



## II. FINDINGS

The Commission finds the following:

### A. SUMMARY

Derivatives Clearing Organizations (“DCOs”) are an essential part of the U.S. futures and options markets and, as such, they are required to be structured to manage and reduce risk. In instances where a DCO is not structured and operated appropriately, it can pose a risk to the broader financial system. Disruption to a DCO’s operations, or failure by a DCO to appropriately manage risk, could result in significant costs not only to the DCO itself and its members, but also to other market participants.

Section 5b of the Act, 7 U.S.C. § 7a-1, creates a regulatory regime for DCOs that is implemented by the Commission’s Part 39 Regulations, 17 C.F.R. pt. 39 (2022) (collectively, “DCO Core Principles”).<sup>2</sup> As a registered DCO, OCC is required to comply with the DCO Core Principles, which establish the standards for the operation of DCOs. The DCO Core Principles impose, among other things, requirements relating to the financial, operational and managerial resources of a DCO; risk management standards; rules and procedures relating to management of clearing member defaults; risk analysis and oversight of operations and automated systems; and clearinghouse governance standards.

From October 2019 through May 17, 2021 (the “Relevant Period”), OCC failed to establish, implement, maintain and enforce certain policies and procedures reasonably designed to manage its operational risks by identifying the plausible sources of operational risk and mitigating their impact through the use of appropriate systems, policies, procedures, and controls. Specifically, to address the impact of certain transaction-based costs associated with the cost of liquidating a Clearing Member’s portfolio, OCC implemented an add-on charge to better account for the cost of liquidating a defaulting Clearing Member’s portfolio (the “LC Charge”) in its STANS methodology used to calculate margin. OCC failed, however, to make a corresponding change to incorporate the LC Charge in its Clearing Fund calculation in violation of OCC’s Comprehensive Stress Testing and Clearing Fund Methodology, and Liquidity Risk Management Description, which is an OCC rule. As a result, OCC’s Clearing Fund was underfunded by between \$200 million to \$588 million at various times during the Relevant Period. As a result of this conduct, OCC violated Sections 5b(c)(2)(H) and (I) of the Act, 7 U.S.C. § 7a-1(c)(2)(H), (I), and Regulations 39.17(a)(1) and 39.18(b)(1) and (2), 17 C.F.R. §§ 39.17(a)(1), 39.18(b)(1), (2) (2022).

In September 2019, the Commission instituted an action against OCC, which ordered OCC to cease and desist from committing or causing any violations and any future violations of Core Principle I (requiring system safeguards to identify and minimize sources of operational risk), and Regulation 39.18, among other provisions, and undertakings requiring that OCC

---

<sup>2</sup> See Commodity Futures Modernization Act of 2000, P.L. 106-554, 114 Stat. 2763, enacted December 21, 2000, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, P.L. 111-2013, 124 Stat. 1376, effective July 16, 2011; see also A New Regulatory Framework for Clearing Organizations, 66 Fed. Reg. 45,604 (Oct. 29, 2001).

establish and implement internal controls, and policies and procedures reasonably designed to comply with DCO Core Principles and the Regulations. *See In re OCC*, CFTC No. 19-19, 2019 WL 4267847 (Sept. 4, 2019) (consent order) (the “2019 Order”). The Commission notes its concern that OCC’s violation occurred after the Commission’s prior action finding that OCC had violated Core Principle I and Regulation 39.18 and requiring OCC to establish and implement policies and procedures reasonably designed to ensure compliance on a going forward basis.

In accepting Respondent’s Offer, the Commission recognizes OCC’s cooperation with the Division of Enforcement’s investigation of this matter. The Commission also acknowledges Respondent’s representations concerning its remediation in connection with this matter. The Commission’s recognition of Respondent’s cooperation and appropriate remediation is further reflected in the form of a reduced penalty.

## **B. RESPONDENT**

**The Options Clearing Corporation** is a Delaware corporation with its principal place of business in Chicago, Illinois. Since 2001, OCC has been registered with the Commission as a DCO for the clearing of futures contracts and options on futures contracts. Since 2008, OCC has been further authorized by the Commission to clear commodity options executed on a designated contract market in addition to futures contracts and options on futures contracts.

## **C. FACTS**

As a condition of registration, DCOs are obligated to comply with the DCO Core Principles established in Section 5b of the Act, as well as the implementing regulations promulgated by the Commission that are found in Part 39 of the Regulations. *See* CEA § 5b(c)(2)(A)(i), 7 U.S.C. § 7a-1(c)(2)(A)(i). This Order addresses OCC’s failure during the Relevant Period to comply with Core Principle I, found in Section 5b(c)(2)(I) of the Act and Regulations 39.17(a)(1) and 39.18(b)(1) and (2).

