THE OPTIONS CLEARING
CORPORATION

May 3, 2012

Submitted Electronically (http://www.regulations.gov)

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Identity Theft Red Flags Rules; SEC File Number S7-02-12; RIN: 3235 – AL26

Dear Ms. Murphy and Mr. Stawick,

The Options Clearing Corporation ("OCC") respectfully submits to the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC," and together with the SEC, the "Commissions") the following comments in response to the Commissions' proposed rules regarding identity theft red flags (the "Proposed Rules").[1] We appreciate the opportunity to comment on the Proposed Rules.

Overview of OCC and its Stock Loan Programs

OCC is the world's largest equity derivatives clearing organization. While OCC began as a clearinghouse for listed equity options, it has since grown into a globally recognized entity that clears a multitude of diverse and sophisticated products. OCC now provides central counterparty clearing and settlement services to 15 exchanges and trading platforms for options, financial and commodity futures, security futures, and securities lending transactions. OCC operates under the jurisdiction of both the SEC, as a Registered Clearing Agency, and the CFTC, as a Derivatives Clearing Organization. All of OCC's Clearing Members are either registered broker-dealers or futures commission merchants.[2]

[1] Identity Theft Red Flags Rules, 77 Fed. Reg. 13450 (March 6, 2012) (to be codified at 17 C.F.R. parts 162, 248).
[2] A handful of OCC's Clearing Members are Canadian registered broker-dealers.

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As part of the suite of services OCC provides to its Clearing Members, OCC offers two stock loan programs in support of the ability of Clearing Members to engage in stock lending among themselves, a Stock Loan/Hedge Program and a Market Loan Program. Under OCC's Stock Loan/Hedge Program, OCC clears and guarantees stock loan transactions entered bilaterally between Clearing Members, thereby permitting Clearing Members to use borrowed and loaned securities to reduce OCC margin requirements by reflecting the real risk of their inter-market hedged positions. Under OCC's Market Loan Program, OCC processes and maintains stock loan positions that have originated through a stock loan market. Currently, OCC clears securities lending transactions for Automated Equity Finance Markets, Inc., which operates the AQS securities lending market.

Under both programs, OCC acts as a principal counterparty in order to facilitate transaction clearing and settlement, becoming the lender to the borrower and the borrower to the lender for each transaction, and guaranteeing the return of the securities to the lender and the return of cash collateral to the borrower. All of OCC's counterparties in these transactions are Clearing Members. Notably, OCC is in a unique position among clearing organizations as the only clearinghouse offering central counterparty clearing for securities lending transactions in the U.S.

Discussion

The Proposed Rules were published pursuant to Sections 1088(a)(8) and (10) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), which amended the Fair Credit Reporting Act of 1970 ("FCRA") to add the Commissions to the list of federal agencies required to prescribe and enforce identity theft red flag rules and guidelines. The Proposed Rules generally would require an entity subject to the Commissions' guidelines to periodically determine whether it offers or maintains "covered accounts" and, if so, to develop and implement a written identity theft prevention program that is designed to detect, prevent, and mitigate identity theft in connection with certain existing accounts or the opening of new accounts.

Our comments on the Proposed Rules are limited to the scope of the Proposed Rules and application of the Proposed Rules to OCC and other clearing organizations that may support securities loan clearing services for their clearing members in the future. As explained below, the scope and definitions of the Proposed Rules are unnecessarily broad and could be read to include OCC because of its novation of securities loans among its Clearing Members. However, clearing organizations that support securities lending activities among their Clearing Members present little risk from identity theft, since all participants in the transaction are closely regulated for this purpose and the transactions themselves are strictly controlled wholesale institutional operations rather than the type of retail operations that are the focus of the red flags rules. Accordingly, we urge the Commissions specifically to exclude clearing organizations from the scope of the Proposed Rules.

A. *The scope of the Proposed Rules and definitions of a "creditor" are unclear and unnecessarily broad.*

The Commissions' respective scope sections, when read together with their respective definitions of a "creditor," are unclear and unnecessarily broad. In particular, proposed subsection 248.201(a)(1) provides that the SEC's Proposed Rule would apply to any financial institution[3] or creditor that is registered or required to be registered under the Securities Exchange Act of 1934.[4] Proposed subsection 248.201(b)(5) would define a "creditor" by reference to the FCRA statutory definition, but adds that the term "includes lenders such as brokers or dealers offering margin accounts, securities lending services, and short selling services."[5] When read together, these two subsections could be read to apply the SEC's Proposed Rule to OCC, an entity registered with the SEC that acts as principal in order to clear securities lending transactions among its Clearing Members.

