

procedures reasonably designed to ensure the covered clearing agency has the authority to take timely action to contain losses and liquidity demands and continue to meet its obligations.<sup>53</sup>

As described above, the proposal would establish a more detailed and structured loss allocation process by (1) applying a defined and mandatory Corporate Contribution to a loss; (2) introducing an Event Period; (3) introducing a loss allocation round and notice process; (4) modifying the termination process and the cap of terminating Participant's loss allocation exposure; and (5) providing the governance around a non-default loss. The Commission believes that each of these proposed changes helps establish a more transparent and clear loss allocation process and authority of DTC to take certain actions, such as announcing a Declared Non-Default Loss Event, within the loss allocation process. Further, having a more transparent and clear loss allocation process as proposed would provide clear authority to DTC to allocate losses from Default Loss Events and Declared Non-Default Loss Events and take timely actions to meet its clearance and settlement obligations.

Therefore, the Commission believes that DTC's proposal is consistent with Rule 17Ad-22(e)(13) under the Act.<sup>54</sup>

#### *E. Consistency With Rule 17Ad-22(e)(23)(i) and (ii)*

Rule 17Ad-22(e)(23)(i) under the Act requires that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to publicly disclose all relevant rules and material procedures, including key aspects of its default rules and procedures.<sup>55</sup> Rule 17Ad-22(e)(23)(ii) under the Act requires that a covered clearing agency establish, implement, maintain and enforce written policies and procedures reasonably designed to provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency.<sup>56</sup>

As described above, the proposal would publicly disclose how DTC's Corporate Contribution would be calculated and applied. In addition, the proposal would establish and publicly disclose a detailed procedure in the Rules for loss allocation. More

specifically, the proposed changes would establish an Event Period, loss allocation rounds, a termination process followed by a settlement charge process or loss allocation process, and a Loss Allocation Cap that would apply to Participants after termination. Additionally, the proposal would align the loss allocation rules across the DTCC Clearing Agencies, to help provide consistent treatment, and clarify that non-default losses would trigger loss allocation to Participants. The proposal would also provide for and make known to members the procedures to trigger a loss allocation procedure, contribute DTC's Corporate Contribution, allocate losses, and withdraw and limit Participant's loss exposure. Accordingly, the Commission believes that the proposal is reasonably designed to (1) publicly disclose all relevant rules and material procedures concerning key aspects of DTC's default rules and procedures, and (2) provide sufficient information to enable Participants to identify and evaluate the risks by participating in DTC.

Therefore, the Commission believes that DTC's proposal is consistent with Rules 17Ad-22(e)(23)(i) and (ii) under the Act.<sup>57</sup>

### III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act<sup>58</sup> and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>59</sup> that proposed rule change SR-DTC-2017-022, as modified by Amendment No. 1, be, and it hereby is, approved<sup>60</sup> as of the date of this order or the date of a notice by the Commission authorizing DTC to implement advance notice SR-DTC-2017-804, as modified by Amendment No. 1, whichever is later.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>61</sup>

**Eduardo A. Aleman,**

*Assistant Secretary.*

[FR Doc. 2018-19061 Filed 8-31-18; 8:45 am]

**BILLING CODE 8011-01-P**

<sup>53</sup> 17 CFR 240.17Ad-22(e)(23)(i) and (ii).

<sup>54</sup> 15 U.S.C. 78q-1.

<sup>55</sup> 15 U.S.C. 78s(b)(2).

<sup>60</sup> In approving the Proposed Rule Change, the Commission has considered the Proposed Rule Change's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>61</sup> 17 CFR 200.30-3(a)(12).

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-83972; File No. SR-DTC-2017-021]

### Self-Regulatory Organizations; The Depository Trust Company; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, To Adopt a Recovery & Wind-Down Plan and Related Rules

August 28, 2018.

On December 18, 2017, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-DTC-2017-021 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder<sup>2</sup> to adopt a recovery and wind-down plan and related rules.<sup>3</sup> The proposed rule

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

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

<sup>3</sup> On December 18, 2017, DTC filed the proposed rule change as advance notice SR-DTC-2017-803 with the Commission 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") and Rule 19b-4(n)(1)(i) of the Act ("Advance Notice"). 12 U.S.C. 5465(e)(1) and 17 CFR 240.19b-4(m)(1)(i), respectively. The Advance Notice was published for comment in the **Federal Register** on January 30, 2018. In that publication, the Commission also extended the review period of the Advance Notice for an additional 60 days, pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act. 12 U.S.C. 5465(e)(1)(H); Securities Exchange Act Release No. 82579 (January 24, 2018), 83 FR 4310 (January 30, 2018) (SR-DTC-2017-803). On April 10, 2018, the Commission required additional information from DTC pursuant to Section 806(e)(1)(D) of the Clearing Supervision Act, which tolled the Commission's period of review of the Advance Notice until 60 days from the date the information required by the Commission was received by the Commission. 12 U.S.C. 5465(e)(1)(D); see 12 U.S.C. 5465(e)(1)(E)(ii) and (G)(ii); see Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled "Commission's Request for Additional Information," available at <http://www.sec.gov/rules/sro/dtc-an.shtml> since June 29, 2018. On June 28, 2018, DTC filed Amendment No. 1 to the Advance Notice to amend and replace in its entirety the Advance Notice as originally filed on December 18, 2017. Securities Exchange Act Release No. 83743 (July 31, 2018), 83 FR 38344 (August 6, 2018) (SR-DTC-2017-803). DTC submitted a courtesy copy of Amendment No. 1 to the Advance Notice through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Advance Notice has been publicly available on the Commission's website at <http://www.sec.gov/rules/sro/dtc-an.shtml> since June 29, 2018. On July 6, 2018, the Commission received a response to its request for additional information in consideration of the Advance Notice, which, in turn, added a further 60-days to the review period pursuant to Section 806(e)(1)(E) and (G) of the Clearing Supervision Act. 12 U.S.C. 5465(e)(1)(E) and (G); see Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled "Response to the Commission's Request for Additional Information," available at

<sup>53</sup> 17 CFR 240.17Ad-22(e)(13).

