For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.20

Kevin M. O’Neill,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION


Self-Regulatory Organizations;
National Securities Clearing Corporation; Notice of Filing Amendment No. 3 to a Proposed Rule Change, as Previously Modified by Amendment Nos. 1 and 2, To Institute Supplemental Liquidity Deposits To Its Clearing Fund Designed To Increase Liquidity Resources To Meet Its Liquidity Needs

October 15, 2013.

On March 21, 2013, National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR–NSCC–2013–02 (“Proposed Rule Change”) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”).1 and Rule 19b–4 thereunder.2 The Proposed Rule Change was published for comment in the Federal Register on April 10, 2013.3 On April 19, 2013, NSCC filed with the Commission Amendment No. 1 to the Proposed Rule Change, which the Commission published for comment in the Federal Register on May 29, 2013 and designated a longer period for Commission action on the Proposed Rule Change, as amended.4 On June 11, 2013, NSCC filed with the Commission Amendment No. 2 to the Proposed Rule Change, as previously modified by Amendment No. 1, which the Commission published for comment in the Federal Register on July 15, 2013, with an order instituting proceedings to determine whether to approve or disapprove the Proposed Rule Change (“Order Instituting Proceedings”).5 On September 25, 2013, the Commission designated a longer period of review for Commission action on the Order Instituting Proceedings.6 As of October 15, 2013, the Commission had received 22 comment letters on the proposal contained in the Proposed Rule Change and its related Advance Notice,7 including NSCC’s two responses to the comment letters received as of August 20, 2013.8 Pursuant to Section 19(b)(1) of the Exchange Act9 and Rule 19b–4 thereunder,10 notice is hereby given that on October 7, 2013, NSCC filed with the Commission Amendment No. 3 to the Proposed Rule Change, as previously modified by Amendment Nos. 1 and 2, as described in Items I and II below, which Items have been prepared primarily by NSCC. The Commission is publishing this notice to solicit comments on the Proposed Rule Change, as modified by Amendment No. 3, from interested persons.11

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

The Proposed Rule Change, as modified by Amendments No. 1, No. 2, and No. 3, is a proposal by NSCC to amend its Rules & Procedures (the “NSCC Rules”) to provide for supplemental liquidity deposits to its Clearing Fund (the “NSCC Clearing Fund”) to ensure that NSCC has adequate liquidity resources to meet its liquidity needs (the “SLD Proposal” or sometimes the “Proposal”), as described below. NSCC filed Amendment No. 3 (this “Amendment”) to the Proposed Rule Change, as previously modified by Amendment No. 1 and No. 2, in order to delete the provisions in the proposed rule relating to Regular Activity Liquidity Obligations (as defined), to respond to concerns raised by Members. As a result the Proposal, as revised, would impose supplemental liquidity obligations on affected Members only with respect to activity relating to monthly options expiry periods (defined in the proposed Rule as “Special Activity Liquidity Obligations”).

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, NSCC included statements concerning the purpose of and basis for the Proposed Rule Change, as modified by Amendment No. 3, 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. NSCC has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

(A) Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Description of Change

Existing Proposal

As noted in the original proposal contained in the Proposed Rule Change, as modified by Amendments No. 1 and No. 2 (the “Rule Filing”), the SLD Proposal would modify the NSCC Rules to add a new Rule 4(A), to establish a supplemental liquidity funding obligation designed to cover the liquidity exposure attributable to those Members and families of affiliated Members (“Affiliated Families”) that regularly incur the largest gross settlement debits over a settlement cycle during both times of normal trading activity (“Regular Activity Periods”) and times of increased trading and settlement activity that arise around monthly options expiry dates (“Options Expiration Activity Periods”). Under the existing proposal, the Liquidity Obligation of a Member or Affiliated Family with respect to a
Regular Activity Period (a “Regular Activity Liquidity Obligation”) or an Options Expiration Activity Period (a “Special Activity Liquidity Obligation”) would be imposed on the 30 Members or Affiliated Families who generate the largest aggregate liquidity needs over a settlement cycle that would apply in the event of a closeout (that is, over a period from date of default through the following three settlement days), based upon an historical look-back period. The calculations for both the Regular Activity Liquidity Obligation and the Special Activity Liquidity Obligation were designed so that NSCC has adequate liquidity resources to enable it to settle transactions, notwithstanding the default of one of these 30 largest Members or Affiliated Families during Regular Activity Periods, as well as during Options Expiration Activity Periods. The liquidity obligations imposed on Members of Affiliated Families would be apportioned among the Members and affiliation status and liquidity needs of those Members. NSCC is proposing to amend the existing Proposal to address any additional liquidity needs in excess of NSCC’s available liquidity resources. The revision of the existing Proposal is anticompetitive or discriminatory because the obligation to provide supplemental liquidity was imposed on only the 30 largest Unaffiliated Members or Affiliated Families (even though those Members collectively represent approximately 85% of NSCC’s total membership by peak liquidity needs), rather than all Members of NSCC. This concern was raised in the context of Regular Activity Supplemental Deposits.

The proposed Rule, as so revised, would amend the existing Proposal by removing those provisions that, collectively, dealt with the imposition of Regular Activity Liquidity Obligations, while maintaining the provisions relating to how commitments under the Credit Facility would be credited against the cash deposit provisions relating to how commitments under the Credit Facility would be credited against the cash deposit.

Third, commenters claimed that the existing Proposal was anticompetitive or discriminatory because of its provisions relating to how commitments under the Credit Facility would be credited against the cash deposit.

