CHAPTER VII

FINANCIAL REGULATION IN THE OPTIONS MARKETS

INTRODUCTION

The Options Study examined the financial protections currently employed in the options markets in order to determine whether sufficient safeguards and controls exist to protect the options marketplace, and ultimately customers, from being financially harmed by the failure of broker-dealers. This examination involved a review of (1) financial and operational data supplied by The Options Clearing Corporation ("OCC"), the options exchanges, the National Association of Securities Dealers ("NASD") and the New York Stock Exchange ("NYSE"); (2) OCC clearing procedures; and (3) information about OCC member clearing firms and options floor participants. The data covered the period from the end of 1976 to April 28, 1978 with particular emphasis on the period between April 13 and 18, 1978 when dramatic upward stock price and volume movements occurred.

The present regulatory system provides financial protection through a variety of approaches: (1) the Commission's uniform net capital rule which requires that broker-dealers maintain a certain minimum amount of readily liquid assets in excess of their liabilities; (2) the Commission's customer protection rule which limits a broker-dealer's use of customer funds and securities in its business; (3) the Commission's and the self-regulatory organizations' financial reporting and early warning filing requirements which serve to alert the Commission and the self-regulatory
organizations to broker-dealers with potential operational and financial problems; (4) the Federal Reserve Board ("FRB") initial margin requirements and the self-regulatory organization margin maintenance requirements which serve to prevent both broker-dealers and customers from overextending their financial resources by, among other things, limiting the amount of credit a broker-dealer may extend to finance customer securities purchases and holdings; and (5) the Securities Investor Protection Act ("SIPA") which provides to each public customer up to $100,000 protection for the customer's funds and securities held by a broker-dealer if that broker-dealer becomes insolvent.

Additional safeguards to protect the options market place and public customers engaging in options transactions are provided by the OCC's regulation of its members. These regulations establish minimum net capital requirements for OCC members (in some respects greater than those reported by the Commission), regulate OCC clearing procedures, and set margin maintenance requirements for positions carried at OCC. The OCC guarantees the performance of all options contracts accepted by it and its guarantee is backed by a clearing fund maintained by required deposits from OCC members.

Broker-dealers which confine their business to "maintaining a market" on the floor of an options exchange, as defined by the options exchanges, are subject to different Commission net capital requirements and different FRB margin requirements than those applicable to other
broker-dealers and to public customers. The net capital and margin requirements for market making transactions recognize the special role of those maintaining a market in securities.

To conduct its study of the financial integrity of the options markets, and to test the adequacy of the provisions of the Commission's net capital rule the Options Study reviewed: (1) broker-dealer financial data which are collected by the self-regulatory organizations and filed with the Commission on a quarterly basis; 1/ (2) impact studies and reports submitted by interested parties; (3) OCC operational and financial data submitted by the OCC in response to the Options Study's letter dated May 5, 1978; 2/ (4) OCC clearing member and option floor participant operational and financial data submitted by the self-regulatory organizations in response to the Options Study's letters dated June 7, June 16, and June 27, 1978; 3/ and (5) two questionnaires ("Form A" and "Form B"), attached to the June 7, 1978 letter, developed by the Options Study to obtain certain financial data and operational information regarding OCC clearing members (Form A) and options floor participants (Form B). 4/

1/ Form X-17A-5 Part II and Part IIA, appended as Exhibit 1.
4/ Form A and Form B, appended as Exhibit 4.
The Options Study received 150 Form As and over 2,000 Form Bs in response to its requests and developed 29 computer programs to compile, edit, and sort the data received. The computer programs, among other things, sorted and tested the information by exchange affiliation, by size of market maker equity, by market maker clearing firm and by options floor participant status (i.e., market maker, specialist or registered options trader).

Based on these computer analyses and impact studies, the Options Study concluded that the amount of capital required by existing financial safeguards is sufficient to protect both the market and public investors in periods of normal volume and price movements. The Options Study is concerned, however, that these financial safeguards as they pertain to broker-dealers maintaining a market on the floor of an options exchange and OCC member firms clearing their accounts may be inadequate when there are abnormal volume surges and price fluctuations.

On the other hand, the Options Study concluded that the net capital requirements appear unduly restrictive in measuring the risks of certain options strategies engaged in by broker-dealers trading for their own account both on and off the floor of an options exchange and that these requirements, in particular, may be discouraging more active participation in the options market by broker-dealers trading off the floor of an options exchange and whose participation would possibly contribute additional liquidity to the markets. These findings are discussed more
fully below in the first section of this chapter, "Broker-Dealer Financial Regulation."