### **1. In 2019, The Commission Instituted an Action Against OCC**

In September 2019, the Commission entered an Order against OCC finding that OCC failed to establish and enforce policies and procedures involving financial risk management, operational requirements, and information-systems security in violation of Section 5b(c)(2)(B), (D), and (I) of the Act, 7 U.S.C. § 7a-1(c)(2)(B), (D), (I), and Regulations 39.11(a) and (c), 39.13(a), (b), (f), and (g)(1) and (2), and 39.18(b)(1) and (e)(1), 17 C.F.R. §§ 39.11(a), (c), 39.13(a), (b), (f), (g)(1)-(2), 39.18(b)(1), (e)(1) (2019). 2019 Order, 2019 WL 4267847.

The Commission required OCC to pay a \$5 million civil monetary penalty, and to cease and desist from violating the provisions identified above. The Commission also required OCC to comply with certain undertakings, including “implement internal controls, policies and procedures reasonably designed to comply with the DCO Core Principles and Regulations,” retain a qualified independent third-party compliance auditor, and submit a report after the auditor completed their review.

2. OCC Failed to Implement and Enforce Policies and Procedures Reasonably Designed to Manage A Certain Aspect of Its Operational Risks

After the Commission issued the 2019 Order and during the Relevant Period, OCC failed to establish, implement, maintain, and enforce policies and procedures reasonably designed to manage a certain aspect of its operational risks related to its automated systems. Specifically, in October 2019, OCC implemented the “LC Charge” in its STANS methodology used to calculate margin. OCC also planned to incorporate the LC Charge in its comparison of portfolio stress test results to ensure the LC Charge was accounted for in both the stress test results and the actual margin charge when comparing those numbers for Clearing Fund calculations. However, OCC did not properly implement changes to its Clearing Fund methodology to account for the LC Charge. Neither OCC’s Quantitative Risk Management team, its Model Validation Group, nor the Internal Audit Department identified the implementation error until at least April 21, 2021. Due to deficiencies in certain internal controls, human errors, and oversight failures, OCC did not incorporate the LC Charge into its Clearing Fund calculations until May 2021.

During the Relevant Period, OCC failed to properly account for the LC Charge in its Clearing Fund shortfall calculation. As a result of these failures, OCC’s Clearing Fund was underfunded by \$200 million to \$588 million at various times during the Relevant Period<sup>3</sup>

OCC discovered the failure on April 21, 2021 and orally informed staff of the Commission’s Division of Clearing and Risk (“DCR”) of the failure on May 7, 2021. On August 3, 2021, DCR notified OCC that the failure was a material impairment and subject to the notification requirements of Regulation 39.18(g). Accordingly, OCC formally notified the Commission of the failure on August 16, 2021.

In determining to accept the Offer, the Commission recognizes OCC's cooperation with the Division of Enforcement’s investigation and its remedial efforts. OCC voluntarily conducted and shared with Staff the factual results of an internal investigation conducted by a third party. In addition, OCC provided documents and information regarding the key issues and events that significantly advanced Staff’s investigation and conserved Commission resources.

OCC represents that it has increased its Clearing Fund and undertaken remediation to strengthen its internal controls, including the following, among other actions:

- A. On May 17, 2021, OCC increased the size of its Clearing Fund from \$11.23 billion to \$11.82 billion, an increase of approximately \$588 million or 5.24%;
- B. Developing and executing a plan designed to remediate the root causes of the implementation error associated with incorporation of the LC Charge in the OCC Clearing Fund Methodology;

---

<sup>3</sup> Notwithstanding the underfunding, OCC represents that, throughout the Relevant Period, OCC’s Clearing Fund maintained sufficient financial resources to meet its obligations in the event of a default by the single member or participant creating the largest financial exposure in extreme but plausible market conditions, in accordance with the requirements of Regulation 39.11(a)(1).

- C. Enhancing management and information technology delivery processes and controls;
- D. Engaging a third party to conduct an independent risk management review;
- E. Conducting a comprehensive review of all business logic calculations related to Clearing Fund, margin, and liquidity risk, and incorporating business logic review into the Model Valuation Group's annual review of models and review of new models; and
- F. Enhancing OCC's monitoring of model inputs and outputs.

### III. LEGAL DISCUSSION

#### A. **Violation of Section 5b(c)(2)(I)(i) of the Act and Regulation 39.18(b)(1) and (2)**

DCO Core Principle I and Regulation 39.18(b)(1), require a DCO to establish and maintain a program of risk analysis and oversight to identify and minimize sources of operational risk through the development of appropriate controls and procedures, and automated systems, that are reliable, secure, and have adequate scalable capacity. Section 5b(c)(2)(I)(i) of the Act, 7 U.S.C. § 7a-1(c)(2)(I)(i); 17 C.F.R. § 39.18(b)(1) (2022).

