

post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSE-2017-15 and should be submitted on or before May 4, 2017.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>12</sup>

**Eduardo A. Aleman,**  
Assistant Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-80396; File No. SR-NSCC-2017-801]

### Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Advance Notice To Enhance the Credit Risk Rating Matrix and Make Other Changes

April 7, 2017.

Pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act entitled the Payment, Clearing, and Settlement Supervision Act of 2010 ("Clearing Supervision Act")<sup>1</sup> and Rule 19b-4(n)(1)(i) under the Securities Exchange Act of 1934 ("Act"),<sup>2</sup> notice is hereby given that on March 22, 2017, National Securities Clearing Corporation ("NSCC") filed with the Securities and

Exchange Commission ("Commission") the advance notice SR-NSCC-2017-801 ("Advance Notice") as described in Items I, II and III below, which Items have been prepared by NSCC.<sup>3</sup> The Commission is publishing this notice to solicit comments on the Advance Notice from interested persons.

#### I. Clearing Agency's Statement of the Terms of Substance of the Advance Notice

This Advance Notice consists of proposed modifications to NSCC's Rules and Procedures ("Rules").<sup>4</sup> The proposed rule change would amend the Rules in order to (i) enhance the matrix (hereinafter referred to as the "Credit Risk Rating Matrix" or "CRRM")<sup>5</sup> developed by NSCC to evaluate the risks posed by certain Members ("CRRM-Rated Members") to NSCC and its Members from providing services to these CRRM-Rated Members and (ii) make other amendments to the Rules to provide more transparency and clarity regarding NSCC's current ongoing membership monitoring process.

#### II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Advance Notice

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

##### (A) Clearing Agency's Statement on Comments on the Advance Notice Received From Members, Participants, or Others

Written comments relating to this proposal have not been solicited or received. NSCC will notify the Commission of any written comments received by NSCC.

<sup>3</sup> On March 22, 2017, NSCC filed this Advance Notice as a proposed rule change (SR-NSCC-2017-002) with the Commission pursuant to Section 19(b)(1) of the Act, 15 U.S.C. 78s(b)(1), and Rule 19b-4, 17 CFR 240.19b-4. A copy of the proposed rule change is available at <http://www.dtcc.com/legal/sec-rule-filings.aspx>.

<sup>4</sup> Capitalized terms not defined herein are defined in the Rules, available at [http://www.dtcc.com/-/media/Files/Downloads/legal/rules/nsccl\\_rules.pdf](http://www.dtcc.com/-/media/Files/Downloads/legal/rules/nsccl_rules.pdf).

<sup>5</sup> The proposed rule changes with respect to the enhancement of the CRRM are reflected in the inclusion of (i) qualitative factors and examples thereof in the proposed new definition for "Credit Risk Rating Matrix" in Rule 1 and (ii) Members that are foreign banks or trust companies that have audited financial data that is publicly available in Section 4(b)(i) of Rule 2B.

##### (B) Advance Notice Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

###### Nature of the Proposed Change

The proposed rule change would, among other things, enhance the CRRM to enable it to rate Members that are foreign banks or trust companies and have audited financial data that is publicly available. It would also enhance the CRRM by allowing it to take into account qualitative factors when generating credit ratings for Members. In addition, it would enhance the CRRM by shifting it from a relative scoring approach to an absolute scoring approach.

This rule filing also contains proposed rule changes that are not related to the proposed CRRM enhancements but that provide specificity, clarity and additional transparency to the Rules related to NSCC's current ongoing membership monitoring process.

###### (i) Background

NSCC occupies an important role in the securities settlement system by interposing itself as a central counterparty between Members that are counterparties to transactions accepted for clearing by NSCC, thereby reducing the risk faced by Members. NSCC uses the CRRM, the Watch List (as defined below) and the enhanced surveillance to manage and monitor default risks of Members on an ongoing basis, as discussed below. The level and frequency of such monitoring for a Member is determined by the Member's risk of default as assessed by NSCC. Members that are deemed by NSCC to pose a heightened risk to NSCC and its Members are subject to closer and more frequent monitoring.

###### Existing Credit Risk Rating Matrix

In 2005, the Commission approved a proposed rule change filed by NSCC ("Initial Filing")<sup>6</sup> to establish new criteria for placing certain Members on a list for closer monitoring ("Watch List").

NSCC proposed in the Initial Filing that all U.S. broker-dealers and U.S. banks that were Members would be assigned a rating generated by entering financial data of those Members into an internal risk assessment matrix, *i.e.*, the CRRM. However, the text of the current Rule 2B, Section 4, does not specify which Members are CRRM-Rated Members and whether non-CRRM-Rated

<sup>6</sup> See Securities Exchange Act Release No. 51362 (March 11, 2005), 70 FR 13562 (March 21, 2005) (SR-NSCC-2003-11).

<sup>12</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 12 U.S.C. 5465(e)(1).