In addition, under the revised SLD Proposal, as under the existing Proposal as it relates to Special Activity Liquidity Obligations, Unaffiliated Members and Affiliated Families, will be able to manage their exposures by making Special Activities Prefund Deposits where they project their own activity will increase their liquidity exposure. For example, if a Special Activity Liquidity Provider anticipates that its Special Activity Peak Liquidity Exposure at any time during a particular Options Expiration Activity Period will be greater than the amount calculated by NSCC, it can make an additional cash deposit to the Clearing Fund in (in excess of its Required Deposit) that it designates as a “Special Activity Prefund Deposit.” However, to the extent that a Member fails to adequately prefund its activity, it may be subject to a Special Activity Liquidity Call in the same manner as provided in the existing Proposal.

Objections From Commenters

The key concerns raised by commenters with respect to the existing SLD Proposal were as follows:

First, commenters claimed that Members were not sufficiently consulted or involved during the development of the Proposal (even though NSCC management conducted significant Member outreach), so that the Proposal lacked input that could have potentially resulted in a less burdensome approach.

Second, commenters claimed that the Proposal was anticompetitive or discriminatory because the obligation to provide supplemental liquidity was imposed on only the 30 largest Unaffiliated Members or Affiliated Families (even though those Members collectively represent approximately 85% of NSCC’s total membership by peak liquidity needs), rather than all Members of NSCC. This concern was raised in the context of Regular Activity Supplemental Deposits.

The proposed Rule, as so revised, would amend the existing Proposal by removing those provisions that, collectively, dealt with the imposition of Regular Activity Liquidity Obligations, while maintaining the provisions relating to how commitments under the Credit Facility would be credited against the cash deposit.

In addition, under the revised SLD Proposal, as under the existing Proposal as it relates to Special Activity Liquidity Obligations, Unaffiliated Members and Affiliated Families, will be able to manage their exposures by making Special Activities Prefund Deposits where they project their own activity will increase their liquidity exposure. For example, if a Special Activity Liquidity Provider anticipates that its Special Activity Peak Liquidity Exposure at any time during a particular Options Expiration Activity Period will be greater than the amount calculated by NSCC, it can make an additional cash deposit to the Clearing Fund in (in excess of its Required Deposit) that it designates as a “Special Activity Prefund Deposit.” However, to the extent that a Member fails to adequately prefund its activity, it may be subject to a Special Activity Liquidity Call in the same manner as provided in the existing Proposal.

With these changes, NSCC is removing those provisions of the existing SLD Proposal that generated most concern from commenters, while retaining those provisions that enable NSCC to collect additional liquidity resources to cover the heightened liquidity needs that arise during monthly Options Expiration Activity Periods. Every Unaffiliated Member and Affiliated Family among the top 30 whose activity causes a liquidity need in excess of NSCC’s available liquidity resources will contribute ratably to such shortfall, so the Proposal fairly and equitably apportions the obligation among those Unaffiliated Members and Affiliated Families whose activity cause the need. The removal of those provisions relating to how commitments under the Credit Facility would be credited against the cash deposit obligations of Regular Activity Liquidity Providers render concerns about such allocation moot.

As indicated in NSCC’s August 20, 2013 letter to the Commission, DTCC is separately establishing a standing member-based advisory group, the Clearing Agency Liquidity Council (“CALC”), as a forum for the discussion of liquidity and liquidity-related financing needs and trends. The CALC will initially focus on liquidity initiatives currently being considered by NSCC to address liquidity funding during periods of normal activity, including issues raised by commenters in the existing SLD Proposal. In response to commenters’ more general concerns regarding NSCC’s reliance on
the Credit Facility and related refinancing risk. NSCC will review with the CALC the financing options available to NSCC to supplement the Clearing Fund as a liquidity resource, and the related costs of those options. Any new initiatives proposed as a result of the CALC review that require regulatory approval will be addressed in a separate filing.

Reporting. As noted in the previous amendment to the Rule Filing, NSCC agrees that Members have to be able to plan for their liquidity obligations. At the same time, NSCC also believes it is critical that Members understand the risks that their own activity presents to NSCC, and be prepared to monitor their activity and alter their behavior if they want to minimize the liquidity risk they present to NSCC. Accordingly, NSCC will make available to each Member a daily report showing the amount of liquidity NSCC would need in the event of the default of such Member. Separately, NSCC will provide, and continue to discuss with Special Activity Liquidity Providers, the reports regarding their Special Activity Liquidity Obligations as currently provided in the proposed Rule.

Implementation Timeframe. The SLD Proposal will be implemented on February 1, 2014. As a result, the first time that Members will be obligated to fund any Special Activity Supplemental Deposits will be for the Options Expiration Activity Period in February 2014. NSCC Risk staff will provide to affected Members their Special Activity Peak Liquidity Calls must be satisfied.

Finally, the amendment makes certain technical corrections and clarifies the time period for when Special Activity Liquidity Calls must be satisfied.

II. Solicitation of Comments

Written comments on the Proposed Rule Change, including NSCC’s formal response to the written comments, have been filed with the Commission and are available on the Commission’s Web site.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the Proposed Rule Change, as modified by Amendment No. 3, is consistent with the Section 17A(b)(5) and any other provision of the Exchange Act, or the rules and regulations thereunder. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission’s Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an email to rule-comments@sec.gov. Please include File No. SR–NSCC–2013–02 and should be submitted on or before November 5, 2013.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.

Kevin M. O’Neill,
Deputy Secretary.
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