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OCC news

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occ expands futures clearing portfolio

OCC was chosen as the clearinghouse for two new futures exchanges this fall. Both should be on line in early 2009 and promise to boost futures volumes and add new functionalities to OCC's services.

In October, NYSE Liffe selected OCC to clear and settle the exchange's new futures and futures options contracts on gold and silver. These contracts will begin trading in the first quarter of 2009.

NYSE Liffe, the U.S. futures exchange of NYSE Euronext, received Designated Contract Market (DCM) status on August 21 and launched on September 8, 2008, providing a transparent, liquid market for 100 oz. gold futures, 5,000 oz. silver futures, options on gold and silver futures, and mini-sized 33.2 oz. gold and 1,000 oz. silver futures. These products were purchased from the Chicago Mercantile Exchange in early 2008. Clearing will



transfer from CME to OCC by the end of the first quarter 2009. While OCC already clears futures products, NYSE Liffe's metals contracts allow for expansion and new functionality. More specifically, OCC is adding processing to support around-the-clock trading and updating the delivery processes so the interfaces will include a delivery agent.

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The Electronic Liquidity Exchange (ELX) announced in early December that it had selected OCC to provide clearing and settlement services. ELX was established as a competitive alternative serving global futures market participants with a mission of bringing enhanced liquidity, cost-effectiveness, and reliability to global futures trading. Investors in ELX include Bank of America, Barclays Capital, BGC Partners, Citi, Credit Suisse, Deutsche Bank Securities, GETCO, J.P. Morgan, Merrill Lynch, PEAK6-Breakwater and The Royal Bank of Scotland.

Initially ELX plans to offer Treasury futures before evolving into a multi-asset class platform.

With the addition of ELX and NYSE Liffe products, OCC will be expanding its clearing capacity, especially in the physical settlement of products.

Well established as the world's premier derivatives clearing organization known for the clearing and settlement of equity options, OCC currently clears contracts for the seven U.S. options markets as well as CBOE Futures Exchange, OneChicago and the Philadelphia Board of Trade.

updates from the hill

By Bradley Edgell



OCC has worked throughout 2008 in Washington, D.C. to address critical issues facing our industry. During the first quarter of 2008, Congress focused on reauthorizing the Commodity Futures Trading Commission (CFTC), which is one of two federal regulators overseeing OCC. Also, we have devoted attention to passing legislation that makes customer portfolio margining

more efficient. OCC has also been working closely on issues related to the financial crisis that has gripped our economy.

The CFTC must be reauthorized by Congress every five years. Since this legislation provides direction for one of OCC's primary regulators, it frequently addresses several issues impacting our organization. For example, we helped influence the debate surrounding this legislation by seeking an amendment that would protect portfolio margining customers who desired to carry futures and securities in their portfolio margining account. Currently, portfolio margining customers are not permitted to carry futures in these accounts due to legal limitations. As a result, we sought for legislators drafting the CFTC reauthorization bill to amend the Securities Investor Protection Act (SIPA) to insure these investors are covered by its customer protection regime. Although these legislators ultimately decided not to include a SIPA amendment in the CFTC reauthorization bill, our efforts helped lead to its inclusion in the Securities Act of 2008.

The Securities Act of 2008, introduced by Rep. Paul Kanjorski, includes a variety of provisions aimed to enhance the effectiveness of another OCC regulator, the Securities and Exchange Commission (SEC). Title VIII of this bill would amend SIPA to protect all portfolio margining customers from a broker-dealer insolvency. The House of Representatives passed this bill by voice vote on September 11, 2008, and we are working to encourage the Senate to pass the bill before Congress adjourns. Regardless of the legislation's

outcome, a great deal of progress has been made on this issue for Congress to consider in 2009.

During the latter half of the year, we focused our efforts on both legislative and regulatory issues related to the financial crisis. For example, OCC worked closely with industry representatives and the SEC to insure the SEC's Emergency Order against short selling did not adversely disrupt the options markets.

We are also working closely with lawmakers as they consider alternative approaches to our nation's financial regulatory structure. In July, several OCC executives met with key congressional staff to discuss various risk management models that could be used for clearing credit-default swaps. A variety of Senate and House Committees held hearings about the clearing of credit default swaps. Witnesses at these hearings included both regulators and representatives from the proposed credit default swap clearinghouses. We expect further regulatory and Congressional action on this issue in the near future.

Policymakers are debating the merits of reforming our regulatory system. The Treasury Department issued its Blueprint for a Modernized Financial Regulatory Structure and Congress is expected to debate and consider complex legislation next year on how to reform our nation's financial regulatory structure.