<sup>2</sup> 17 CFR 240.19b-4(n)(1)(i).

Members may be included on the Watch List.

Currently, Members that are U.S. broker-dealers and U.S. banks are assessed against the CRRM and assigned a credit rating based on certain quantitative factors.<sup>7</sup> Unfavorably-rated Members are placed on the Watch List. In addition, NSCC credit risk staff may downgrade a particular Member's credit rating based on various qualitative factors. An example of such qualitative factors might be that the Member in question received a qualified audit opinion on its annual audit. NSCC believes that, in order to protect NSCC and its other Members, it is important that credit risk staff maintain the discretion to downgrade a Member's credit rating on the CRRM and thus subject the Member to closer monitoring.

The current CRRM is comprised of two credit rating models—one for the U.S. broker-dealers and one for the U.S. banks—and generates credit ratings for the relevant Members based on a 7-point rating system, with “1” being the strongest credit rating and “7” being the weakest credit rating.

Over time, the current CRRM has not kept pace with NSCC's evolving membership base and heightened expectations from regulators and stakeholders for robustness of financial models. Specifically, the current CRRM only generates credit ratings for those Members that are U.S. banks or U.S. broker-dealers that file standard reports with their regulators. Although these types of Members currently represent the vast majority (approximately 95%) of Members at NSCC,<sup>8</sup> foreign banks and trust companies are expected to be a growing category of NSCC's membership base in the future, and the proposed enhancements to the CRRM would enable it to assign credit ratings to these entities. Foreign banks and trust companies are typically large global financial institutions that have complex businesses and conduct a high volume of activities. Although foreign banks and trust companies are not currently rated by the CRRM, they are monitored by NSCC's credit risk staff using financial criteria deemed relevant by NSCC and can be placed on the Watch List if they experience a financial change that presents risk to NSCC. Given the

potential increase in the number of Members that are foreign banks or trust companies in the coming years, there is a need to formalize NSCC's credit risk evaluation process of these Members by assigning credit ratings to them in order to better facilitate the comparability of credit risks among Members.<sup>9</sup>

In addition, the current CRRM assigns each Member that is a U.S. bank or U.S. broker-dealer and that files standard reports with its regulator(s) a credit rating based on inputting certain quantitative data relative to the applicable Member into the CRRM. Accordingly, a Member's credit rating is currently based solely upon quantitative factors. It is only after the CRRM has generated a credit rating with respect to a particular Member that such Member's credit rating may be downgraded manually by credit risk staff, after taking into consideration relevant qualitative factors. The inability of the current CRRM to take into account qualitative factors requires frequent and manual overrides by credit risk staff, which may result in inconsistent and/or incomplete credit ratings for Members.

Furthermore, the current CRRM uses a relative scoring approach and relies on peer grouping of Members to calculate the credit rating of a Member. This approach is not ideal because a Member's credit rating can be affected by changes in its peer group even if the Member's financial condition is unchanged.

#### Proposed Credit Risk Rating Matrix Enhancements

To improve the coverage and the effectiveness of the current CRRM, NSCC is proposing three enhancements. The first proposed enhancement would expand the scope of CRRM coverage by enabling the CRRM to generate credit ratings for Members that are foreign banks or trust companies and that have audited financial data that is publicly available. The second proposed enhancement would incorporate qualitative factors into the CRRM and therefore is expected to reduce the need and the frequency of manual overrides of Member credit ratings. The third enhancement would replace the relative scoring approach currently used by CRRM with a statistical approach to

estimate the absolute probability of default of each Member.

#### A. Enable the CRRM to Generate Credit Ratings for Foreign Bank or Trust Company Members

The current CRRM is comprised of two credit rating models—one for the U.S. broker-dealers and one for the U.S. banks. NSCC is proposing to enhance the CRRM by adding an additional credit rating model for the foreign banks and trust companies. The additional model would expand the membership classes to which the CRRM would apply to include Members that are foreign banks or trust companies and that have audited financial data that is publicly available. The CRRM credit rating of a Member that is a foreign bank or trust company would be based on quantitative factors, including size, capital, leverage, liquidity, profitability and growth, and qualitative factors, including market position and sustainability, information reporting and compliance, management quality, capital management and business/product diversity. By enabling the CRRM to generate credit ratings for these Members, the enhanced CRRM would provide more comprehensive credit risk coverage of NSCC's membership base.

With the proposed enhancement to the CRRM as described above, applicable foreign bank or trust company Members would be included in the CRRM process and be evaluated more effectively and efficiently because financial data with respect to these foreign bank or trust company Members could be extracted from data sources in an automated form.<sup>10</sup>

After the proposed enhancement, CRRM would be able to generate credit ratings on an ongoing basis for all Members that are U.S. banks, U.S. brokers-dealers and foreign banks and trust companies, which together represent approximately 96% of the NSCC Members.<sup>11</sup>

#### B. Incorporate Qualitative Factors Into the CRRM

In addition, as proposed, the enhanced CRRM would blend qualitative factors with quantitative factors to produce a credit rating for each applicable Member in relation to

<sup>7</sup> Quantitative factors considered by NSCC include (a) for broker dealers, size (*i.e.*, total excess net capital), capital, leverage, liquidity, and profitability and (b) for banks, size, capital, asset quality, earnings, and liquidity.