<sup>54</sup> *Id.*

<sup>55</sup> 17 CFR 240.17Ad-22(e)(23)(i).

<sup>56</sup> 17 CFR 240.17Ad-22(e)(23)(ii).

change was published for comment in the **Federal Register** on January 8, 2018.<sup>4</sup> On February 8, 2018, the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the proposed rule change.<sup>5</sup> On March 20, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change.<sup>6</sup> On June 25, 2018, the Commission designated a longer period for Commission action on the proceedings to determine whether to approve or disapprove the proposed rule change.<sup>7</sup> On June 28, 2018, DTC filed Amendment No. 1 to the proposed rule change to amend and replace in its entirety the proposed rule change as originally submitted on December 18, 2017.<sup>8</sup> The Commission did not receive any comments. This order approves the proposed rule change, as modified by Amendment No. 1 (hereinafter “Proposed Rule Change”).

## I. Description

In the Proposed Rule Change, DTC proposes to (1) adopt an R&W Plan; and (2) amend the Rules, By-Laws and Organization Certificate of DTC (“Rules”)<sup>9</sup> to adopt Rule 32(A) (Wind-down of the Corporation) and Rule 38 (Market Disruption and Force Majeure) (each proposed Rule 32(A) and proposed Rule 38, a “Proposed Rule” and, collectively, the “Proposed Rules”).

DTC states that the R&W Plan would be used by the Board of Directors of

<http://www.sec.gov/rules/sro/dtc-an.shtml>. The Commission did not receive any comments. The proposal, as set forth in both the Advance Notice and the proposed rule change, each as modified by Amendments No. 1, shall not take effect until all required regulatory actions are completed.

<sup>4</sup> Securities Exchange Act Release No. 82432 (January 2, 2018), 83 FR 884 (January 8, 2018) (SR-DTC-2017-021).

<sup>5</sup> Securities Exchange Act Release No. 82669 (February 8, 2018), 83 FR 6653 (February 14, 2018) (SR-DTC-2017-021, SR-FICC-2017-021, SR-NSCC-2017-017).

<sup>6</sup> Securities Exchange Act Release No. 82912 (March 20, 2018), 83 FR 12999 (March 26, 2018) (SR-DTC-2017-021).

<sup>7</sup> Securities Exchange Act Release No. 83509 (June 25, 2018), 83 FR 30785 (June 29, 2018) (SR-DTC-2017-021, SR-FICC-2017-021, SR-NSCC-2017-017).

<sup>8</sup> Securities Exchange Act Release No. 83628 (July 13, 2018), 83 FR 34263 (July 19, 2018) (SR-DTC-2017-021). DTC submitted a courtesy copy of Amendment No. 1 to the proposed rule change through the Commission’s electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the proposed rule change has been publicly available on the Commission’s website at <https://www.sec.gov/rules/sro/dtc.htm> since June 29, 2018.

<sup>9</sup> Capitalized terms used herein and not otherwise defined herein are defined in the Rules.

DTC (“Board”) and DTC’s management in the event DTC encounters scenarios that could potentially prevent it from being able to provide its critical services as a going concern.

DTC states that the Proposed Rules are designed to (1) facilitate the implementation of the R&W Plan when necessary and, in particular, allow DTC to effectuate its strategy for winding down and transferring its business; (2) provide Participants with transparency around critical provisions of the R&W Plan that relate to their rights, responsibilities and obligations; and (3) provide DTC with the legal basis to implement those provisions of the R&W Plan when necessary.

### A. DTC R&W Plan

The R&W Plan would be structured to provide a roadmap, define the strategy, and identify the tools available to DTC to either (i) recover, in the event it experiences losses that exceed its prefunded resources (such strategies and tools referred to herein as the “Recovery Plan”) or (ii) wind-down its business in a manner designed to permit the continuation of its critical services in the event that such recovery efforts are not successful (such strategies and tools referred to herein as the “Wind-down Plan”).

The R&W Plan would identify (i) the recovery tools available to DTC to address the risks of (a) uncovered losses or liquidity shortfalls resulting from the default of one or more of its Participants, and (b) losses arising from non-default events, such as damage to its physical assets, a cyber-attack, or custody and investment losses, and (ii) the strategy for implementation of such tools. The R&W Plan would also establish the strategy and framework for the orderly wind-down of DTC and the transfer of its business in the remote event the implementation of the available recovery tools does not successfully return DTC to financial viability.

As discussed in greater detail below, the R&W Plan would provide, among other matters, (i) an overview of the business of DTC and its parent, The Depository Trust & Clearing Corporation (“DTCC”);<sup>10</sup> (ii) an analysis of DTC’s intercompany arrangements and critical links to other financial market

<sup>10</sup> DTCC is a user-owned and user-governed holding company and is the parent company of DTC and its affiliates, National Securities Clearing Corporation (“NSCC”) and Fixed Income Clearing Corporation (“FICC,” and, together with NSCC and DTC, the “Clearing Agencies”). The R&W Plan would describe how corporate support services are provided to DTC from DTCC and DTCC’s other subsidiaries through intercompany agreements under a shared services model.

infrastructure (“FMI”); (iii) a description of DTC’s services, and the criteria used to determine which services are considered critical; (iv) a description of the DTC and DTCC governance structure; (v) a description of the governance around the overall recovery and wind-down program; (vi) a discussion of tools available to DTC to mitigate credit/market<sup>11</sup> risks and liquidity risks, including recovery indicators and triggers, and the governance around management of a stress event along a Crisis Continuum timeline; (vii) a discussion of potential non-default losses and the resources available to DTC to address such losses, including recovery triggers and tools to mitigate such losses; (viii) an analysis of the recovery tools’ characteristics, including how they are designed to be comprehensive, effective, and transparent, how the tools provide incentives to Participants to, among other things, control and monitor the risks they may present to DTC, and how DTC seeks to minimize the negative consequences of executing its recovery tools; and (ix) the framework and approach for the orderly wind-down and transfer of DTC’s business, including an estimate of the time and costs to effect a recovery or orderly wind-down of DTC.

