

defined in rule 2a-7 under the Act. No Participant would be permitted to invest in a Joint Account or joint Purchase Account unless the Short-Term Investments made by the Participant in such Joint Account or joint Purchase Account satisfied the investment policies and guidelines of that Participant. Short-Term Investments that are repurchase agreements would have a remaining maturity of 60 days or less and other Short-Term Investments would have a remaining maturity of 90 days or less, as calculated in accordance with rule 2a-7 under the Act.

3. All assets held in the Joint Accounts would be valued on an amortized cost basis to the extent permitted by applicable SEC releases, rules, or orders.

4. Each Participant that is a registered investment company valuing its net assets in reliance on rule 2a-7 under the Act will use the average maturity of the instruments in the Joint Account in which such Participant has an interest (determined on a dollar-weighted basis) for the purpose of computing its average portfolio maturity with respect to its portion of assets held in a Joint Account on that day.

5. In order to assure that there will be no opportunity for one Participant to use any part of a balance of a Joint Account or joint Purchase Account credited to another Participant, no Participant will be allowed to create a negative balance in any Joint Account or joint Purchase Account for any reason, although each Participant would be permitted to draw down its entire balance at any time. In no case would an early termination by less than all Participants be permitted if it would reduce the principal amount or yield received by other Participants in a particular Joint Account or joint Purchase Account or otherwise adversely affect the other Participants. Each Participant's decision to invest in a Joint Account would be solely at its option, and no Participant will be obligated to invest in the Joint Account or to maintain any minimum balance in the Joint Account. In addition, each Participant will retain the sole rights of ownership of any of its assets invested in the Joint Account or joint Purchase Account, including interest payable on such assets invested in the Joint Account or joint Purchase Account.

6. The Advisers will administer the investment of cash balances in, and the operation of, the Joint Accounts or joint Purchase Accounts as part of their general duties under their advisory agreements with Participants and will not collect any additional or separate

fees for advising any Joint Account or joint Purchase Account.

7. The administration of the Joint Accounts or joint Purchase Accounts will be within the fidelity bond coverage required by section 17(g) of the Act and rule 17g-1 thereunder.

8. The directors or trustees of the Funds will adopt procedures pursuant to which the Joint Accounts or joint Purchase Accounts will operate, which will be reasonably designed to provide that the requirements of the application will be met. The directors or trustees will make and approve such changes as they deem necessary to ensure that such procedures are followed. The directors or trustees will determine, no less frequently than annually, that the Joint Accounts have been operated in accordance with the proposed procedures. Furthermore, the directors or trustees will only permit a Participant to continue to participate in a Joint Account or joint Purchase Account if they determine that there is a reasonable likelihood that the Participant and its shareholders will benefit from the Participant's continued participation.

9. Any Short-Term Investment made through the Joint Accounts will satisfy the investment criteria of all Participants in that investment. Repurchase agreements purchased through a joint Purchase Account will satisfy the investment criteria of all Participants in the investment.

10. Each Participant's investment in a Joint Account will be documented daily on the books of each Participant and the books of its custodian. Each Participant will maintain records (in conformity with section 31 of the Act and rules thereunder) documenting for any given day, its aggregate investment in a Joint Account and its *pro rata* share of each Short-Term Investment made through such Joint Account. Each Participant that is not a registered investment company or registered investment adviser will make available to the SEC, upon request, such books and records with respect to its participation in a Joint Account.

11. Every Participant in the Joint Accounts will not necessarily have its cash invested in every Short-Term Investment. However, to the extent that a Participant's cash is applied to a particular Short-Term Investment, the Participant will participate in and own its proportionate share of such Short-Term Investment, and any income earned or accrued thereon, based upon the percentage of such investment purchased with monies contributed by the Participant. This condition shall also apply to the repurchase agreements

purchased through a joint Purchase Account.

12. Short-Term Investments held in a Joint Account generally will not be sold prior to maturity except if: (a) The Advisers believe the investment no longer presents minimal credit risks; (b) the investment no longer satisfies the investment criteria of all Participants in the investment because of downgrading or otherwise; or (c) in the case of a repurchase agreement, the counterparty defaults. The Adviser may, however, sell any Short-Term Investment (or any fractional portion thereof) on behalf of some or all Participants prior to the maturity of the investment if the cost of such transaction will be borne solely by the selling Participants and the transaction will not adversely affect other Participants. Each Participant in a Joint Account will be deemed to have consented to such sale and partition of the investments in the Joint Account.

13. Short-Term Investments held through a Joint Account with a remaining maturity of more than seven days, as calculated pursuant to rule 2a-7 under the Act, will be considered illiquid ("Illiquid Joint Account Investments"). For any Participant that is an open-end investment company registered under the Act, if an Adviser cannot sell the instrument, or the Participant's fractional interest in such instrument, pursuant to the preceding condition, such Illiquid Joint Account Investments shall be included among those securities which are subject to the restriction that the fund may not invest more than 15% (or such other percentage as set forth by the SEC from time to time) of its net assets in illiquid securities.