Regulations 39.18(b)(2)(iv) and (v) require that a DCO's program of risk analysis and oversight with respect to its operations and automated systems must address the following elements:

(iv) Systems operations, including, but not limited to, system maintenance; configuration management (including, baseline configuration, configuration change and patch management, least functionality, inventory of authorized and unauthorized devices and software); event and problem response and management; and any other elements of system operations included in generally accepted best practices; and

(v) Systems development and quality assurance, including, but not limited to, requirements development; pre-production and regression testing; change management procedures and approvals; outsourcing and vendor management; training in secure coding practices; and any other elements of systems development and quality assurance included in generally accepted best practices.

As described above, during the Relevant Period, OCC failed to establish, implement, maintain and enforce certain policies and procedures reasonably designed to manage its operational risks by neglecting to incorporate the LC Charge, in violation of its Comprehensive Stress Testing and Clearing Fund Methodology, and Liquidity Risk Management Description, which is an OCC rule. By engaging in this conduct OCC violated Section 5b(c)(2)(I)(i) of the Act and Regulation 39.18(b)(1) and (2).

**B. Violation of Section 5b(c)(2)(H)(i) of the Act and Regulation 39.17(a)(1)**

DCO Core Principle H and Regulation 39.17(a)(1) require a DCO to “maintain adequate arrangements and resources for the effective monitoring and enforcement of compliance (by itself and its clearing members) with the rules of the derivatives clearing organization and the resolution of disputes.” Section 5b(c)(2)(H)(i) of the Act, 7 U.S.C. § 7a-l(c)(2)(H)(i); 17 C.F.R. § 39.17(a)(1) (2022).

As described above, during the Relevant Period, OCC failed to maintain adequate arrangements and resources to effectively monitor and enforce compliance with its rules related to the LC Charge. By engaging in this conduct, OCC violated Core Principle H and Regulation 39.17(a)(1).

**IV. FINDINGS OF VIOLATIONS**

Based on the foregoing, the Commission finds that during the Relevant Period Respondent violated Sections 5b(c)(2)(H) and (I) of the Act, 7 U.S.C. § 7a-l(c)(2)(H), (I), and Regulations 39.17(a)(1) and 39.18(b)(1) and (2), 17 C.F.R. §§ 39.17(a)(1), 39.18(b)(1), (2) (2022).

**V. OFFER OF SETTLEMENT**

Respondent has submitted the Offer in which it, without admitting or denying the findings or conclusions herein:

- A. Acknowledges service of this Order;
- B. Admits the jurisdiction of the Commission with respect to this Order only and for any action or proceeding brought or authorized by the Commission based on violation of or enforcement of this Order;
- C. Waives:
  - 1. the filing and service of a complaint and notice of hearing;
  - 2. a hearing;
  - 3. all post-hearing procedures;
  - 4. judicial review by any court;
  - 5. any and all objections to the participation by any member of the Commission’s staff in the Commission’s consideration of the Offer;
  - 6. any and all claims that it may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 and 28 U.S.C. § 2412, and/or the rules promulgated

by the Commission in conformity therewith, Part 148 of the Regulations, 17 C.F.R. pt. 148 (2022), relating to, or arising from, this proceeding;

7. any and all claims that it may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, §§ 201-253, tit. II, 110 Stat. 847, 857-74 (codified as amended at 28 U.S.C. § 2412 and in scattered sections of 5 U.S.C. and 15 U.S.C.), relating to, or arising from, this proceeding; and
  8. any claims of Double Jeopardy based on the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief, including this Order;
- D. Stipulates that the record basis on which this Order is entered shall consist solely of the findings contained in this Order to which Respondent has consented in the Offer;
- E. Consents, solely on the basis of the Offer, to the Commission's entry of this Order that:
1. makes findings by the Commission that Respondent violated Sections 5b(c)(2)(H) and (I) of the Act, 7 U.S.C. § 7a-1(c)(2)(H), (I), and Regulations 39.17(a)(1) and 39.18(b)(1) and (2), 17 C.F.R. §§ 39.17(a)(1), 39.18(b)(1), (2) (2022).
  2. orders Respondent to cease and desist from violating Sections 5b(c)(2)(H) and (I) of the Act and Regulations 39.17(a)(1) and 39.18(b)(1) and (2).
  3. orders Respondent to pay a civil monetary penalty in the amount of five million U.S. dollars (\$5,000,000) plus any post-judgment interest; and
  4. orders Respondent and its successors and assigns to comply with the conditions and undertakings consented to in the Offer and as set forth in Part VI of this Order; and
- F. Represents that it has taken and completed remedial steps, as set forth in its August 16, 2021 Regulation 39.18 Notification including, but not limited to, engaging an independent consultant to review its remediation efforts regarding incorporating the LC Charge into its Clearing Fund methodology and to conduct a comprehensive and strategic review of OCC's overarching risk management framework and governance.