Certain recovery tools that would be identified in the R&W Plan are based in the Rules (including the Proposed Rules); therefore, descriptions of those tools in the R&W Plan would include descriptions of, and reference to, the applicable Rules and any related internal policies and procedures. Other recovery tools that would be identified in the R&W Plan are based in contractual arrangements to which DTC is a party, including, for example, existing committed or pre-arranged liquidity arrangements. Further, the R&W Plan would state that DTC may develop further supporting internal guidelines and materials that may provide operational support for matters described in the R&W Plan, and that such documents would be supplemental and subordinate to the R&W Plan.

DTC states that many of the tools available to DTC that would be described in the R&W Plan are DTC’s existing, business-as-usual risk management and default management tools, which would continue to be applied in scenarios of increasing stress. In addition to these existing, business-as-usual tools, the R&W Plan would

<sup>11</sup> DTC states that it uses the term “credit/market” risks in the R&W Plan because, for DTC, credit risk and market risk are closely related. *See infra* note 22.

describe DTC's other principal recovery tools, which include, for example, (i) identifying, monitoring and managing general business risk and holding sufficient liquid net assets funded by equity ("LNA") to cover potential general business losses pursuant to the Clearing Agency Policy on Capital Requirements ("Capital Policy"),<sup>12</sup> (ii) maintaining the Clearing Agency Capital Replenishment Plan ("Replenishment Plan") as a viable plan for the replenishment of capital should DTC's equity fall close to or below the amount being held pursuant to the Capital Policy,<sup>13</sup> and (iii) the process for the allocation of losses among Participants as provided in Rule 4 (Participants Fund and Participants Investment).<sup>14</sup> The R&W Plan would provide governance around the selection and implementation of the recovery tool or tools most relevant to mitigate a stress scenario and any applicable loss or liquidity shortfall.

The development of the R&W Plan is facilitated by the Office of Recovery & Resolution Planning ("R&R Team") of DTCC.<sup>15</sup> The R&R Team reports to the DTCC Management Committee ("Management Committee") and is responsible for maintaining the R&W Plan and for the development and ongoing maintenance of the overall recovery and wind-down planning process. The Board, or such committees as may be delegated authority by the Board from time to time pursuant to its charter, would review and approve the R&W Plan biennially, and would also review and approve any changes that are proposed to the R&W Plan outside of the biennial review.

As discussed in greater detail below, the Proposed Rules would define the procedures that may be employed in the event of a DTC wind-down, and would provide for DTC's authority to take certain actions on the occurrence of a Market Disruption Event, as defined therein. DTC states that the Proposed Rules are designed to provide Participants with transparency and certainty with respect to these matters. DTC also states that the Proposed Rules are designed to facilitate the implementation of the R&W Plan,

particularly DTC's strategy for winding down and transferring its business, and are designed to provide DTC with the legal basis to implement those aspects of the R&W Plan.

#### 1. Business Overview, Critical Services, and Governance

The introduction to the R&W Plan would identify the document's purpose and its regulatory background, and would outline a summary of the R&W Plan. The stated purpose of the R&W Plan is that it is to be used by the Board and DTC management in the event DTC encounters scenarios that could potentially prevent it from being able to provide its critical services as a going concern.

The R&W Plan would describe DTCC's business profile, provide a summary of DTC's services, and identify the intercompany arrangements and critical links between DTC and other FMIs. DTC states that the overview section would provide a context for the R&W Plan by describing DTC's business, organizational structure and critical links to other entities. DTC also states that by providing this context, this section would facilitate the analysis of the potential impact of utilizing the recovery tools set forth in later sections of the Recovery Plan, and the analysis of the factors that would be addressed in implementing the Wind-down Plan.

The R&W Plan would provide a description of established links between DTC and other FMIs, both domestic and foreign, including central securities depositories ("CSDs") and central counterparties ("CCPs"), as well as the twelve U.S. Federal Reserve Banks. DTC states that this section of the R&W Plan, which identifies and briefly describes DTC's established links, is designed to provide a mapping of critical connections and dependencies that may need to be relied on or otherwise addressed in connection with the implementation of either the Recovery Plan or the Wind-down Plan.

The R&W Plan would define the criteria for classifying certain of DTC's services as "critical," and would identify those critical services and the rationale for their classification. This section of the R&W Plan would provide an analysis of the potential systemic impact from a service disruption, which DTC states is important for evaluating how the recovery tools and the wind-down strategy would facilitate and provide for the continuation of DTC's critical services to the markets it serves. The criteria that would be used to identify a DTC service or function as critical would include (1) whether there is a lack of alternative providers or

products; (2) whether failure of the service could impact DTC's ability to perform its book-entry and settlement services; (3) whether failure of the service could impact DTC's ability to perform its payment system functions; and (4) whether the service is interconnected with other participants and processes within the U.S. financial system, for example, with other FMIs, settlement banks and broker-dealers. The R&W Plan would then list each of those services, functions or activities that DTC has identified as "critical" based on the applicability of these four criteria. The R&W Plan would also include a non-exhaustive list of DTC services that are not deemed critical.