For the SEC, by the Division of Investment Management, under delegated authority.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 96-21055 Filed 8-16-96; 8:45 am]

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[Release No. 34-37548; File No. SR-GSCC-96-05]

**Self-Regulatory Organizations;
Government Securities Clearing
Corporation; Notice of Filing of
Proposed Rule Change Relating to
Clearing Fund Collateral and Loss
Allocation Provisions**

August 9, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on May 28, 1996, the Government

¹ 15 U.S.C. 78s(b)(1) (1988).

Securities Clearing Corporation ("GSCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which items have been prepared primarily by GSCC. GSCC amended this filing on July 25, 1996.² The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

GSCC proposes to modify its rules and related information to expand the types of securities that are deemed eligible for clearing fund collateral and to redefine the concept of current trading activity for loss allocation purposes.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, GSCC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. GSCC has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.³

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Clearing Fund Collateral

GSCC proposes to expand the types of securities that are deemed eligible for clearing fund collateral to include all eligible netting securities. The purpose of the clearing fund is (i) to have on deposit from each netting member assets sufficient to satisfy any losses that might be incurred by GSCC or its members as the result of default by a member and the resultant close out of that member's settlement positions; (ii) to maintain a total asset amount sufficient to satisfy potential losses to GSCC and its members resulting from the failure of more than one member; and (iii) to ensure that GSCC has sufficient liquidity at all times to meet its payment and delivery obligations.

² Letter from Karen Walraven, Vice President and Associate Counsel, GSCC, to Jerry W. Carpenter, Assistant Director, Division of Market Regulation, Commission (July 22, 1996).

³ The Commission has modified the text of the summaries prepared by GSCC.

GSCC Rule 4 requires each netting member to make and to maintain a deposit to the clearing fund, and Section 4 thereof prescribes the form that a netting member's clearing fund deposit must take. Currently, there are three types of eligible clearing fund collateral: cash, eligible Treasury securities, and eligible letters of credit. An eligible Treasury security is defined as an unmatured, marketable debt security in book-entry form that is a direct obligation of the U.S. government. In practice, GSCC accepts only treasury bills, notes, and bonds as collateral.⁴ Conversely, GSCC currently processes a broad range of securities (*i.e.*, eligible netting securities) through the netting system. GSCC proposes to expand the types of securities that will be deemed acceptable forms of clearing fund collateral⁵ to include all securities that are eligible for the netting system (*e.g.*, any non-mortgage-backed security, including zero-coupon securities, issued or guaranteed by the U.S., a U.S. government agency or instrumentality, or a U.S. government-sponsored corporation). GSCC believes that the risks associated with this broader range of government securities are minimal and can be managed in an appropriate fashion, as discussed below.

GSCC believes that an expansion of acceptable clearing fund collateral will benefit its members by providing them with more flexibility in meeting their clearing fund obligations and that the expansion will enable GSCC to maximize the liquidity of the clearing fund at risk levels that are not significantly higher than those present under the current definition. The securities in the eligible netting security category are eligible for settlement on a book-entry basis over the Fedwire, are liquid, and are not subject to a high degree of price volatility. Nonetheless, GSCC intends to limit liquidity and price volatility risks by applying an appropriate haircut percentage to each type of security accepted as clearing fund collateral. The haircut will be at least equal to the haircut GSCC takes on eligible Treasury securities,⁶ and in no

⁴ Currently, only coupon bearing Treasury notes and bonds are eligible as clearing fund collateral. See Securities Exchange Act Release No. 33237 (December 1, 1993), 58 FR 63414.

⁵ At this time no change is proposed with respect to the cash and letters of credit eligible for clearing fund deposits.

⁶ Section 4 of GSCC Rule 4 provides that eligible Treasury securities with a remaining maturity of greater than one year and less than ten years are subject to a three percent haircut while securities with a remaining maturity of ten years or greater are subject to a five percent haircut. GSCC does not propose to change these existing haircut provisions at this time.

event will the haircut be lower than that applied to the relevant security by GSCC's liquidity bank.

Furthermore, pursuant to action by its Board of Directors, under the proposed rule change GSCC will retain the right to refuse to accept particular types of collateral for liquidity or other reasons. Such refusal could arise under a variety of circumstances such as GSCC's liquidity bank's reluctance to accept a certain type of security as collateral for an extension of credit.

2. Loss Allocation

Rule 20, Section 4(c) of GSCC's rules provides that upon a member's default GSCC will close out the positions of the defaulting member. If the close out of all the defaulting member's positions results in GSCC incurring a loss, that loss will be allocated pursuant to GSCC Rule 4.

Under Section 8 of Rule 4, GSCC looks first to the defaulting member's clearing fund collateral. If the defaulting member's collateral does not fully cover GSCC's loss, GSCC determines the proportion of the remaining loss that arose in connection with non-brokered (*i.e.*, direct) transactions and the proportion that rose in connection with brokered transactions. Brokered transactions are categorized as either brokered transactions involving only members or brokered transactions involving a nonmember on one side of the trade.