We are always focused on educating key members of Congress, the SEC, and CFTC on critical industry developments. We helped coordinate The Options Industry Council's Washington educational events in December in pursuit of our educational objectives.

We are expecting significant changes in the political system due to the recent election. There will be a new Administration as a result of the presidential election and a significant number of new Members of Congress and the U.S. Senate who are likely to be involved in the upcoming debate on financial modernization.

industry insight

ise president and ceo gary katz

OCC News continues its series of interviews with prominent industry leaders from OCC's participant exchanges. Gary Katz, President and CEO of the International Securities Exchange (ISE) recently sat down with OCC News to discuss the revolution of electronic trading and what lies ahead for the industry.



How did you get your start in the options industry?

I had two choices upon leaving NYU's graduate school in 1986. I could go back to my career as an actuary in the insurance field or look for something new in the financial arena. I had heard that the New York Stock Exchange (NYSE) was building a nascent options business headed by Ivers Riley who was well-known for his leadership skill and his industry

knowledge. I accepted the position at the NYSE in the options division and on my first day learned that Ivers was moving to the American Stock Exchange (AMEX).

As with all things, good comes from change because it was at that time that my 22-year working relationship with David Krell was born. My first responsibility at the NYSE was to develop a new index for options trading called the NYSE Beta index. It was designed to move up and down one and a half to two times the amount that the stock market moved. It's ironic that at that time we were designing instruments that were intended to magnify volatility.

In 1997, the NYSE exited the options business, selling it to the Chicago Board Options Exchange (CBOE). David Krell and I used this opportunity to start a consulting business. Our company K-Squared Research's primary goal was to provide marketing services that would attract listed companies to different specialist units. Shortly after we got started, Bill Porter and Marty Averbuch, who were employed at E*TRADE at the time, were thinking about starting an options exchange and were looking for executives who knew how to run an options business. They pitched us their idea about starting an all-electronic market for options. Consequently, we stopped the consulting business and joined Bill and Marty in creating the International Securities Exchange.

What key experience has been pivotal in shaping your professional life?

Founding the ISE in 1997 with David, Bill and Marty was a once-in-a-lifetime experience. What makes the experience so

powerful is recognizing that each one of us brought something to the table that was necessary for the venture to succeed. We raised the seed capital, developed patented intellectual property, searched the globe for technology partners, and hired the best exchange team to run the business in a way that delivered a trading experience far above anyone's expectations. When I think back to that original group, together, we changed the options industry forever.

However, it is important to point out that while the four of us had the ideas and we did the early leg work, we would not have been able to do any of this without the team of people who came on board to build this exchange. From a technological and regulatory perspective to marketing and media relations, every element of what makes a successful company is important and we have, in my opinion, the best team on the street.

ISE was the first all-electronic U.S. options exchange. Were you concerned at all about taking the personal aspect out of options trading by moving market makers and liquidity providers "upstairs" while the other exchanges were on the floor?



In the beginning we knew that the trading floor would have an advantage when it came to trading certain strategies that involved relationships for crossing business or complicated timing for spreads or delta neutral orders. Because of this, we focused on simple

market and limit orders where ISE had an advantage as the first all-electronic exchange: tighter bid-ask spreads, deeper size and speed of execution. Later, as ISE's success and standing grew within the industry, we focused our attention on developing all-electronic mechanisms to replicate the transactions that were being done on the floor, providing greater efficiency without compromising the ability to customize trades by entering multi-legged spread strategies or tied-to-stock orders. At one time some believed that these sophisticated trading strategies could only take place on a floor, but today, volume from our advanced functionalities contributes double-digit market share to our business.

In what ways has ISE reached out on an international level and where do you see options heading within the global marketplace?

Through our merger with Eurex, ISE is now part of the leading global derivatives exchange. Our international consolidation recognizes that technology is making the world smaller while investors are searching for alternative asset classes to diversify their holdings and

manage risk. Exchange-traded and centrally-cleared options are a key product choice for managing risk and will play an increasingly important role in the global marketplace.



Earlier this year, ISE, together with Eurex and Eurex Clearing, announced a partnership with OCC to deliver the first modern international link for trading and clearing. Our market analysis has shown there is a strong desire to trade U.S.-based options from Europe,

Asia and the Middle East. Scheduled to launch in the fourth quarter of 2009, this link will provide Eurex customers with direct access to products listed on ISE's platform using their current connections and clearing accounts.

As the financial marketplace becomes more interconnected, how crucial is it for the industry to stay ahead of the technology curve?