The FRB and the self-regulatory organizations' initial and margin maintenance requirements are discussed in the second section of this chapter, "Credit Regulation." The Options Study is recommending revisions to the margin regulations which would enable broker-dealers maintaining a market on the floor of an options exchange to better use stock to hedge against the risks they incur in maintaining a market. The recommended revision would also restrict the number of stocks on which any broker-dealer would be eligible to receive this special margin treatment.

Only certain types of broker-dealer activity will be discussed in this chapter in order to concentrate on the areas in which the Options Study believes Commission or self-regulatory action is appropriate. These include:

--- Transactions on the floor of an options exchange by a market maker in the course of maintaining a market in options, as defined by the options exchanges;

--- Transactions by a broker-dealer which is a member of OCC in connection with financing and guaranteeing the options transactions of market makers ("market maker clearing firm");

--- Transactions off the floor of an options exchange by a broker-dealer for its own account ("upstairs dealers").

The chapter does not discuss the extension of credit to customers, the use of marketmaker exemptions from the credit regulations, or the
ability of the self-regulatory organizations to detect improper
extensions of credit to options marketmakers. These matters are under
continuing study in the Division of Market Regulation.

BROKER-DEALER FINANCIAL REGULATION

Certain of the broker-dealer financial regulatory controls mentioned
above were established, and others were improved, in response to the
failure of a number of broker-dealers during the period from 1969 to
1972. During that time a number of NYSE members and numerous other
broker-dealer firms, which were not members of an exchange, failed
and were forced to merge or liquidate. Customer exposure exceeded $100
million. 5/ To restore public investor confidence in broker-dealer
firms, and to provide to such investors a measure of protection against
broker-dealer financial failure, the Congress adopted the Securities
Investor Protection Act of 1970 (the "SIPA").

1. THE SECURITIES INVESTOR PROTECTION ACT

The SIPA was designed to protect customers' funds and securities
left with a broker-dealer and is administered by the Securities Investor
Protection Corporation ("SIPC"). As recently amended, the SIPA protects
each securities customer's account with a broker-dealer up to $100,000,
with a limitation of $40,000 for a claim relating to cash. SIPC has

5/ SEC, Study of Unsafe and Unsound Practices of Brokers and Dealers,
established a fund of $150 million which was generated by assessments on member broker-dealers. In emergency circumstances SIPC can supplement its fund by borrowing up to $1 billion from the United States Treasury. SIPA provides for the settlement of customers' claims for securities by the return of securities to the maximum extent possible rather than by cash payment.

2. COMMISSION ACTION
   a. Commission's Customer Protection Rule

   In adopting SIPA the Congress amended the Exchange Act to require the Commission to prescribe rules regulating broker-dealer "acceptance of custody and use of customers' securities", and the "carrying and use of customers' deposits and credit balances." Further, the Commission was to establish rules requiring "the maintenance of reserves with respect to customers' deposits or credit balances."

   In response to these directives, the Commission, in November 1972, adopted its customer protection rule. 6/

   This rule:

   ---Requires that customers' funds left on deposit with a broker-dealer and any cash realized through the permissible use of customers' securities be used only in designated areas of the broker-dealer's business related to servicing its customers. To the extent customer funds are not used in these areas, they must be deposited in a restricted, segregated, bank account;

— Restricts a broker-dealer's use of customers' fully paid and excess margin securities;

— Limits a broker-dealer's ability to use its customers' funds for dealer activities, such as underwriting and trading, for its own account;

— Restricts a broker-dealer's expansion of its business through the use of customer funds.

b. Commission's Uniform Net Capital Rule

Prior to June 1975, a broker-dealer was exempted from the Commission's net capital rule if it was subject to a national securities exchange net capital rule that was deemed by the Commission to be more comprehensive than the Commission's net capital rule. The net capital requirements of the various national securities exchanges, however, were not uniform nor interpreted uniformly which resulted in different capital requirements for firms doing similar businesses.