<sup>8</sup> As of March 16, 2017, there are 155 Members. Of the 155 Members, 11 (or 7%) are U.S. banks, 136 (or 88%) are U.S. broker-dealers and one (or 1%) is a foreign bank or trust company.

<sup>9</sup> CRRM is applied across NSCC and its affiliated clearing agencies, Fixed Income Clearing Corporation (“FICC”) and The Depository Trust Company (“DTC”). Specifically, in order to run the CRRM, credit risk staff uses the financial data of the applicable NSCC Members in addition to data of applicable members and participants of FICC and DTC, respectively. In this way, each applicable NSCC Member is rated against other applicable members and participants of FICC and DTC, respectively.

<sup>10</sup> Currently, these Members are monitored by NSCC credit risk staff that review similar criteria as those reviewed for CRRM-Rated Members, but such review occurs outside of the CRRM process.

<sup>11</sup> As of March 16, 2017, there are 7 Members that would not be rated by the enhanced CRRM, as proposed, because they are central securities depositories, securities exchanges and U.S. trust companies that do not file Call Reports (as defined below).

the Member's credit risk. For U.S. and foreign banks and trust companies, the enhanced CRRM would use a 70/30 weighted split between quantitative and qualitative factors to generate credit ratings. For U.S. broker-dealers, the weight split between quantitative and qualitative factors would be 60/40. These weight splits are chosen by NSCC based on the industry best practice as well as research and sensitivity analysis conducted by NSCC. NSCC would review and adjust the weight splits as well as the quantitative and qualitative factors, as needed, based on recalibration of the CRRM to be conducted by NSCC approximately every three to five years.

Although there are advantages to measuring credit risk quantitatively, quantitative evaluation models alone are incapable of fully capturing all credit risks. Certain qualitative factors may indicate that a Member is or will soon be undergoing financial distress, which may in turn signal a higher default exposure to NSCC and its other Members. As such, a key enhancement being proposed to the CRRM is the incorporation of relevant qualitative factors into each of the three credit rating models mentioned above. By including qualitative factors in the three credit rating models, the enhanced CRRM would capture risks that would otherwise not be accounted for with quantitative factors alone.<sup>12</sup> Adding qualitative factors to the CRRM would not only enable it to generate more consistent and comprehensive credit ratings for applicable Members, but it would also help reduce the need and frequency of manual credit rating overrides by the credit risk staff because overrides would likely only be required under more limited circumstances.<sup>13</sup>

### C. Shifting From Relative Scoring to Absolute Scoring

As proposed, the enhanced CRRM would use an absolute scoring approach and rank each Member based on its

<sup>12</sup> The initial set of qualitative factors that would be incorporated into the CRRM includes (a) for U.S. broker dealers, market position and sustainability, management quality, capital management, liquidity management, geographic diversification, business/product diversity and access to funding, (b) for U.S. banks, environment, compliance/litigation, management quality, liquidity management and parental demands and (c) for foreign banks and trust companies, market position and sustainability, information reporting and compliance, management quality, capital management and business/product diversity.

<sup>13</sup> Once a Member is assigned a credit rating, if circumstances warrant, credit risk staff would still have the ability to override the CRRM-issued credit rating by manually downgrading such rating as they do today. To ensure a conservative approach, the CRRM-issued credit ratings cannot be manually upgraded.

individual probability of default rather than the relative scoring approach that is currently in use. This proposed change is designed to have a Member's CRRM-generated credit rating reflect an absolute measure of the Member's default risk and eliminate any potential distortion of a Member's credit rating from the Member's peer group that may occur under the relative scoring approach used in the existing CRRM.

### D. Watch List and Enhanced Surveillance

In addition to the Watch List, NSCC also maintains an enhanced surveillance list (referenced herein and in the proposed rule text as "enhanced surveillance") for membership monitoring. The enhanced surveillance list is generally used when Members are undergoing drastic and unexpected changes in their financial conditions or operation capabilities and thus are deemed by NSCC to be of the highest risk level and/or warrant additional scrutiny due to NSCC's ongoing concerns about these Members. Accordingly, Members that are subject to enhanced surveillance are reported to NSCC's management committees and are also regularly reviewed by a cross-functional team comprised of senior management of NSCC. More often than not, Members that are subject to enhanced surveillance are also on the Watch List. The group of Members that is subject to enhanced surveillance is generally much smaller than the group on the Watch List. The enhanced surveillance list is an internal tool for NSCC that triggers increased monitoring of a Member above the monitoring that occurs when a Member is on the Watch List.