By contrast, the CFTC's scope section would apply its Proposed Rule to all financial institutions or "creditors" subject to the jurisdiction of the CFTC,[6] but the CFTC's definition of a "creditor" provides that it "includes any futures commission merchant, retail foreign exchange dealer, commodity trading advisor, commodity pool operator, introducing broker, swap dealer, or major swap participant" that regularly extends, renews, or continues credit or makes credit arrangements.[7] Since the list of entities included in the CFTC's proposed definition of a "creditor" does not include derivatives clearing organizations, and since the listed entities are distinguishable from derivatives clearing organizations in that they all engage in retail customer business and maintain retail customer accounts, it appears that the CFTC's Proposed Rule is not intended to apply to OCC. The CFTC's Proposed Rule is not entirely clear in this regard, however, because the listed examples do not necessarily preclude a broader application of the Proposed Rule.

In light of the inconsistent structure of the Commissions' respective Proposed Rules, and the ambiguities of each, we encourage the Commissions to expressly exclude clearing organizations from the scope of the Proposed Rules because, as explained below, clearing organizations like OCC should not be considered "creditors" for these purposes.

B. *OCC does not satisfy the statutory definition of "creditor."*

As a threshold matter, it is critical to understand that OCC does not meet the statutorily specified criteria of a "creditor" under the FCRA. Specifically, OCC does not, regularly and in the ordinary course of business (i) obtain or use consumer reports, directly or indirectly, in connection with credit transactions; (ii) furnish information to consumer reporting agencies in connection with credit transactions; or (iii) advance "funds" to or on behalf of a person, based on

[3] We address only the reference to "creditor" in this comment because OCC does not engage in any activities that could result in it being considered a "financial institution" for these purposes.
[4] Proposed 17 C.F.R. § 248.201(a)(1).
[5] *Id.* § 248.201(b)(5).
[6] *Id.* § 162.30(a).
[7] *Id.* § 162.30(b)(5).

an obligation of the person to repay the funds.[8] Although, as explained above, OCC does novate securities loans as part of its clearing and settlement services on behalf of Clearing Members, securities are not "funds" and lending securities should not be deemed to be "advancing funds" for this purpose.[9] Although the FCRA itself does not define the term "funds," the legislative history indicates that the term was intended as a synonym for money.[10] If Congress had intended the red flags rules to apply to loans of other assets categories, surely it would have specified that the provision applied to such transactions rather than solely to transactions involving the advancing of funds.

The fact that securities lending does not satisfy the foregoing statutory criteria is not the end of the analysis, however, because Congress did grant the enforcement agencies further authority to include in the definition of creditor: "any other type of creditor, as defined in that section 1691a of this title, as the agency described in paragraph (1) having authority over that creditor may determine appropriate by rule promulgated by that agency, *based on a determination that such creditor offers or maintains accounts that are subject to a reasonably foreseeable risk of identity theft.*"[11] If the Commissions intend to exercise this authority, however, it is incumbent upon them to provide reasoned justification for why they believe that securities clearing accounts with a clearing organization are subject to a reasonably foreseeable risk of identity theft.[12] No such rationale accompanies the Proposed Rules. To the contrary, the Commissions simply ask the question whether broker-dealers (not clearing organizations) that offer securities lending services are likely to qualify as creditors. We believe that there is no reasonable basis for concluding that the securities loan clearing services offered by OCC as described above would pose a reasonably foreseeable risk of identity theft or that such services should cause OCC to be considered a "creditor."

The Commissions acknowledge in the Supplementary Information to the Proposed Rules that "some financial institutions or creditors regulated by the Commissions may engage only in transactions with businesses where the risk of identity theft is minimal."[13] Nowhere is this more true than in connection with OCC's novation of securities loans. OCC maintains no consumer accounts. As a clearing organization, it merely acts as an intermediary in securities lending

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[8] *See* 15 U.S.C. § 1681m(e)(4). It should also be noted that while OCC acts as a principal counterparty in its securities lending transactions, when the transaction is viewed as a whole, OCC merely acts as an intermediary between Clearing Members. As such, OCC is not acting as a creditor in the sense generally targeted by the red flags provisions, but is merely facilitating settlement among counter-parties.

[9] The Clearing Member that lends the securities receives cash collateral pledged by the borrowing Clearing Member. Although cash collateral could be considered "funds", to the extent that OCC handles the cash collateral, OCC merely acts as an intermediary with respect to the receipt and repledge of this collateral to the securities lender. It does not lend its own "funds" and its role in facilitating the pledge of collateral between two regulated market participants should not be considered lending of those funds merely because it novates the transaction in order to enable the collateral pledge between Clearing Members.