To further upgrade the financial responsibility of brokers and dealers, the Commission adopted a uniform net capital rule ("net capital rule") in June 1975, which established uniform requirements for all broker-dealers except specialists and other market makers on a national securities exchange who do not carry customer accounts and whose exemption from the rule was continued. This net capital rule continued the basic net capital concept which the Commission and the national securities exchanges had adopted, but for the first time established a uniform rule with minimum financial standards.
The objective of the Commission's net capital rule is to require a broker-dealer to maintain a sufficient cushion of assets readily convertible into cash ("liquid assets") to satisfy all customer claims. The net capital rule establishes minimum financial requirements depending on the nature of the business a broker-dealer conducts, ranging from $2,500, for a firm conducting a business solely in the sale and redemption of investment company shares, to a maximum of $100,000 for a firm which makes dealer markets in over-the-counter securities. Broker-dealers that carry customer accounts are subject to a minimum $25,000 requirement. 7/

Speaking generally, "net capital" is determined by subtracting from the broker-dealer's net worth (total assets less total liabilities) assets that are not readily convertible into cash, such as unsecured receivables, fixed assets and unmarketable securities. From the asset balance thus derived there is further deducted a certain percentage of the value of marketable securities, called "haircuts," ranging from 1/8 of a percent for commercial paper to 30 percent for common stock. These haircuts are designed to provide a cushion in the event of adverse market movement. 8/

The net capital rule also serves to limit a broker-dealer's volume of business in relation to its net capital. The limitation

is accomplished in three ways. First, the rule limits the amount of unsecured and customer related liabilities a broker-dealer can assume, by requiring one dollar of net capital for every fifteen dollars of unsecured and customer related liabilities — an amount defined as "aggregate indebtedness." Second, the rule provides that the net capital requirement may be measured by the amount of customer activity. This is an elective alternative to measuring aggregate indebtedness and is a derivative of the Commission's customer protection rule. To determine its required net capital under the alternative, the broker-dealer must complete a prescribed formula which measures total customer funds held by the broker-dealer (credit side of the formula) against the amount of customer activity the broker-dealer has financed (debit side of the formula). Broker-dealers which elect the alternative are required to maintain net capital equal to the greater of $100,000 or 4 percent of the debit side of the formula. 9/ The excess of credits over debits must be segregated in a restricted bank account. Third, in the case of OCC member clearing firms, the rule limits the aggregate amount of options positions such firms can finance and guarantee on behalf of the market maker accounts they carry. 10/ This limitation is discussed more fully below.

9/ 17 CFR 240.15c3-1(f).
10/ 17 CFR 240.15c3-1(a)(6), 15c3-1(c)(2)(x).
3. THE OPTIONS CLEARING CORPORATION FINANCIAL RULES

The predecessor of OCC, called the Chicago Board Options Exchange Clearing Corporation, was established by the CBOE to act as agent for issuing and guaranteeing CBOE listed options contracts and to assign and process exercised options contracts. OCC, now jointly owned by the five options exchanges, is the sole authorized issuer and guarantor of listed options. In addition, OCC is a self-regulatory organization registered under the Exchange Act. Under authority derived from the Exchange Act, the OCC has adopted regulations designed to provide financial protection to its members and public customers with respect to options transactions. These regulations require a broker-dealer that is an OCC member which executes, processes, or clears options transactions for itself, customers or other broker-dealers (1) to maintain a minimum net capital of $100,000; (2) to pay OCC for options transactions the next business day after the transactions occur; (3) to maintain deposits at OCC based on a percentage of the value of short options positions held by the OCC member on behalf of itself and others for which it clears; and (4) to contribute to a common fund maintained at OCC to back OCC's performance guarantee of options contracts in the event one or more of the OCC's members default on their obligations.

a. OCC Clearing Members

To conduct a listed options business, a broker-dealer must be an OCC member or have its options business cleared by an OCC member. OCC
membership is typically obtained by a broker-dealer to facilitate its options business with public customers, to trade options for the broker-dealer's own account, or to enter into the business of clearing market maker or other broker-dealer accounts. An OCC member, which clears market maker accounts, is called a market maker clearing firm. It finances and guarantees the transactions in the market maker accounts it clears, and performs the necessary recordkeeping and processing required to clear the accounts' transactions through OCC. For these services the market maker clearing firm charges the market makers a fee. On March 31, 1978, OCC had 150 members of which 22 carried the accounts of market makers.