A Member could be placed on the Watch List either based on its credit rating of 5, 6 or 7, which can either be generated by the CRRM or from a manual downgrade, or when NSCC deems such placement as necessary to protect NSCC and its Members. In contrast, a Member would be subject to enhanced surveillance only when close monitoring of the Member is deemed necessary to protect NSCC and its Members.

The Watch List and enhanced surveillance tools are not mutually exclusive; they may complement each other under certain circumstances. A key distinction between the Watch List and enhanced surveillance is that being placed on the Watch List may result in Required Deposit<sup>14</sup> related

<sup>14</sup> See Rule 4 (Section 1). The "Required Deposit" is the amount that each Member is required to

consequences under the Rules, whereas enhanced surveillance does not.<sup>15</sup> For example, a Member that is in a precarious situation could be placed on the Watch List and be subject to enhanced surveillance; however, because the Watch List status could increase a Member's Required Deposit, when NSCC has preliminary concerns about a Member, to avoid potential increase to a Member's Required Deposit, NSCC may opt not to place the Member on the Watch List until it is certain that such concerns would not be alleviated in the short-term. Instead, in such a situation, NSCC might first subject the Member to enhanced surveillance in order to closely monitor the Member's situation without affecting the Member's Required Deposit. If the Member's situation improves, then it will no longer be subject to enhanced surveillance. If the situation of the Member worsens, the Member may then be placed on the Watch List as deemed necessary by NSCC.

### (ii) Detailed Description of the Proposed Rule Changes Related to the Proposed CRRM Enhancements

In connection with the proposed enhancements to the CRRM, NSCC proposes to amend the Rules to (1) incorporate qualitative factors into CRRM and (2) add Members that are foreign banks or trust companies to the categories of Members that would be assigned credit ratings by NSCC using the CRRM.

#### A. Proposed Changes to Rule 1 (Definitions and Descriptions)

NSCC is proposing to include qualitative factors, such as management quality, market position/environment, and capital and liquidity risk management in the proposed new definition for "Credit Risk Rating Matrix" in Rule 1 because, as proposed, the enhanced CRRM would blend both qualitative factors and quantitative factors to produce a credit rating for each applicable Member.

#### B. Proposed Changes to Section 4(b)(i) of Rule 2B (Ongoing Membership Requirements and Monitoring)

NSCC is proposing to expand the membership types to which the CRRM would apply to include Members that are foreign banks or trust companies and that have audited financial data that is

deposit in NSCC's Clearing Fund. Rules, *supra* note 4.

<sup>15</sup> NSCC expects to provide additional clarity to Members regarding the Watch List and its impact on Required Deposit in a subsequent proposed rule change to be filed with the Commission in 2017.

publicly available by amending Section 4 of Rule 2B.

The enhanced CRRM would assign credit ratings for each Member that is a foreign bank or trust company based on its publicly available audited financial data. The credit rating would be based on an 18-point scale, which is then mapped to the 7-point rating system currently in use today, with “1” being the strongest credit rating and “7” being the weakest credit rating.

#### (iii) Other Proposed Rule Changes

This rule filing also contains proposed rule changes that are unrelated to the proposed enhancement of the CRRM. These proposed rule changes would provide specificity, clarity and additional transparency to the Rules with respect to NSCC’s current ongoing membership monitoring process, as described below.

#### A. Proposed Changes to Rule 1 (Definitions and Descriptions)

NSCC is proposing to amend Rule 1 to add definitions for the CRRM and the Watch List.

The proposed definition of the CRRM would provide that the term “Credit Risk Rating Matrix” means a matrix of credit ratings of Members as specified in Section 4 of Rule 2B. The definition would state that the CRRM is developed by NSCC to evaluate the credit risk such Members pose to NSCC and its Members and is based on factors determined to be relevant by NSCC from time to time, which factors are designed to collectively reflect the financial and operational condition of a Member. The proposed definition would state that, in addition to the proposed qualitative factors described above, these factors include quantitative factors, such as capital, assets, earnings and liquidity.

The proposed definition of the Watch List would provide that the term “Watch List” means, at any time and from time to time, the list of Members whose credit ratings derived from the CRRM are 5, 6 or 7, as well as Members and Limited Members that, based on NSCC’s consideration of relevant factors, including those set forth in Section 4(d) of Rule 2B (described below), are deemed by NSCC to pose a heightened risk to NSCC and its Members.

#### B. Proposed Changes to Rule 2B (Ongoing Membership Requirements and Monitoring)

##### Section 2B of Rule 2B

NSCC is proposing to amend Section 2B of Rule 2B to state that NSCC may review the financial responsibility and operational capability of each Member

and may otherwise require additional reporting from the Member regarding its financial or operational condition that may (1) include information regarding the businesses and operations of the Member and its risk management practices with respect to NSCC’s services utilized by the Member for another Person and (2) result in the Member being placed on the Watch List and/or being subject to enhanced surveillance as determined by NSCC.

