to customers, unless the Commission determines otherwise, having due regard to the adequacy of the information disclosed and the public interest and protection of investors.[15] In addition, five copies of the definitive ODD, as amended or supplemented, must be filed with the Commission not later than the date the amendment or supplement, or the amended ODD, is furnished to customers. The Commission has reviewed the October 2018 Supplement, and the amendments to the ODD contained therein, and finds that, having due regard to the adequacy of the information disclosed and the public interest and protection of investors, the supplement may be furnished to customers as of the date of this order.

IT IS THEREFORE ORDERED, pursuant to Rule 9b-1 under the Act,[16] that definitive

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13 The Commission notes that the options markets must continue to ensure that the ODD is in compliance with the requirements of Rule 9b-1(b)(2)(i) under the Act, 17 CFR 240.9b-1(b)(2)(i), including when changes regarding foreign currency index options and implied volatility index options are made in the future. Any future changes to the rules of the options markets concerning foreign currency index options and implied volatility index options would need to be submitted to the Commission under Section 19(b) of the Act. 15 U.S.C. 78s(b).

14 17 CFR 240.9b-1(b)(2)(i).

15 This provision permits the Commission to shorten or lengthen the period of time which must elapse before definitive copies may be furnished to customers.

16 17 CFR 240.9b-1.

copies of the October 2018 Supplement to the ODD (SR-ODD-2018-01), reflecting the inclusion of disclosure regarding foreign currency index options and implied volatility index options, certain contract adjustment disclosures, and T+2 settlement, may be furnished to customers as of the date of this order.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[17]

Eduardo A. Aleman,
Assistant Secretary.

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[17] 17 CFR 200.30-3(a)(39).

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