The role of an OCC member as guarantor of the market maker accounts it carries is a unique feature of the options markets. In establishing a marketplace for the trading of listed options, the founders of the CBOE stated that they sought to assure that the market makers on the floor of the CBOE would not be prevented from entering the market due to highly restrictive and selective capital requirements. To accomplish this objective the CBOE looked to the clearing firms which carried these market makers' positions to provide sufficient capital to protect the marketplace from a market maker's failure. Market makers that were not clearing firms or did not do a public business were prohibited by the CBOE from executing any transaction on its floor unless an OCC clearing member accepted financial responsibility for all the market maker's exchange transactions under a letter of guarantee.
issued by the market maker clearing firm, approved by OCC, and filed with CBOE. 11/

The MSE and PSE adopted similar requirements. 12/ The AMEX and PHLX, however, followed their existing equity specialist systems and adopted minimum financial requirements for each specialist unit. These rules require that each unit maintain cash or liquid assets of $100,000 at AMEX and $25,000 at the PHLX. 13/ In addition, the AMEX and PHLX established minimum financial standards for certain members called "registered options traders," who trade options on the floor of the exchange for their own account in the same manner as competing market makers at the CBOE. These requirements are currently $15,000 at AMEX and $25,000 at PHLX. 14/

Notwithstanding the financial requirements established for floor participants by the options exchanges, each market maker clearing firm is financially responsible for the accounts of the specialists, market makers, or registered options traders (collectively referred to as "market makers") it clears at OCC and is thereby obligated: (1) to submit full payment to OCC for all purchasing transactions by the market maker accounts it clears; (2) to satisfy all OCC margin requirements

11/ CBOE rule 8.5.
12/ MSE art. XLVII, rule 4; PSE rule IV, Sec. 77.
13/ AMEX rule 171; PHLX rule 1021.
14/ AMEX rule 110 and PHLX rule 1014.
for its market makers' accounts; and (3) to satisfy its market makers' stock or payment delivery requirements on the exercise of call or put options. 15/

The accounts of market makers on the CBOE and PSE are generally carried by OCC members whose securities business is substantially confined to performing clearing functions for such accounts ("specialized market maker clearing firms"). The accounts of market makers on the AMEX and PHLX are carried by OCC members that conduct a more fully-integrated securities business including a business with public customers ("integrated market maker clearing firms"). The accounts of market makers on the MSE are carried by both specialized and integrated market maker clearing firms.

b. OCC Member Capital Requirements

OCC requires that members' net capital, aggregate indebtedness and alternative net capital be computed in accordance with the Commission's rules. OCC, however, requires greater minimum net capital than is required under the Commission's net capital rule.

OCC requires each of its new members to have an initial net capital of $150,000 and from then on to maintain net capital of not less than $100,000. The member's aggregate indebtedness may not exceed eight

15/ OCC art. VI §§ 4, 14.
dollars for each one dollar of net capital at the time it becomes a member and thereafter may not exceed fifteen dollars for each one dollar of net capital. Initially, a clearing member electing the alternative net capital requirement must have net capital of not less than seven percent of its aggregate debit items and thereafter must have net capital of not less than four percent of its aggregate debit items. If on any day an OCC member's net capital falls below $150,000, or its aggregate indebtedness increases to twelve dollars for each one dollar of net capital or, in the case of a member electing the alternative, its net capital falls below six percent of its aggregate debit items, the OCC member must notify OCC of these facts by 4:00 p.m. the following day.

All OCC members carrying market maker accounts are subject to the net capital requirements of the Commission and the OCC, but the market makers that are not members of the OCC and clear through an OCC member are exempt from the Commission's net capital requirements as long as they restrict their securities business to options market making. As indicated above, an OCC member finances and guarantees the options transactions of the market maker accounts it carries and, in effect, provides the net capital required to provide financial protection to the options market and public customers.

16/ OCC rules 301, 302.
c. Commission's Net Capital Requirements

The Commission's net capital rule requires a market maker clearing firm to reduce its net capital to the extent that the deductions required under the net capital rule (to recognize the risks of a market maker's stock and options positions) exceed the equity in that market maker's account. The equity in the market maker's account is determined by taking the market value of all long positions in his account, less the market value of his short positions, adjusted by the amount due to or from his clearing firm. A positive amount is the equity in the account. A negative amount would indicate a deficit. Market makers with a deficit equity position must cease doing a securities business until such time as the deficit is eliminated. Generally, the deductions required under the Commission's net capital rule, to recognize the risks with respect to positions in a market maker's account, are determined separately for each options class held in the market maker's account by multiplying the market value of net long positions by 50 percent and net short positions by 75 percent. Whichever is the greater amount — be it 50 percent of the long positions or 75 percent of the short positions in the particular class — is the required deduction in that options class. If the aggregate of the deductions for all the classes of options held by the market maker exceeds the equity in the market maker's account, the OCC member which clears that account is required to reduce its net capital by the amount of the excess.
Any time the market maker clearing firm is required to reduce its net capital because the equity in a market maker's account is less than the deductions with respect to the account, the OCC member is prohibited from extending further credit to that market maker account unless the carrying firm either (1) reduces its net capital by the amount of the equity short fall, or (2) calls upon the market maker to add sufficient equity to the account to eliminate the net capital charge. If a market maker fails to meet a call for additional equity, the OCC member must liquidate the market maker's account and give notice of the market maker's failure to meet the call to the Commission, and to the self-regulatory organization responsible for examining the financial condition of the OCC member and the market maker.