Members are direct participants of NSCC. However, there are firms that rely on the services provided by Members in order to have their activity cleared and settled through NSCC’s facilities (the “indirect participants”). These indirect participants pose certain risks to NSCC that need to be identified and monitored as part of NSCC’s ongoing member due diligence process. In order for NSCC to understand (1) the material dependencies between Members and the indirect participants that rely on the Members for the clearance and settlement of the indirect participants’ transactions, (2) significant Member-indirect participant relationships and (3) the various risk controls and mitigants that these Members employ to manage their risks with respect to such relationships, NSCC may request information from Members regarding the Members’ businesses and operations as well as their risk management practices with respect to services of NSCC utilized by the Members for indirect participants. The information provided by Members would then be taken into consideration by NSCC when determining whether a Member may need to be placed on the Watch List, be subject to enhanced surveillance or both.

##### Section 4 of NSCC Rule 2B

NSCC is proposing to amend Section 4 of Rule 2B in order to (1) specify the membership types that are currently subject to NSCC’s ongoing monitoring and review, (2) clarify which U.S. broker-dealers and U.S. banks will be assigned a credit rating by NSCC in accordance with the CRRM, (3) provide that NSCC may manually downgrade a CRRM-Rated Member’s credit rating in certain instances, (4) provide that NSCC may place non-CRRM-Rated Members and certain Limited Members on the Watch List and/or subject them to enhanced surveillance, if necessary, (5) describe some of the factors that could be taken into consideration by NSCC when downgrading a Member’s or Limited Member’s credit rating, placing a Member or Limited Member on the Watch List and/or subjecting a Member or Limited Member to enhanced

surveillance, (6) allow NSCC to collect additional deposits to the Clearing Fund and to retain deposits in excess of the Required Deposit from Members or Limited Members that are on the Watch List and (7) provide for enhanced monitoring of Members or Limited Members that are on the Watch List and/or are subject to enhanced surveillance.

In connection with the forgoing, NSCC proposes to delete the current first paragraph in Section 4 of NSCC Rule 2B and add the following:

1. Section 4(a), specifying that NSCC currently monitors and reviews all Members and certain Limited Members on an ongoing and periodic basis, which may include monitoring news and market developments relating to these Members and Limited Members and conducting reviews of financial reports and other public information of these Members and Limited Members.

2. Section 4(b)(i), clarifying that (1) Members that are (A) U.S. banks or trust companies that file the Consolidated Report of Condition and Income (“Call Report”) or (B) U.S. broker-dealers that file the Financial and Operational Combined Uniform Single Report (“FOCUS Report”) or the equivalent with their regulators, would be assigned a credit rating by NSCC in accordance with the CRRM and (2) each CRRM-Rated Member’s credit rating would be reassessed upon receipt of additional information from the Member.

3. Section 4(b)(ii), providing that, because the factors used as part of the CRRM may not identify all risks that a Member may pose to NSCC, NSCC may, in addition to other actions permitted by the Rules, downgrade the Member’s credit rating derived from the CRRM if NSCC believes the CRRM-generated rating is insufficiently conservative or if it deems such downgrade as necessary to protect NSCC and its Members. Depending on the credit rating of the Member, a downgrade may result in the Member being placed on the Watch List and/or being subject to enhanced surveillance based on relevant factors.

4. Section 4(c), specifying that, other than CRRM-Rated Members, NSCC may place Members and Limited Members that are monitored and reviewed by NSCC on the Watch List and/or subject them to enhanced surveillance even though they are not being assigned credit ratings by NSCC in accordance with the CRRM.

5. Section 4(d), describing some of the factors that could be taken into consideration by NSCC when downgrading a Member’s credit rating, placing a Member or Limited Member on the Watch List and/or subjecting a

Member or Limited Member to enhanced surveillance. These factors include but are not limited to (i) news reports and/or regulatory observations that raise reasonable concerns relating to the Member or Limited Member, (ii) reasonable concerns around the Member's or Limited Member's liquidity arrangements, (iii) material changes to the Member's or Limited Member's organizational structure, (iv) reasonable concerns of NSCC about the Member's or Limited Member's financial stability due to particular facts and circumstances, such as material litigation or other legal and/or regulatory risks, (v) failure of the Member or Limited Member to demonstrate satisfactory financial condition or operational capability or if NSCC has a reasonable concern regarding the Member's or Limited Member's ability to maintain applicable membership standards and (vi) failure of the Member or Limited Member to provide information required by NSCC to assess risk exposures posed by the Member's or Limited Member's activity.

6. Section 4(e), allowing NSCC to (1) require a Member or Limited Member that has been placed on the Watch List to make and maintain additional deposits to the Clearing Fund and (2) withhold any deposit in excess of the Required Deposit of a Member or Limited Member that has been placed on the Watch List as provided in Section 9 of Rule 4.