DTC states that the evaluation of which services provided by DTC are deemed critical is important for purposes of determining how the R&W Plan would facilitate the continuity of those services. While DTC's Wind-down Plan would provide for the transfer of all critical services to a transferee in the event DTC's wind-down is implemented, it would anticipate that any non-critical services that are ancillary and beneficial to a critical service, or that otherwise have substantial user demand from the continuing membership, would also be transferred.

The R&W Plan would describe the governance structure of both DTCC and DTC. This section of the R&W Plan would identify the ownership and governance model of these entities at both the Board and management levels. The R&W Plan would state that the stages of escalation required to manage recovery under the Recovery Plan or to invoke DTC's wind-down under the Wind-down Plan would range from relevant business line managers up to the Board through DTC's governance structure. The R&W Plan would then identify the parties responsible for certain activities under both the Recovery Plan and the Wind-down Plan, and would describe their respective roles. The R&W Plan would identify the Risk Committee of the Board ("Board Risk Committee") as being responsible for oversight of risk management activities at DTC, which include focusing on both oversight of risk management systems and processes designed to identify and manage various risks faced by DTC as well as oversight of DTC's efforts to mitigate systemic risks that could impact those markets and the broader financial system.<sup>16</sup> The

<sup>12</sup> See Securities Exchange Act Release No. 81105 (July 7, 2017), 82 FR 32399 (July 13, 2017) (SR-DTC-2017-003, SR-FICC-2017-007, SR-NSCC-2017-004).

<sup>13</sup> See *id.*

<sup>14</sup> See *supra* note 9.

<sup>15</sup> DTCC operates on a shared services model with respect to DTC and its other subsidiaries. Most corporate functions are established and managed on an enterprise-wide basis pursuant to intercompany agreements under which it is generally DTCC that provides a relevant service to a subsidiary, including DTC.

<sup>16</sup> The DTCC, DTC, NSCC, FICC Risk Committee Charter is available at <http://www.dtcc.com/-/media/Files/Downloads/legal/policy-and-compliance/DTCC-BOD-Risk-Committee-Charter.pdf>.

R&W Plan would identify the DTCC Management Risk Committee (“Management Risk Committee”) as primarily responsible for general, day-to-day risk management through delegated authority from the Board Risk Committee. The R&W Plan would state that the Management Risk Committee has delegated specific day-to-day risk management, including management of risks addressed through margining systems and related activities, to the DTCC Group Chief Risk Office (“GCRO”), which works with staff within the DTCC Financial Risk Management group. Finally, the R&W Plan would describe the role of the Management Committee, which provides overall direction for all aspects of DTC’s business, technology, and operations and the functional areas that support these activities.

The R&W Plan would describe the governance of recovery efforts in response to both default losses and non-default losses under the Recovery Plan, identifying the groups responsible for those recovery efforts. Specifically, the R&W Plan would state that the Management Risk Committee provides oversight of actions relating to the default of a Participant, which would be reported and escalated to it through the GCRO, and the Management Committee provides oversight of actions relating to non-default events that could result in a loss, which would be reported and escalated to it from the DTCC Chief Financial Officer (“CFO”) and the DTCC Treasury group that reports to the CFO, and from other relevant subject matter experts based on the nature and circumstances of the non-default event.<sup>17</sup> More generally, the R&W Plan would state that the type of loss and the nature and circumstances of the events that lead to the loss would dictate the components of governance to address that loss, including the escalation path to authorize those actions. Both the Recovery Plan and the Wind-down Plan would describe the governance of escalations, decisions, and actions under each of those plans.

Finally, the R&W Plan would describe the role of the R&R Team in managing the overall recovery and wind-down program and plans for each of the Clearing Agencies.

<sup>17</sup> The R&W Plan would state that these groups would be involved to address how to mitigate the financial impact of non-default losses, and in recommending mitigating actions, the Management Committee would consider information and recommendations from relevant subject matter experts based on the nature and circumstances of the non-default event. Any necessary operational response to these events, however, would be managed in accordance with applicable incident response/business continuity process.

## 2. DTC Recovery Plan

DTC states that the Recovery Plan is intended to be a roadmap of those actions that DTC may employ to monitor and, as needed, stabilize its financial condition. DTC also states that as each event that could lead to a financial loss could be unique in its circumstances, DTC proposes that the Recovery Plan would not be prescriptive and would permit DTC to maintain flexibility in its use of identified tools and in the sequence in which such tools are used, subject to any conditions in the Rules or the contractual arrangement on which such tool is based. DTC’s Recovery Plan would consist of (1) a description of the risk management surveillance, tools, and governance that DTC would employ across evolving stress scenarios that it may face as it transitions through a Crisis Continuum, described below; (2) a description of DTC’s risk of losses that may result from non-default events, and the financial resources and recovery tools available to DTC to manage those risks and any resulting losses; and (3) an evaluation of the characteristics of the recovery tools that may be used in response to either losses arising out of a Participant Default (as defined below) or non-default losses. In all cases, DTC states that it would act in accordance with the Rules, within the governance structure described in the R&W Plan, and in accordance with applicable regulatory oversight to address each situation to best protect DTC, its Participants and the markets in which it operates.

### (i) Managing Participant Default Losses and Liquidity Needs Through the Crisis Continuum

The Recovery Plan would describe the risk management surveillance, tools, and governance that DTC may employ across an increasing stress environment, which is referred to as the Crisis Continuum. This description would identify those tools that can be employed to mitigate losses, and mitigate or minimize liquidity needs, as the market environment becomes increasingly stressed. The phases of the Crisis Continuum would include (1) a stable market phase, (2) a stress market phase, (3) a phase commencing with DTC’s decision to cease to act for a Participant or Affiliated Family of Participants<sup>18</sup> (referred to in the R&W Plan as the “Participant Default phase”), and (4) a recovery phase. In the R&W Plan, the term “cease to act” and the actions that may lead to such decision

<sup>18</sup> The R&W Plan would define an “Affiliated Family” of Participants as a number of affiliated entities that are all Participants of DTC.

are used within the context of the Rules.<sup>19</sup> The R&W Plan would, for purposes of the R&W Plan, use the term “Participant Default Losses” to refer to losses that arise out of or relate to the Participant Default and resulting cease to act (including any losses that arise from liquidation of the Participant’s Collateral).