Each market maker's account must be computed separately. Market maker clearing firms are expressly prohibited from offsetting a deficit in one market maker account with the excess equity in another market maker account. 17/

The Commission's net capital rule also limits the volume of market maker business an OCC member can carry in relation to its net capital. This provision was designed to prevent an OCC member firm from carrying excessive market maker positions and to provide a cushion of capital in view of the unique and somewhat risky nature of the business of carrying market maker accounts. Currently, the net capital rule requires that the

aggregate deductions with respect to all the market maker accounts
carried by an OCC member, not exceed ten times the carrying firm's net
capital for a period exceeding five consecutive business days.

d. OCC Settlement Requirements

The premiums owed to and by OCC members as a result of the options
transactions cleared by them are due in cash the business day following
the transactions. These premiums and other amounts owed OCC are referred
to as "margin deposits," although they bear no relationship to FRB margin
requirements.

OCC clearing members maintain separate clearing accounts at OCC
defined by the origin of the transactions in the accounts. One account
is maintained for options transactions for public and non-market maker
broker-dealer customers ("customer account"). A second is maintained
for options transactions for the OCC member's own account ("proprietary
account"). A third account is maintained for options transactions for
the market maker accounts carried by the OCC member ("market maker account").

OCC determines, daily, the settlement requirements for each options
class in each of these separate accounts. Amounts due to and from OCC
are netted within each account to arrive at a daily settlement amount
for each separate account.

The net amount due to and from OCC is determined differently for
the customer accounts than it is for the proprietary and market maker
accounts. Long options and short options positions in customers' accounts are not netted against one another. The premiums on all options transactions must be paid in full and, in the case of uncovered short options positions, the short options premium plus an additional 30 percent of that premium is also due to OCC to protect against the risks of adverse options price movements. All short options positions are treated as uncovered by OCC until it receives a depository or escrow receipt for the underlying stock. No margin offset for long options positions in customer accounts is permitted by OCC since these positions must be segregated by broker-dealers pursuant to the Commission's customer protection rule which generally prohibits a broker-dealer from subjecting customers' fully paid securities to a lien. 18/  

When computing the margin deposit for options positions in firm proprietary and market maker accounts, long options positions can be used to offset short options positions in the same options class by pairing the long and short positions on a contract-by-contract basis. The market value of the paired long and short options positions are then totaled. If the total market value of the short options positions exceeds the total market value of the long positions, 130 percent of the excess must be deposited with OCC. In addition, 130 percent of the market value of total short positions which are

18/ OCC Rule 601a.
not paired with a long position in the same options class must be deposited with OCC. The premium received on the sale of short options positions is left with OCC and can be used to satisfy the deposit requirement. In addition, if the total market value of the long options positions exceeds the total market value of the paired short positions, 70 percent of the excess long positions market value can be used to meet the "margin deposit" for unpaired short options positions in the same options class in the particular account and, to the extent not so used, 35 percent of the excess market value of any long options position may be used as "margin" for amounts due OCC for other options classes in only that account. 19/

For purposes of these computations, assignment of an exercise notice to an options account will result in treating options contracts that have been assigned as uncovered short positions unless they are offset by long positions in the same options class, or, if calls are involved, the calls are covered with the underlying security.

The following chart sets forth an example of the computation of the margin deposit in a clearing firm's proprietary or market maker account with both net long and net short positions in different classes of options.