7. Section 4(f), providing that NSCC would, in addition to other actions permitted by the Rules, conduct a more thorough monitoring of the financial condition and/or operational capability of, and require more frequent financial disclosures from, not only those Members and Limited Members that are placed on the Watch List but also Members and Limited Members subject to enhanced surveillance, including examples of how the monitoring could be conducted and the types of disclosures that may be required. In addition, Members and Limited Members that are subject to enhanced surveillance would be reported to NSCC's management committees and regularly reviewed by a cross-functional team comprised of senior management of NSCC.

In addition to the proposed changes described above, NSCC is proposing to make technical corrections to the second paragraph of Section 4 of Rule 2B to (1) renumber the paragraph as Section 4(g), (2) update an internal cross reference and (3) clarify that the references in the paragraph to Members under surveillance are referring to Members on the Watch List.

#### C. Proposed Changes to Rule 4 (Clearing Fund)

NSCC is proposing to amend Section 9 of Rule 4 to clarify that NSCC may, in its discretion, withhold all or part of any excess Clearing Fund deposit of Members that are on the Watch List.

#### D. Proposed Changes to Procedure XV (Clearing Fund Formula and Other Matters)

NSCC is proposing to amend Section I(B)(1) of Procedure XV to clarify that Members or Limited Members that are placed on the Watch List would be required to make additional Clearing Fund deposits, as determined by NSCC.

In addition, NSCC is proposing to make the following technical corrections to Section I(B)(1) of Procedure XV, (i) renumber the final three paragraphs as Section I(B)(2) and title the new subsection "Family Issued Securities" to reflect the different subject matter of the new subsection, (ii) capitalize references to the Credit Risk Rating Matrix to reflect the proposed addition of the defined term to Rule 1 and (iii) make other grammatical corrections to the new Section I(B)(2).

Finally, NSCC is proposing to amend Section II(C) of Procedure XV to clarify that, although NSCC would not request additional Clearing Fund deposits from Members unless they exceed a predetermined threshold, such floor would not apply to Members or Limited Members that are on the Watch List.

#### E. Additional Proposed Changes to Rule 1 (Definitions and Descriptions) and Procedure XV (Clearing Fund Formula and Other Matters)

NSCC is proposing to amend the definition of "Illiquid Position" in Rule 1 as well as Procedure XV Sections I(A)(1) and I(A)(2), each as proposed in connection with a separate proposed rule change filed with the Commission but not yet approved.<sup>16</sup> Specifically, the proposed amendments would replace and conform references to "credit risk matrix" with "Credit Risk Rating Matrix" in the proposed definition of "Illiquid Position" in Rule 1 as well as Procedure XV Sections I(A)(1) and I(A)(2).

#### Implementation Timeframe

Pending Commission approval, NSCC expects to implement this proposal promptly. Members would be advised of the implementation date of this proposal through issuance of a NSCC Important Notice.

#### Expected Effect on Risks to the Clearing Agency, Its Participants and the Market

The proposed rule changes would mitigate counterparty credit risk for NSCC by allowing NSCC to more accurately monitor the creditworthiness and risk profile of its Members. The enhanced CRRM would provide a more robust credit rating methodology by incorporating qualitative factors and adopting an absolute scoring approach. Both of these enhancements would improve NSCC's ability to monitor the credit risk of its Members and are expected to lessen the frequency of manual overrides. The enhanced CRRM would also expand the coverage of NSCC's membership by providing credit ratings for Members that are foreign banks or trust companies, which are not covered under the existing CRRM.

By mitigating counterparty credit risk for NSCC as described above, the enhanced CRRM would also mitigate risk for Members because lowering the risk profile for NSCC would in turn lower the risk exposure that Members may have with respect to NSCC in its role as a central counterparty.

#### Management of Identified Risks

The proposed rule changes are designed to mitigate counterparty credit risk for NSCC and to provide greater clarity and transparency to Members regarding the counterparty credit risk management approach used by NSCC.

The enhanced CRRM would improve NSCC's ability to monitor the probability of default for Members that are rated by the CRRM and is expected to lessen the need and the frequency of manual downgrades due to the anticipated improvement in the accuracy of the credit ratings generated by the enhanced CRRM.

NSCC employs a risk-based approach to conducting monitoring and review of its Members by using the CRRM to identify higher risk Members. Once identified, NSCC would place these Members on the Watch List, which would result in more frequent review by NSCC of these Members than the other Members. For Members that are placed on the Watch List, NSCC would conduct more thorough monitoring of these Members' financial condition and/or operational capability, which could include, for example, on-site visits or additional due diligence information requests.

Members that have been placed on the Watch List may also be required to maintain a higher deposit to the Clearing Fund, which would help offset potential risks to NSCC and its Members arising from activity submitted by these Members.