DTC states that the Recovery Plan would provide context to its roadmap through this Crisis Continuum by describing DTC’s ongoing management of credit, market, and liquidity risk, and its existing process for measuring and reporting its risks as they align with established thresholds for its tolerance of those risks. DTC also states that the Recovery Plan would discuss the management of credit/market risk and liquidity exposures together because the tools that address these risks can be deployed either separately or in a coordinated approach in order to address both exposures. DTC states that it manages these risk exposures collectively to limit their overall impact on DTC and its Participants. DTC states that it has built-in mechanisms to limit exposures and replenish financial resources used in a stress event, in order to continue to operate in a safe and sound manner. DTC states that it is a closed, collateralized system in which liquidity resources are matched against risk management controls, so, at any time, the potential net settlement obligation of the Participant or Affiliated Family of Participants with the largest net settlement obligation cannot exceed the amount of liquidity resources.<sup>20</sup> DTC states that while Collateral securities are subject to market price risk, DTC manages its liquidity and market risks through the calculation of the required deposits to the Participants Fund<sup>21</sup> and risk management controls, *i.e.*, collateral

<sup>19</sup> See Rule 4 (Participants Fund and Participants Investment), Rule 9(A) (Transactions in Securities and Money Payments), Rule 9(B) (Transactions in Eligible Securities), Rule 9(C) (Transactions in MMI Securities), Rule 10 (Discretionary Termination), Rule 11 (Mandatory Termination) and Rule 12 (Insolvency), *supra* note 9. Further, the term “Participant Default” would also be used in the R&W Plan as such term is defined in Rule 4 (Participants Fund and Participants Investment), *see supra* note 9.

<sup>20</sup> DTC’s liquidity risk management strategy, including the manner in which DTC would deploy liquidity tools as well as its intraday use of liquidity, is described in the Clearing Agency Liquidity Risk Management Framework. See Securities Exchange Act Release No. 82377 (December 21, 2017), 82 FR 61617 (December 28, 2017) (SR-DTC-2017-004, SR-FICC-2017-008, SR-NSCC-2017-005).

<sup>21</sup> See Rule 4 (Participants Fund and Participants Investment), *supra* note 9.

haircuts, the Collateral Monitor<sup>22</sup> and Net Debit Cap.<sup>23</sup>

The Recovery Plan would outline the metrics and indicators that DTC has developed to evaluate a stress situation against established risk tolerance thresholds. Each risk mitigation tool identified in the Recovery Plan would include a description of the escalation thresholds that allow for effective and timely reporting to the appropriate internal management staff and committees, or to the Board. DTC states that the Recovery Plan is designed to make clear that these tools and escalation protocols would be calibrated across each phase of the Crisis Continuum. The Recovery Plan would also establish that DTC would retain the flexibility to deploy such tools either separately or in a coordinated approach, and to use other alternatives to these actions and tools as necessitated by the circumstances of a particular Participant Default event, in accordance with the Rules. Therefore, DTC states that the Recovery Plan would both provide DTC with a roadmap to follow within each phase of the Crisis Continuum, and would permit it to adjust its risk management measures to address the unique circumstances of each event.

The Recovery Plan would describe the conditions that mark each phase of the Crisis Continuum, and would identify actions that DTC could take as it transitions through each phase in order to both prevent losses from materializing through active risk management, and to restore the financial health of DTC during a period of stress.

The stable market phase of the Crisis Continuum would describe active risk management activities in the normal course of business. These activities would include performing (1) backtests to evaluate the adequacy of the collateral level and the haircut sufficiency for covering market price volatility and (2) stress testing to cover market price moves under real historical and hypothetical scenarios to assess the

haircut adequacy under extreme but plausible market conditions. The backtesting and stress testing results are escalated, as necessary, to internal and Board committees.<sup>24</sup>

The Recovery Plan would describe some of the indicators of the stress market phase of the Crisis Continuum, which would include, for example, volatility in market prices of certain assets where there is increased uncertainty among market participants about the fundamental value of those assets. This phase would involve general market stresses, when no Participant Default would be imminent. Within the description of this phase, the Recovery Plan would provide that DTC may take targeted, routine risk management measures as necessary and as permitted by the Rules.

Within the Participant Default phase of the Crisis Continuum, the Recovery Plan would provide a roadmap for the existing procedures that DTC would follow in the event of a Participant Default and any decision by DTC to cease to act for that Participant.<sup>25</sup> The Recovery Plan would provide that the objectives of DTC's actions upon a Participant Default are to (1) minimize losses and market exposure, and (2), to the extent practicable, minimize disturbances to the affected markets. The Recovery Plan would describe tools, actions, and related governance for both market risk monitoring and liquidity risk monitoring through this phase. Management of liquidity risk through this phase would involve ongoing monitoring of, among other things, the adequacy of the Participants Fund and risk controls, and the Recovery Plan would identify certain actions DTC may deploy as it deems necessary to mitigate a potential liquidity shortfall. The Recovery Plan would state that, throughout this phase, relevant information would be escalated and reported to both internal management committees and the Board Risk Committee.