It is critical. Staying ahead of the curve is not just about speed. It also includes system reliability, peak processing capability, customer service tools and innovative functionality. This commitment to continuous improvement is part of what explains our success, and is embedded in ISE's DNA. If you don't stay ahead of the curve, it's like trying to rest on an icy mountain slope – you slide backward if you stop moving forward. That is why we recently announced a new cutting edge Global Trading System that we are jointly building with Eurex and Deutsche Börse. The scalable platform is being designed with input from customers and will have multi-asset class trading capabilities. ISE will begin trading options on this new platform in 2011. Ultimately, it may be used as a common platform for all Deutsche Börse exchanges.

ISE changed the landscape of the industry almost a decade ago by opening up the multiple listing of options. From your perspective, what have been some of ISE's other major contributions?

We brought full transparency to the markets. Prior to ISE, options quotes did not display size and were only good for customers. ISE was the first exchange in the U.S. to display size not only through OPRA but through a front-end workstation as well. In addition, we were the first options exchange to provide a "What You See Is What You Get" market with firm quotes for all participants whether they were customers, proprietary traders or market makers. Together, the competition, transparency and efficiency that ISE introduced to the industry revolutionized the way that options were traded.

oic builds upon its global outreach efforts

As the financial marketplace becomes increasingly interconnected on an international level, The Options Industry Council (OIC) continues to make enormous strides towards building educational cooperatives with its overseas counterparts. This past November, the Warsaw Stock Exchange (WSE) and OIC announced that they have entered into a licensing agreement that will pave the way towards the development of educational programming geared towards Polish investors.

This agreement, which is the first of its kind between OIC and a European exchange, stands to further increase the visibility of the U.S. options industry within Europe's financial community as well as encourage continued dialogue between the United States and Europe.

"Investor interest in trading equity options continues to rise globally," said Gina McFadden, President of OIC. "This new licensing agreement with the Warsaw Stock Exchange expands OIC's efforts in educating European investors who already have a significant impact on U.S. options volume."

A similar licensing agreement has also been established in Canada as OIC partnered with the Montreal Exchange Inc. (MX) to host four options education days in Calgary, Edmonton, Toronto and Montreal. In total, more than 600 investors attended full-day events featuring OIC's Basic and Intermediate seminars.

In addition, OIC has further expanded its international outreach efforts in Asia by entering into a content sharing agreement with the Thailand Futures Exchange (TFEX). OIC and TFEX are currently collaborating on a number of information sharing and co-branding initiatives including the translation of several key areas of OIC's web site to Thai and the distribution of popular educational tools, such as the Options Investigator CD, to Thai investors. The CDs feature both OIC and TFEX branding. This past spring, OIC and TFEX co-hosted options seminars in Thailand. Video presentations of the two-day event are being made available for viewing on TFEX's web site.

Going into 2009, OIC will continue to build upon the ties that have been established in several key markets abroad and aggressively seek out new alliances that will further promote and raise awareness about options within the international financial community.



symbology symposium updates as osi prepares for next stages

This past September, the Options Symbology Symposium was held in New York. The one-day conference was a chance for industry professionals to hear from the exchanges, vendors, broker-dealers and OCC about the implementation schedule, testing requirements and upcoming enhancements that have been outlined through the industry-wide Symbology project.

Dave Harrison, OCC Vice President, Member Services stated that the general take-away from the conference is that the exchanges and OCC have been consistent in their message about preparing for scripted industry testing and will continue to encourage the industry to become certified prior to the start of the testing date in September 2009. Conference sessions covered topics such as updates on test connections with exchanges and utilities; how the certification process works; requirements for Electronic Blue Sheet reporting; best practices for front-end displays; and the differences between conversion and consolidation.

Discussions during the Symposium included recommendations of a standard display for the Options Symbology Initiative (OSI) key, outlined costs for the industry conversion, and client involvement and communication about the industry initiative. The OSI committee encouraged firms to support the four key fields as appropriate within their systems. The committee stated that while they understood the desire for a standardized key, there simply wasn't a solution that would fit every participant's needs. Another session prompted a discus-

sion of the costs associated with the Symbology conversion project. Cost figures presented at the Symposium were extrapolated from responses that were received from survey participants which may or may not accurately represent a diverse sampling of industry. The committee reminded Symposium attendees that the OSI was never entered into by the industry as a cost-savings venture. OSI has and continues to be viewed as an opportunity to move the industry forward. In addition, presenters emphasized the need for clearing members to communicate with their customers to ensure that they understand OSI's impact. To view conference presentations, visit <http://events.sifma.org/2008>.