To the extent a remaining loss is determined to arise in connection with direct transactions, the loss is allocated pro rata among netting members other than interdealer brokers based on the dollar value of the trading activity of each such netting member with the defaulting member netted and novated on the day of default. If the loss is determined to arise in connection with member brokered transactions, GSCC allocates ten percent of the loss to the interdealer broker netting members on an equal basis regardless of the level of trading activity of each such broker with the defaulting member. The remainder of the loss is divided pro rata among all other netting members based upon the dollar value of each netting member's trading activity through interdealer brokers with the defaulting member netted and novated on the day of default. If the loss is determined to arise in connection with nonmember brokered transactions, GSCC allocates ten percent of the loss to the interdealer broker netting members on an equal basis regardless of the level of trading activity of each such broker with the defaulting member. The remainder of the loss is allocated pro rata among the

Category 2 interdealer broker netting members that were parties to such nonmember brokered transactions based upon the dollar value of each such broker member's trading activity with the defaulting member netted and novated on the day of default.⁷

An important principle in the loss allocation process is the definition of "trading activity with the defaulting member netted and novated on the day of default."⁸ GSCC's rules define this as trading activity with a defaulting member submitted by a netting member that was compared, entered the net, and was novated on the business day on which the failure of the defaulting member to fulfill its obligations to GSCC occurred. However, if the aggregate level of such trading activity is less than the dollar value amount of the defaulting member's securities liquidated pursuant to GSCC's close out procedure, the term will encompass trading activity going back as many days as is necessary to reach a level of activity that is equal to or greater than the dollar value amount of such liquidated securities.

GSCC proposes to modify its loss allocation procedures by redefining the concept of "trading activity with the defaulting member netted and novated on the day of default" to capture a level of trading activity that is at least five times the dollar value amount of the securities of the defaulting member that are liquidated. The five-fold multiple is based on the approximate netting factor of eighty percent. Historically, the aggregate transactions processed through GSCC's netting system net down to approximately twenty percent of the aggregate transactional volume (*i.e.*, for approximately every five transactions that enter the netting process, only one needs to be settled through the movement of securities and cash).

GSCC's current approach to loss allocation focuses on the date on which a transaction is netted and novated by GSCC and this will continue to be the case. However, with the advent of netting of repurchase agreements ("repos") and the resultant increase in the number of relatively longterm transactions introduced into the netting process, GSCC has reevaluated its loss allocation process with a view toward better taking into account the duration of netted transactions.

⁷ Category 1 interdealer brokers act exclusively as brokers and trade only with netting members and with certain grandfathered nonmember firms. Category 2 interdealer brokers are permitted to have up to ten percent of their business with nonnetting members other than grandfathered nonmembers.

⁸ GSCC Rule 4, Section 8(a)(v).

The proposed approach does not take into account the duration of the trade (*i.e.*, the time between trade date and settlement date). Rather, GSCC seeks a balance between assessing transactions based purely on when they were entered into versus taking into account their duration by expanding the amount of trading that will be encompassed for loss allocation purposes. GSCC believes this will have the effect of establishing a greater incentive for members to assess the creditworthiness of counterparties.

GSCC believes the proposed rule change is consistent with its obligations under Section 17A of the Act⁹ because by broadening the range of securities acceptable as clearing fund collateral and by modifying the loss allocation procedures to encompass more trades, GSCC will facilitate member transactions and will cause members to assess the creditworthiness of their counterparties based on duration of transactions. This should promote the prompt and accurate clearance and settlement of securities transactions.

B. Self-Regulatory Organization's Statement on Burden on Competition

GSCC does not believe that the proposed rule change will have an impact or impose a burden on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Comments on the proposed rule change have not yet been solicited or received. Members will be notified of the rule filing, and comments will be solicited by an important notice. GSCC will notify the Commission of any written comments received by GSCC.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within thirty-five days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

⁹ 15 U.S.C. 78q-1 (1988).

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. § 552, will be available for inspection and copying in the Commission's Public Reference Section, 450 Fifth Street N.W., Washington, D.C. 20549. Copies of such filing will also be available for inspection and copying at the principal office of GSCC. All submissions should refer to File No. SR-GSCC-96-05 and should be submitted by September 9, 1996.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Margaret H. McFarland,
Deputy Secretary.

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[Release No. 34-37549; File No. SR-NSCC-96-13]

Self Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Proposed Rule Change Relating to the Guarantee of When-Issued and Balance Order Trades

August 9, 1996.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ notice is hereby given that on June 21, 1996, the National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which items have been prepared primarily by NSCC. On August 1, 1996, NSCC amended the proposed rule change.² The Commission is publishing this notice to solicit

¹⁰ 17 CFR 200.30-3(a)(12) (1995).

¹ 15 U.S.C. 78s(b)(1) (1988).

² Letter from Julie Beyers, Associate Counsel, NSCC, to Jerry Carpenter, Assistant Director, Division of Market Regulation, Commission (August 1, 1996).