The Recovery Plan would also identify financial resources available to DTC, pursuant to the Rules, to address losses arising out of a Participant Default. Specifically, Rule 4 (Participants Fund and Participants Investment) provides that losses remaining after application of the

Defaulting Participant's resources be satisfied first by applying a Corporate Contribution, and then, if necessary, by allocating remaining losses among the membership in accordance with Rule 4 (Participants Fund and Participants Investment).<sup>26</sup>

In order to provide for an effective and timely recovery, the Recovery Plan would describe the period of time that would occur near the end of the Participant Default phase, during which DTC may experience stress events or observe early warning indicators that allow it to evaluate its options and prepare for the recovery phase (referred to in the R&W Plan as the Recovery Corridor). The Recovery Plan would then describe the recovery phase of the Crisis Continuum, which would begin on the date that DTC issues the first Loss Allocation Notice of the second loss allocation round with respect to a given Event Period.<sup>27</sup> The recovery phase would describe actions that DTC may take to avoid entering into a wind-down of its business.

DTC states that it expects that significant deterioration of liquidity resources would cause it to enter the Recovery Corridor. Therefore, the R&W Plan would describe the actions DTC may take aimed at replenishing those resources. Throughout the Recovery Corridor, DTC would monitor the adequacy of its resources and the expected timing of replenishment of those resources, and would do so through the monitoring of certain corridor indicator metrics.

<sup>26</sup> See *supra* note 9. Rule 4 (Participants Fund and Participants Investment) defines the amount DTC would contribute to address a loss resulting from either a Participant Default or a non-default event as the Corporate Contribution. This amount is 50 percent of the General Business Risk Capital Requirement, which is calculated pursuant to the Capital Policy and, which DTC states is an amount sufficient to cover potential general business losses so that DTC can continue operations and services as a going concern if those losses materialize, in an effort to comply with Rule 17Ad-22(e)(15) under the Act. See *supra* note 12 (concerning the Capital Policy); 17 CFR 240.17Ad-22(e)(15).

<sup>27</sup> As provided for in Rule 4 (Participants Fund and Participants Investment), the "Event Period" is ten Business Days beginning on (i) with respect to a Participant Default, the day on which DTC notifies Participants that it has ceased to act for a Participant, or (ii) with respect to a non-default loss, the day that DTC notifies Participants of the determination by the Board that there is a non-default loss event. Rule 4 (Participants Fund and Participants Investment) defines a "round" as a series of loss allocations relating to an Event Period, and provides that the first Loss Allocation Notice in a first, second, or subsequent round shall expressly state that such notice reflects the beginning of a first, second, or subsequent round. The maximum allocable loss amount of a round is equal to the sum of the Loss Allocation Caps of those Participants included in the round. See Rule 4 (Participants Fund and Participants Investment), *supra* note 9.

<sup>22</sup> See Rule 1 (Definitions; Governing Law), Section 1, *supra* note 9. DTC states that credit risk and market risk are closely related for DTC, because DTC monitors credit exposures from Participants through these risk management controls, which limit Participant settlement obligations to the amount of available liquidity resources and require those obligations to be fully collateralized. The pledge or liquidation of collateral in an amount sufficient to restore liquidity resources depends on market values and demand, *i.e.*, market risk exposure. DTC states that such risk management controls are part of DTC's market risk management strategy and are designed to comply with Rule 17Ad-22(e)(4) under the Act, where these risks are referred to as "credit risks." See 17 CFR 240.17Ad-22(e)(4).

<sup>23</sup> *Id.*

<sup>24</sup> DTC's stress testing practices are described in the Clearing Agency Stress Testing Framework (Market Risk). See Securities Exchange Act Release No. 82638 (December 19, 2017), 82 FR 61082 (December 26, 2017) (SR-DTC-2017-005, SR-FICC-2017-009, SR-NSCC-2017-006).

<sup>25</sup> See Rule 10 (Discretionary Termination); Rule 11 (Mandatory Termination); Rule 12 (Insolvency), *supra* note 9.

DTC states that the majority of the corridor indicators, as identified in the Recovery Plan, relate directly to conditions that may require DTC to adjust its strategy for hedging and liquidating Collateral securities, and any such changes would include an assessment of the status of the corridor indicators. For each corridor indicator, the Recovery Plan would identify (1) measures of the indicator, (2) evaluations of the status of the indicator, (3) metrics for determining the status of the deterioration or improvement of the indicator, and (4) Corridor Actions, which are steps that may be taken to improve the status of the indicator,<sup>28</sup> as well as management escalations required to authorize those steps. DTC states that because DTC has never experienced the default of multiple Participants, it has not, historically, measured the deterioration or improvements metrics of the corridor indicators. Therefore, DTC states that these metrics were chosen based on the business judgment of DTC management.

The Recovery Plan would also describe the reporting and escalation of the status of the corridor indicators throughout the Recovery Corridor. Significant deterioration of a corridor indicator, as measured by the metrics set out in the Recovery Plan, would be escalated to the Board. DTC management would review the corridor indicators and the related metrics at least annually, and would modify these metrics as necessary in light of observations from simulations of Participant Defaults and other analyses. Any proposed modifications would be reviewed by the Management Risk Committee and the Board Risk Committee. The Recovery Plan would estimate that DTC may remain in the Recovery Corridor stage between one day and two weeks. DTC states that this estimate is based on historical data observed in past Participant Default events, the results of simulations of Participant Defaults, and periodic liquidity analyses conducted by DTC. DTC states that the actual length of a Recovery Corridor would vary based on actual market conditions observed at the time, and DTC would expect the Recovery Corridor to be shorter in market conditions of increased stress.

The Recovery Plan would outline steps by which DTC may allocate its

losses, which would occur when and in the order provided in Rule 4 (Participants Fund and Participants Investment).<sup>29</sup> The Recovery Plan would also identify tools that may be used to address foreseeable shortfalls of DTC's liquidity resources following a Participant Default, and would provide that these tools may be used as appropriate during the Crisis Continuum to address liquidity shortfalls if they arise. DTC states that the goal in managing DTC's liquidity resources is to maximize resource availability in an evolving stress situation, to maintain flexibility in the order and use of sources of liquidity, and to repay any third party lenders in a timely manner. DTC states that the Recovery Plan would state that the availability and capacity of these liquidity tools cannot be accurately predicted and are dependent on the circumstances of the applicable stress period, including market price volatility, actual or perceived disruptions in financial markets, the costs to DTC of utilizing these tools, and any potential impact on DTC's credit rating.