Upon consideration, the Commission has determined to accept the Offer.

## VI. ORDER

### Accordingly, IT IS HEREBY ORDERED THAT:

1. Respondent, and its successors and assigns, shall cease and desist from violating Sections 5b(c)(2)(H) and (I) of the Act, 7 U.S.C. § 7a-l(c)(2)(H), (I), and Regulations 39.17(a)(1) and 39.18(b)(1) and (2), 17 C.F.R. §§ 39.17(a)(1), 39.18(b)(1), (2) (2022).
2. Respondent shall pay a civil monetary penalty in the amount of \$5 million (“CMP Obligation”), within thirty days of the date of entry of this Order. If the CMP Obligation is not paid in full within thirty days of the date of entry of this Order, then post-judgment interest shall accrue on the CMP Obligation beginning on the date of entry of this Order and shall be determined by using the Treasury Bill rate prevailing on the date the payment installment became due pursuant to 28 U.S.C. § 1961.

Respondent shall pay the CMP Obligation and any post-judgment interest by electronic funds transfer, U.S. postal money order, certified check, bank cashier’s check, or bank money order. If payment is to be made other than by electronic funds transfer, the payment shall be made payable to the Commodity Futures Trading Commission, and sent to the address below:

MMAC/ESC/AMK326  
Commodity Futures Trading Commission  
6500 S. MacArthur Blvd.  
HQ Room 181  
Oklahoma City, OK 73169  
9-AMC-AR-CFTC@faa.gov

If payment is to be made by electronic transfer, Respondent shall contact Tonia King or her successor at the above address to receive payment instructions and shall fully comply with those instructions. Respondent shall accompany payment of the CMP Obligation with a cover letter that identifies Respondent and the name and docket number of this proceeding. Respondent shall simultaneously transmit copies of the cover letter and the form of payment to the Chief Financial Officer, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21<sup>st</sup> Street, NW, Washington, D.C. 20581.

3. Respondent and its successors and assigns shall comply with the following conditions and undertakings set forth in the Offer:
  - i. As noted above, Respondent represents that it has already undertaken and continues to undertake remedial measures set forth in its August 16, 2021 Regulation 39.18 Notification, including related to implementing the LC Charge into its Clearing Fund methodologies and a comprehensive

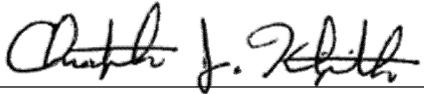
strategic review of OCC's risk management framework and governance. To the extent it has not already done so, Respondent undertakes that it will complete those remedial measures no later than one year from the date of this Order.

- ii. Respondent will undertake to complete the remediation plans discussed in Appendix C attached to the Independent Compliance Auditor's final report, dated March 22, 2022, no later than eighteen months from the date of this Order.
- iii. Respondent's Chief Executive Officer shall certify, in writing, that OCC, to the best of its knowledge based upon reasonable inquiry, has complied with the undertaking(s) set forth above. The certification shall identify the undertaking(s), provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. Staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to the Directors of the Division of Enforcement and the Division of Clearing and Risk no later than thirty (30) days from the date of OCC's completion of all remedial measures identified in the undertakings set forth herein.
- iv. Cooperation with the Commission: In this action, and in any investigation or other action instituted by the Commission related to the subject matter of this action, Respondent shall cooperate fully and expeditiously with the Commission, including the Division of Enforcement, in this action, and in any current or future Commission investigation or action related thereto.
- v. Public Statements: Respondent agrees that neither it nor any of its successors, assigns, agents, or employees under its authority or control shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in this Order, or creating, or tending to create, the impression that this Order is without a factual basis; provided, however, that nothing in this provision shall affect Respondent's: (i) testimonial obligations; or (ii) its right to take positions in other proceedings to which the Commission is not a party. Respondent and its successors and assigns shall undertake all steps necessary to ensure that all of its agents and and/or employees under its authority or control understand and comply with this agreement.
- vi. Partial Satisfaction: Respondent understands and agrees that any acceptance by the Commission of partial payment of Respondent's CMP Obligation shall not be deemed a waiver of its obligation to make further payments pursuant to this Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance.

- vii. Change of Address/Phone: Until such time as Respondent satisfies in full its CMP Obligation as set forth in this Order, Respondent shall provide written notice to the Commission by certified mail of any change to its telephone number and mailing address within ten calendar days of the change.

**The provisions of this Order shall be effective on this date.**

By the Commission:



Christopher J. Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission

Dated: February 16, 2023