The OSI Committee has also been working on finalizing the test scripts following the end of the comment period. The latest version of the test scripts is available for download on OCC's web site. Certification testing with OCC and the exchanges has begun and is tentatively scheduled to be completed prior to industry script testing in September 2009. Exchanges will distribute an information memo with pre-certification guidelines. OCC has released its own memo which is available under the Symbology Initiative link at <http://www.theocc.com/>. Clearing members who have questions regarding testing should contact staff at OSI_Testing@theocc.com.

For more information on Symbology or technical specifications on the upcoming testing plan and project milestones, visit OCC's web site, or contact Erin Collins at ecollins@theocc.com.

system enhancements improve trading processing efficiency

Since 2007, OCC has been managing a coordinated effort among its production and technology departments to improve cleared trade processing for its members. This cross-team effort has been supported by staff in many different departments including Application Services, Member Services, Production Services and Technology Services. Some of the improved benefits to OCC's cleared trade processing include increased High Volume Testing (HVT) capabilities, increased maximum trades per hour from 140k in 2007 to 277k this year, an improved OCC processing average (up to 90% of

cleared trades within 5-10 minutes), and streamlined cleared trade processing, which reflect a more accurate, real-time process.

Network enhancements resulting in improved production include changing out system wiring to reduce overall network communication time, and installing a z9 Processor with a faster engine which has freed up one-third of the processing time. The technology departments also implemented specialty engine processors – zIIP and zAAP – providing additional capacity on the network, which has resulted in faster processing.

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The Application Assist Processor (zAAP) was able to take on the majority of the JAVA processing workload contributing to freeing up space for data server (DB2) work on the main processor. The Integrated Information Processor's (zIIP) implementation assisted in processing over one-third of the DB2 workload from the main processor. The combined improvements attributed to decreasing the DB2 workload but also helped reduce costs by an average of \$30,000 per month.

OCC was able to make improvements in regards to the out-bound piece of cleared trades. Upgrades that contributed to better processing include installing performance changes to Data Distribution Service (DDS) cleared trades in order to tune the Standard Query Language (SQL), switching to Application Unix Servers, increasing the bandwidth to the disk from 100MB to 1GB, changing the trades job from three threads to four, changing the trades job to write temporary data to non-SRDF (Symmetrix Remote Data Facility) disks, changing to a commit count in order to process more records before writing it to permanent files, and implementing a best practice to adjust DDS trades SQL when new opportunities arise. Application Services

worked with OCC's technology staff to reduce bottleneck areas in the processing system. The HVTs have contributed to identifying these bottleneck areas, along with testing solutions, which has resulted in decreased roadblocks to efficient trade processing.

"From March 2007 through last Spring, we've made some major improvements due mainly to OCC's ability to work as a cross-functional team," said David Cerda, Application Development Manager, Application Services. "The communication between departments enables us to test solutions that modernize our processing systems. This effort really benefits our clearing members, delivering them a more real-time, efficient processing and helps OCC meet those quality standards time and time again."

Looking ahead, OCC plans to take additional steps to increase network availability and dependability to grow efficiency standards even further. Projected enhancements include implementing Parallel Access Volumes (PAVs) that will update the physical disk writing process to help free up network usage. There is also a 2009 initiative to upgrade the Storage Area Networks (SANs) that will help reduce processing overhead.

options prominently featured at fia expo

The options industry was again featured with a full day of panels devoted to options issues during the FIA Futures and Options Expo which took place in Chicago this past November. As part of the Expo agenda for the past few years, the options track continues to grow in popularity as the sessions draw increasing numbers of attendees.

Overall, it was another tremendous year for the FIA Expo as more than 4,500 individuals from over 30 different countries took part in this annual event. The five options sessions included the ever-popular exchange leaders panel, while other sessions focused on regulatory, trading platform and market structure issues.

OCC Senior Vice Presidents Susan Milligan and Mike Walinskas are both a part of the 12-member Expo Equity Options Steering Committee, helping to design the options track along with representatives of the options exchanges and member firms.

Perhaps no panel discussion at Expo has seen greater attendance growth over the last several years than the clearing panel. Once again, Michael Cahill, OCC President and Chief Operating Officer, participated in the discussion, this year titled "New Concepts for Clearing." Featuring a distinguished panel of clearinghouse leaders from the United States and Europe, this session covered, among other things, the recent headline topics of bringing over-the-counter products and credit derivative swaps into a central counterparty clearing system.

OCC was also represented by Amy Lawson, Vice President, Products and Business Development, during the Give-Up Workshop. This session examined the operational side of give-up agreements, including getting the agreement in place, managing rates, third-party billing, and execution pay and collect systems.

OCC news

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Editor/Designer: Leisha Nicol