The Recovery Plan would state that DTC will have entered the recovery phase on the date that it issues the first Loss Allocation Notice of the second loss allocation round with respect to a given Event Period. The Recovery Plan would provide that, during the recovery phase, DTC would continue and, as needed, enhance, the monitoring and remedial actions already described in connection with previous phases of the Crisis Continuum, and would remain in the recovery phase until its financial resources are expected to be or are fully replenished, or until the Wind-down Plan is triggered.

The Recovery Plan would describe governance for the actions and tools that may be employed within each phase of the Crisis Continuum, which would be dictated by the facts and circumstances applicable to the situation being addressed. Such facts and circumstances would be measured by the various indicators and metrics applicable to that phase of the Crisis Continuum, and would follow relevant escalation protocol that would be described in the Recovery Plan. The Recovery Plan would also describe the governance procedures around a decision to cease to act for a Participant, pursuant to the Rules, and around the management and oversight of the subsequent liquidation of Collateral securities. The Recovery Plan would state that, overall, DTC would retain

flexibility in accordance with the Rules, its governance structure, and its regulatory oversight, to address a particular situation in order to best protect DTC and its Participants, and to meet the primary objectives, throughout the Crisis Continuum, of minimizing losses and, where consistent and practicable, minimizing disturbance to affected markets.

#### (ii) Non-Default Losses

The Recovery Plan would outline how DTC may address losses that result from events other than a Participant Default. While these matters are addressed in greater detail in other documents, this section of the R&W Plan would provide a roadmap to those documents and an outline for DTC's approach to monitoring and managing losses that could result from a non-default event. The R&W Plan would first identify some of the risks DTC faces that could lead to these losses, which include, for example, (1) the business and profit/loss risks of unexpected declines in revenue or growth of expenses; (2) the operational risks of disruptions to systems or processes that could lead to large losses, including those resulting from, for example, a cyber-attack; and (3) custody or investment risks that could lead to financial losses. The Recovery Plan would describe DTC's overall strategy for the management of these risks, which includes a "three lines of defense" approach to risk management that allows for comprehensive management of risk across the organization.<sup>30</sup> The Recovery Plan would also describe DTC's approach to financial risk and capital management. The R&W Plan would identify key aspects of this approach, including, for example, an annual budget process, business line

<sup>30</sup>DTC states that the "three lines of defense" approach to risk management includes (1) a first line of defense comprised of the various business lines and functional units that support the products and services offered by DTC; (2) a second line of defense comprised of control functions that support DTC, including the risk management, legal and compliance areas; and (3) a third line of defense, which is performed by an internal audit group. The Clearing Agency Risk Management Framework includes a description of this "three lines of defense" approach to risk management, and addresses how DTC comprehensively manages various risks, including operational, general business, investment, custody, and other risks that arise in or are borne by it. Securities Exchange Act Release No. 81635 (September 15, 2017), 82 FR 44224 (September 21, 2017) (SR-DTC-2017-013, SR-FICC-2017-016, SR-NSCC-2017-012). The Clearing Agency Operational Risk Management Framework describes the manner in which DTC manages operational risks, as defined therein. Securities Exchange Act Release No. 81745 (September 28, 2017), 82 FR 46332 (October 4, 2017) (SR-DTC-2017-014, SR-FICC-2017-017, SR-NSCC-2017-013).

<sup>28</sup>The Corridor Actions that would be identified in the R&W Plan are designed to be indicative, but not prescriptive; therefore, if DTC needs to consider alternative actions due to the applicable facts and circumstances, the escalation of those alternative actions would follow the same escalation protocol identified in the R&W Plan for the Corridor Indicator to which the action relates.

<sup>29</sup> See *supra* note 9.

performance reviews with management, and regular review of capital requirements against LNA. These risk management strategies are collectively intended to allow DTC to effectively identify, monitor, and manage risks of non-default losses.

The R&W Plan would identify the two categories of financial resources DTC maintains to cover losses and expenses arising from non-default risks or events as (1) LNA, maintained, monitored, and managed pursuant to the Capital Policy, which include (a) amounts held in satisfaction of the General Business Risk Capital Requirement,<sup>31</sup> (b) the Corporate Contribution,<sup>32</sup> and (c) other amounts held in excess of DTC's capital requirements pursuant to the Capital Policy; and (2) resources available pursuant to the loss allocation provisions of Rule 4 (Participants Fund and Participants Investment).<sup>33</sup>

The R&W Plan would address the process by which the CFO and the DTCC Treasury group would determine which available LNA resources are most appropriate to cover a loss that is caused by a non-default event. This determination involves an evaluation of a number of factors, including the current and expected size of the loss, the expected time horizon over when the loss or additional expenses would materialize, the current and projected available LNA, and the likelihood LNA could be successfully replenished pursuant to the Replenishment Plan, if triggered.<sup>34</sup> Finally the R&W Plan would discuss how DTC would apply its resources to address losses resulting from a non-default event, including the order of resources it would apply if the loss or liability is expected to exceed DTC's excess LNA amounts, or is large relative thereto, and the Board has declared the event a Declared Non-Default Loss Event pursuant to Rule 4 (Participants Fund and Participants Investment).<sup>35</sup>

The R&W Plan would also describe proposed Rule 38 (Market Disruption and Force Majeure), which DTC is proposing to adopt in the Rules. DTC states that this Proposed Rule is designed to provide transparency around how DTC would address extraordinary events that may occur outside its control. Specifically, the Proposed Rule would define a Market Disruption Event and the governance around a determination that such an

event has occurred. The Proposed Rule would also describe DTC's authority to take actions during the pendency of a Market Disruption Event that it deems appropriate to address such an event and facilitate the continuation of its services, if practicable.