19/ OCC Rule 601b.
### Market maker RLS Account
#### Daily Margin Report

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<td>$2,860</td>
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<td>margin on excess short</td>
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<td>$1,560</td>
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<td>margin on paired short</td>
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<td>4,420</td>
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<td>margin on YYY class</td>
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<td>- 1,970</td>
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<td>50% of XXX excess credit</td>
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<td>$2,450</td>
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<td>net margin reg</td>
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Prepared by Options Study Staff
OCC members clearing market maker accounts may establish at
OCC either a separate account for each market maker or a combined
account for all market maker accounts it clears. In either case,
the OCC member must obtain from each market maker for which the
member clears an account, an agreement which provides that:

—OCC has a lien on all long positions, securities,
margin and other funds in the market maker's
account as security for the clearing member's
obligations for all transactions effected in the
account, short positions maintained in the account
and exercises assigned to the account;

—OCC has the right to net all short positions
against all long positions in the account; and

—OCC can close out the position in the account
without prior notice to the market maker.

If the market maker positions are carried in a combined account the
agreement must also provide that the positions of one market maker can
be combined in the account with other market maker's positions. 20/

Most OCC member market maker clearing firms maintain combined
market maker accounts at OCC because netting one market maker's
position with another may reduce the clearing firm's OCC "margin
deposit" requirements. The market maker clearing firm's net capital
requirements, however, are the same whether the market makers'
accounts are maintained at OCC on a combined or separate basis.

20/ OCC art. VI, § 3.
The daily settlement amounts, or "margin deposits," due to OCC are either paid utilizing excess cash in the member's margin account at OCC, or are obtained through the issuance of a draft upon the OCC member's account at an approved bank on which OCC is authorized to draw.

Although OCC initially requires cash to satisfy amounts owed to it, clearing members may subsequently deposit with OCC during the day approved bank letters of credit, United States government securities maturing within 10 years, or stock underlying uncovered short options positions, and they may withdraw any excess "margin deposits". 21/

United States government securities or securities underlying short options contracts are not deposited directly with OCC for margin purposes. An approved bank, trust company or securities depository will issue a depository receipt to the OCC member which directs the bank, trust company or depository to deliver the receipted securities directly to OCC upon written request. Another method of depositing securities is an escrow receipt issued by an approved custodian in either the name of an OCC clearing member, or its customer, representing that the custodian will deliver the escrowed securities to OCC or the clearing member upon assignment. 22/

OCC has the authority to demand additional "margin deposits" ("variation margin calls") from any one or more of its members for

21/ OCC rule 604.

22/ OCC rule 610.
expected but unpredictable occurrences, such as rapid price and volume changes, when the regular daily "margin deposit" requirements described above might prove to be insufficient.

Variation margin calls typically will be made when there is a sudden movement in the Dow Jones Industrial Average ("DJIA") or if the next business day is a bank holiday in one of the cities in which OCC maintains a clearing facility. OCC will make a variation margin call demanding a 10 percent increase in the clearing member's regularly required margin deposits by 12:00 noon if the DJIA is then up or down ten points from the previous close or if the clearing member's bank will be closed on the next business day. If the DJIA is up or down by 20 points or more, the variation margin call will amount to a 20 percent increase in the regularly required margin deposit.

From 1975 to May 1978 the OCC made thirty-two variation margin calls. Twenty-four were due to a ten point DJIA move, one was due to a 20 point DJIA move and seven were due to bank holidays. 23/

In determining whether a variation margin call will be issued to a particular clearing firm, OCC reviews the member's accounts for:

--- Market price fluctuations in an options series held in a short position in such account;

--- Market price fluctuations of any security underlying a short option that has been exercised;

-- Changes in the size of a clearing member's options position; or

-- Changes in the clearing member's financial condition. 24/

e. OCC Clearing Fund

For the protection of options customers and OCC participants, OCC requires each new clearing member to contribute to an OCC maintained common fund (the "clearing fund") an initial base contribution of $10,000 plus such variable contribution as may be fixed by the Board of Directors in its discretion at the time such clearing member's application is approved. Effective October 31, 1978, each OCC member is required to maintain on deposit with OCC in the clearing fund a base contribution of $10,000 plus a proportionate share of the variable portion of the clearing fund. The variable portion is 7 per cent of the average daily value of all clearing members' option contracts in open short positions during the preceding calendar quarter. A clearing member's proportionate share of the variable portion of the fund is a fraction; the numerator of which is the average daily number of option contracts carried by such clearing member in open positions during the preceding three calendar months and the denominator of which is the average daily number of contracts carried by all clearing members during the period. The contribution each OCC member is required to maintain in the clearing fund is currently recomputed at the end of each month.