<sup>16</sup> See Securities Exchange Act Release No. 80260 (March 16, 2017), 82 FR 14781 (March 22, 2017) (SR-NSCC-2017-001).

The enhanced CRRM would also expand the coverage of NSCC's membership by providing credit ratings for foreign banks and trust companies, which are not currently rated under the existing CRRM. The addition of these entities would allow NSCC to employ its risk-based approach to identify those higher risk Members for additional monitoring with more efficiency (by reducing the need for manual overrides) and effectiveness (by generating a more comprehensive and accurate credit rating after taking into account both quantitative and qualitative factors and adopting the absolute scoring approach).

Thus, the enhanced CRRM would help NSCC to identify those Members that could present credit risk to NSCC, which then would allow NSCC to better manage the potential risks from these Members.

#### Consistency With the Clearing Supervision Act

The proposed enhancements to the CRRM as described in detail above would be consistent with Section 805(b) of Clearing Supervision Act.<sup>17</sup> The objectives and principles of Section 805(b) of the Clearing Supervision Act include, among other things, the promotion of robust risk management.<sup>18</sup>

By enhancing the CRRM to enable it to assign credit ratings to Members that are foreign banks or trust companies and that have audited financial data that is publicly available, the proposed rule change would expand the CRRM's applicability to a wider group of Members, which would improve NSCC's membership monitoring process and promote robust risk management, consistent with the objectives and principles of Section 805(b) of the Clearing Supervision Act cited above.

Similarly, by enhancing the CRRM to enable it to incorporate qualitative factors when assigning a Member's credit rating, the proposed change would enable NSCC to take into account relevant qualitative factors in an automated and more effective manner when monitoring the credit risks presented by the Members, which would improve NSCC's membership monitoring process overall and promote robust risk management, consistent with the objectives and principles of Section 805(b) of the Clearing Supervision Act cited above.

Likewise, by enhancing the CRRM to shift from a relative scoring approach to an absolute scoring approach when assigning a Member's credit rating, the proposed rule change would enable

NSCC to generate credit ratings for Members that are more reflective of the Members' default risk, which would improve NSCC's membership monitoring process and promote robust risk management, consistent with the objectives and principles of Section 805(b) of the Clearing Supervision Act cited above.

The proposed enhancements to the CRRM are consistent with Rule 17Ad-22(e)(3)(i) under the Act, which was recently adopted by the Commission.<sup>19</sup> Rule 17Ad-22(e)(3)(i) will require NSCC to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing risks that arise in or are born by NSCC, which includes \* \* \* systems designed to identify, measure, monitor and manage the range of risks that arise in or are borne by NSCC.<sup>20</sup> The proposed enhancements to the CRRM have been designed to assist NSCC in identifying, measuring, monitoring and managing the credit risks to NSCC posed by its Members. The proposed enhancements to the CRRM accomplish this by (i) expanding the CRRM's applicability to a wider group of Members to include Members that are foreign banks or trust companies, (ii) enabling the CRRM to take into account relevant qualitative factors in an automated and more effective manner when monitoring the credit risks presented by Members and (iii) enabling the CRRM to generate credit ratings for Members that are more reflective of the Members' default risk by shifting to an absolute scoring approach, all of which would improve NSCC's membership monitoring process overall. Therefore, NSCC believes the proposed enhancements to the CRRM would assist NSCC in identifying, measuring, monitoring and managing risks that arise in or are born by NSCC, consistent with the requirements of Rule 17Ad-22(e)(3)(i).

The proposed rule change to Section 2B of Rule 2B with respect to the scope of information that may be requested by NSCC from its Members has been designed to be consistent with Rule 17Ad-22(e)(19) under the Act, which was recently adopted by the

<sup>19</sup> 17 CFR 240.17Ad-22(e)(3)(i). The Commission adopted amendments to Rule 17Ad-22, including the addition of new subsection 17Ad-22(e), on September 28, 2016. See Securities Exchange Act Release No. 78961 (September 28, 2016), 81 FR 70786 (October 13, 2016) (S7-03-14). FICC is a "covered clearing agency" as defined by the new Rule 17Ad-22(a)(5) and must comply with new subsection (e) of Rule 17Ad-22 by April 11, 2017. *Id.*

<sup>20</sup> *Id.*

Commission.<sup>21</sup> Rule 17Ad-22(e)(19) will require NSCC to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify, monitor, and manage the material risk to NSCC arising from arrangements in which firms that are indirect participants in NSCC rely on the services provided by Members to access NSCC's payment, clearing, or settlement facilities.<sup>22</sup> By expressly reflecting in the Rules what is already NSCC's current practice associated with its request for additional reporting of a Member's financial or operational conditions to state that such request may include information regarding the businesses and operations of the Member, as well as its risk management practices with respect to services of NSCC utilized by the Member for another Person, this proposed rule change would help enable NSCC to have rule provisions that are reasonably designed to identify, monitor and manage the material risks to NSCC arising from tiered participation arrangements consistent with Rule 17Ad-22(e)(19).

