

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-47902; File No. SR-OCC-2002-14]

Self-Regulatory Organizations; the Options Clearing Corporation; Order Granting Approval of a Proposed Rule Change Relating to Procedures for Processing Late and Supplementary Exercise Instructions

May 22, 2003.

I. Introduction

On June 28, 2002, the Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-OCC-2002-14 pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").¹ Notice of the proposal was published in the **Federal Register** on March 4, 2003.² No comment letters were received. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

II. Description

The proposed rule change amends Rules 801(e) and 805(g) to modify OCC's fees for processing late exercise instructions and supplementary exercise notices and amends Rule 801(e) to establish a specific cut-off time for accepting late exercise notices after the start of critical processing and to eliminate OCC's ability to accept instructions to modify a previously submitted exercise notice after the start of critical processing.

Background

Rule 801 sets forth the procedures for submitting exercise notices on a business day which is not an expiration date, including the requirement that such submissions be completed by 7 p.m. (All times are Central Time.) Rule 801(e) provides OCC with the authority to permit clearing members to file, revoke, or modify exercise notices after 7 p.m. for the purpose of correcting *bona fide* errors. Authority to accept or reject such late instructions is vested with the Chairman, Management Vice Chairman, President, or such officer's delegate.

If a late instruction is accepted, Rule 801(e) requires the clearing member submitting the instruction to pay a late filing fee.³ The fees for late instructions increase the later the notice is received. Late instructions accepted for filing after the start of critical processing are processed on a best efforts basis and only if the assigned clearing member(s) can be notified before 8 a.m. Previously submitted exercises may not be revoked after the start of critical processing.

These late exercise procedures help provide a monetary incentive for clearing members to take precautions to avoid exercise errors and to identify those errors that do occur earlier in OCC's processing cycle. The earlier late exercise notices are submitted, the easier and less costly it is for OCC to process these exercises. Late exercise notices submitted before the start of OCC's critical processing cycle can be readily accommodated through standard procedures. Late exercise notices submitted after the start of critical processing require supplemental assignment procedures.

Rule 805 sets forth the procedures for submitting exercise notices on expiration dates. Rule 805 permits clearing members to submit exercise notices with respect to expiring options ("supplementary exercise notices") after the normal deadline but before their expiration time (*i.e.*, 10:59 P.M.) by following prescribed procedures. A clearing member submitting such a supplementary exercise notice is required to pay a late filing fee.⁴ As under Rule 801, the filing fees increase the later the notice is received. Supplementary exercise notices submitted in accordance with the prescribed procedures are irrevocable.

Discussion

OCC recently completed a review of these rules as a result of an increase in the number of late instructions received from clearing members. Based on that review, OCC is changing the applicable fee schedules and cut-off times for processing late instructions and supplementary exercise notices.

Fees

One of the principal purposes for charging a filing fee for late instructions under both Rule 801 and Rule 805 is to provide an incentive for clearing members to discover exercise errors earlier in the processing cycle. The recent increase in the number of late instructions has led OCC to conclude that the current fee schedules do not provide a sufficient incentive. The current and proposed fee schedules are as follows:

Rule 801(e)

Submission time	Current fee	Proposed fee
7 p.m.–8 p.m.	\$500/any accepted request	\$2,000/any accepted request.
8:01 p.m.–start of critical processing	\$2,000/any accepted request	\$5,000/any accepted request.
After start of critical processing up until 8 a.m. ⁵	\$10,000/line item on any exercise notice or modification accepted.	\$20,000/line item on any exercise notice accepted. ⁶

⁵ On approval of this filing, this time will be 6:30 a.m.

⁶ On approval of this filing, only exercise notice (*i.e.*, not modifications) will be accepted after the start of critical processing.

Rule 805(g)

Submission time	Current fee	Proposed fee
After the prescribed deadline for the submission of exercise instructions—start of critical processing.	\$2,000/any exercise notice accepted	\$5,000/any exercise notice accepted.
After start of critical processing—expiration time	\$10,000/line item on any exercise notice accepted.	\$20,000/line item on any exercise notice accepted.

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 47396 (February 24, 2003), 68 FR 10293.

³ Late filings, revocations, and modifications of exercise may also be the subject of disciplinary action. Rule 801(e)(4) and 805(g).

⁴ Late filings of supplementary exercise notices may also be the subject of disciplinary action. See note 3 above.