[10] *See* 156 Cong. Rec. H8060 (daily ed. Dec. 7, 2010) (statement of Rep. Broun); 156 Cong. Rec. S8289 (daily ed. Nov. 30, 2010) (statement of Sen. Dodd) (explaining that the Red Flag Program Clarification Act of 2010 "narrows the applicability of the red flag identity theft provisions of the FACT Act to cover those creditors where identity thieves can do the most harm—creditors that use consumer reports, furnish information to consumer reporting agencies, and other creditors that loan money, such as payday lenders . . . .").

[11] *See* 15 U.S.C. § 1681m(e)(4)(C) (emphasis added).

[12] In the Supplementary Information to the Proposed Rules, the Commissions claim that they are not proposing to exercise this authority and expand the definition of "creditor." 77 Fed Reg. at 13454, n. 38.

[13] 77 Fed. Reg. at 13455.

transactions among its highly regulated Clearing Members. Those sophisticated institutions have stringent controls in place with respect to their operations. Those controls, coupled with transaction auditing conducted both at the individual institutions and at OCC, as the clearing organization, help ensure transaction integrity.

Moreover, while it might be possible to liquidate borrowed securities for fraudulent purposes, the trail created by securities lending transactions among Clearing Members would make if virtually impossible to use those systems for the purposes covered by the red flags rules. Indeed, we are not aware of a single instance of identity theft, or attempted identity theft, in connection with securities lending transactions cleared by OCC in the entire history of those operations. Accordingly, the nature of OCC's clearing business is such that it does not, and will not, maintain any consumer accounts or other accounts for which there is a "reasonably foreseeable risk" to OCC or its Clearing Members from identity theft. To the extent the Commissions have concerns about the underlying consumer accounts held by OCC's Clearing Members being subject to a reasonably foreseeable risk of identity theft, those concerns are better addressed directly in more targeted provisions related to specific "lending" risks at Clearing Members, rather than through unworkable and burdensome obligations on the clearing organization.

C. *OCC's cost and burden of complying with the Proposed Rules would greatly exceed any anticipated benefits.*

Since OCC maintains no covered accounts, and OCC's Clearing Members otherwise are subject to the Proposed Rules, the sole effect of including OCC within the scope of the Proposed Rules would be to require OCC to periodically reassess whether it maintains any covered accounts, including by conducting a risk assessment, and to maintain records demonstrating that it maintains no accounts for which there is a reasonably foreseeable risk to OCC or its Clearing Members from identity theft.[14] Since there is no reasonable likelihood that the outcome of that periodic assessment would change in the absence of a radical change in OCC's business, there would be no consumer or supervisory benefit from requiring OCC to undertake such an assessment. Rather, the periodic assessment merely would increase OCC's compliance costs and divert resources from its other compliance and operational priorities.

Conclusion

While the Commissions may not have intended for OCC's securities loan clearing services to be included in the scope of the Proposed Rules in the first place, we believe the issue is ambiguous enough in the Proposed Rules, and the compliance burden is high enough, to warrant clarification of this point. Unlike other industry participants, OCC, as a clearing organization, does not maintain retail accounts or transact retail business. Rather, OCC and other clearing organization solely serve other regulated industry participants, who may themselves have the retail investor relationships. To the extent that those other industry participants acts as financial institutions or creditors and maintain "covered accounts" for their customers, they are in a better position to monitor, detect, and thwart identity theft and separately are subject to the Proposed Rules. Accordingly, there would be no added benefit realized by

[14] Proposed 17 C.F.R. §§ 162.30(c); 248.201(c).

subjecting OCC to the identity theft prevention program requirements in the Proposed Rules with respect to its purely wholesale and tightly controlled clearing and settlement activities among regulated industry participants. We propose that expressly excluding clearing organizations from the scope of the Proposed Rules would strike the appropriate balance between mitigating the risks to customers and creditors of identity theft and minimizing the compliance burden placed on regulated entities.

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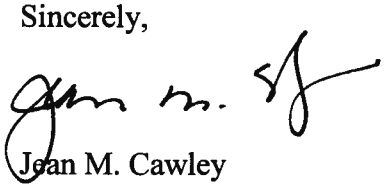
We appreciate this opportunity to comment on the Proposed Rules. If you have any questions regarding these comments, please call me at (312) 322-6269.

Sincerely,



Joan M. Cawley

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