#### III. Date of Effectiveness of the Advance Notice, and Timing for Commission Action

The proposed change may be implemented if the Commission does not object to the proposed change within 60 days of the later of (i) the date that the proposed change was filed with the Commission or (ii) the date that any additional information requested by the Commission is received. The clearing agency shall not implement the proposed change if the Commission has any objection to the proposed change.

The Commission may extend the period for review by an additional 60 days if the proposed change raises novel or complex issues, subject to the Commission providing the clearing agency with prompt written notice of the extension. A proposed change may be implemented in less than 60 days from the date the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the proposed change and authorizes the clearing agency to implement the proposed change on an earlier date, subject to any conditions imposed by the Commission.

The clearing agency shall post notice on its Web site of proposed changes that are implemented.

<sup>21</sup> 17 CFR 240.17Ad-22(e)(19). *Id.*

<sup>22</sup> *Id.*

<sup>17</sup> 12 U.S.C. 5464(b).

<sup>18</sup> *Id.*

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the Advance Notice is consistent with the Clearing Supervision Act. 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](mailto:rule-comments@sec.gov). Please include File Number SR-NSCC-2017-801 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549.

All submissions should refer to File Number SR-NSCC-2017-801. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the Advance Notice that are filed with the Commission, and all written communications relating to the Advance Notice 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 Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of NSCC and on DTCC's Web site (<http://dtcc.com/legal/sec-rule-filings.aspx>). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NSCC-2017-801 and should be submitted on or before April 28, 2017.

By the Commission.  
**Eduardo A. Aleman**,  
*Assistant Secretary*.  
 [FR Doc. 2017-07453 Filed 4-12-17; 8:45 am]  
**BILLING CODE 8011-01-P**

#### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-80401; File No. SR-PEARL-2017-17]

#### Self-Regulatory Organizations; MIAX PEARL, LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend the MIAX PEARL Fee Schedule

April 7, 2017.

Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 6, 2017, MIAX PEARL, LLC ("MIAX PEARL" or "Exchange") filed with the Securities and Exchange Commission ("Commission") a proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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

The Exchange is filing a proposal to amend the MIAX PEARL Fee Schedule (the "Fee Schedule") to waive transaction rebates/fees applicable to transactions executed during the opening and transactions that cross the Away Best Bid or Offer ("ABBO").

The Exchange initially filed the proposal on March 29, 2017 (SR-PEARL-2017-13). That filing has been withdrawn and replaced with the current filing (SR-PEARL-2017-17).

The text of the proposed rule change is available on the Exchange's Web site at <http://www.miaxoptions.com/rule-filings/pearl>, at MIAX PEARL's principal office, and at the Commission's Public Reference Room.

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

In its filing with the Commission, the Exchange 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. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

###### 1. Purpose

The purpose of this proposed rule change is to waive transaction rebates/fees applicable to executions that occur as part of the Exchange's opening procedures as described in Rule 503 ("Openings on the Exchange") or that uncross the ABBO,<sup>3</sup> as described in Rule 515 ("Execution of Orders").

Under the Openings on the Exchange Rule, the Exchange will accept orders for queuing in a series of options prior to the opening of trading in that series of options. As such and as further described in Rule 503, executions might occur in a series as part of the Exchange Opening as the series is being opened for trading. Pursuant to Section 1)a) of the Exchange's Fee Schedule, the Exchange currently assesses transaction rebates and fees for transactions that occur as part of the Exchange Opening. In order to determine the applicable transaction rebate and fee, the Exchange treats orders from Priority Customer<sup>4</sup> origin type as a "Maker," and treats orders from all origin types other than Priority Customer (i.e., MIAX PEARL Market Maker<sup>5</sup> and Non-Priority Customer, Firm, BD and Non-MIAX PEARL Market Maker)<sup>6</sup> as a "Taker." The Exchange now proposes that, for executions occurring as part of the Exchange Opening, the Exchange will neither charge a fee nor provide a rebate, regardless of origin type.

Further, pursuant to Section 1)a) of the Exchange's Fee Schedule, the Exchange currently assesses transaction rebates and fees for transactions that uncross the ABBO. In order to

<sup>3</sup> See MIAX PEARL Rule 100.

<sup>4</sup> The term "Priority Customer" is defined in Exchange Rule 100 to mean a person or entity that (i) is not a broker or dealer in securities, and (ii) does not place more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s). The number of orders is counted in accordance with Rule 100 Interpretation and Policy .01.

<sup>5</sup> The term "Market Maker" is defined in Exchange Rule 100 to mean a Member registered with the Exchange for the purpose of making markets in options contracts traded on the Exchange and that is vested with the rights and responsibilities specified in Chapter VI of the Exchange's Rules.

<sup>6</sup> See MIAX PEARL Fee Schedule, Section 1(a).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.