The R&W Plan would describe the interaction between the Proposed Rule and DTC's existing processes and procedures addressing business continuity management and disaster recovery (generally, the "BCM/DR procedures"). DTC states that the intent is to make clear that the Proposed Rule is designed to support those BCM/DR procedures and to address circumstances that may be exogenous to DTC and not necessarily addressed by the BCM/DR procedures. Finally, the R&W Plan would describe that, because the operation of the Proposed Rule is specific to each applicable Market Disruption Event, the Proposed Rule does not define a time limit on its application. However, the R&W Plan would note that actions authorized by the Proposed Rule would be limited to the pendency of the applicable Market Disruption Event, as made clear in the Proposed Rule. DTC states that, overall, the Proposed Rule is designed to mitigate risks caused by Market Disruption Events and, thereby, minimize the risk of financial loss that may result from such events.

### (iii) Recovery Tool Characteristics

The Recovery Plan would describe DTC's evaluation of the tools identified within the Recovery Plan, and its rationale for concluding that such tools are comprehensive, effective, and transparent, and that such tools provide incentives to Participants and minimize negative impact on Participants and the financial system.

### 3. DTC Wind-Down Plan

The Wind-down Plan would provide the framework and strategy for the orderly wind-down of DTC if the use of the recovery tools described in the Recovery Plan do not successfully return DTC to financial viability. DTC states that, while DTC believes that such event is extremely unlikely, given the comprehensive nature of the recovery tools, DTC is proposing a wind-down strategy that provides for (1) the transfer of DTC's business, assets, securities inventory, and membership to another legal entity, (2) such transfer being effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code,<sup>36</sup> and (3) after effectuating this transfer, DTC

liquidating any remaining assets in an orderly manner in bankruptcy proceedings. DTC states that the proposed transfer approach to a wind-down would meet its objectives of (1) assuring that DTC's critical services will be available to the market as long as there are Participants in good standing, and (2) minimizing disruption to the operations of Participants and financial markets generally that might be caused by DTC's failure.

In describing the transfer approach to DTC's Wind-down Plan, the R&W Plan would identify the factors that DTC considered in developing this approach, including the fact that DTC does not own material assets that are unrelated to its clearance and settlement activities. Therefore, a business reorganization or "bail-in" of debt approach would be unlikely to mitigate significant losses. Additionally, DTC states that its approach was developed in consideration of its critical and unique position in the U.S. markets, which precludes any approach that would cause DTC's critical services to no longer be available.

First, the Wind-down Plan would describe the potential scenarios that could lead to the wind-down of DTC, and the likelihood of such scenarios. The Wind-down Plan would identify the time period leading up to a decision to wind-down DTC as the Runway Period. DTC states that this period would follow the implementation of any recovery tools, as it may take a period of time, depending on the severity of the market stress at that time, for these tools to be effective or for DTC to realize a loss sufficient to cause it to be unable to borrow to complete settlement and to repay such borrowings.<sup>37</sup> The Wind-down Plan would identify some of the indicators that DTC has entered the Runway Period.

The trigger for implementing the Wind-down Plan would be a determination by the Board that recovery efforts have not been, or are unlikely to be, successful in returning DTC to viability as a going concern. As described in the R&W Plan, DTC states that this is an appropriate trigger because it is both broad and flexible enough to cover a variety of scenarios, and would align incentives of DTC and Participants to avoid actions that might undermine DTC's recovery efforts.

<sup>37</sup> The Wind-down Plan would state that, given DTC's position as a user-governed financial market utility, it is possible that its Participants might voluntarily elect to provide additional support during the recovery phase leading up to a potential trigger of the Wind-down Plan, but would also be designed to make clear that DTC cannot predict the willingness of Participants to do so.

<sup>31</sup> See *supra* note 26.

<sup>32</sup> See *supra* note 26.

<sup>33</sup> See *supra* note 9.

<sup>34</sup> See *supra* note 12 (concerning the Capital Policy).

<sup>35</sup> See *supra* note 9.

<sup>36</sup> 11 U.S.C. 101 *et seq.*

Additionally, DTC states that this approach takes into account the characteristics of DTC's recovery tools and enables the Board to consider (1) the presence of indicators of a successful or unsuccessful recovery, and (2) potential for knock-on effects of continued iterative application of DTC's recovery tools.

The Wind-down Plan would describe the general objectives of the transfer strategy, and would address assumptions regarding the transfer of DTC's critical services, business, assets, securities inventory, and membership<sup>38</sup> to another legal entity that is legally, financially, and operationally able to provide DTC's critical services to entities that wish to continue their membership following the transfer ("Transferee"). The Wind-down Plan would provide that the Transferee would be either (1) a third party legal entity, which may be an existing or newly established legal entity or a bridge entity formed to operate the business on an interim basis to enable the business to be transferred subsequently ("Third Party Transferee"); or (2) an existing, debt-free failover legal entity established ex-ante by DTCC ("Failover Transferee") to be used as an alternative Transferee in the event that no viable or preferable Third Party Transferee timely commits to acquire DTC's business. DTC would seek to identify the proposed Transferee, and negotiate and enter into transfer arrangements during the Runway Period and prior to making any filings under Chapter 11 of the U.S. Bankruptcy Code.<sup>39</sup> The Wind-down Plan would anticipate that the transfer to the Transferee, including the transfer and establishment of the Participant and Pledgee securities accounts on the books of the Transferee, be effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code, and pursuant to a bankruptcy court order under Section 363 of the Bankruptcy Code, with the intent that the transfer be free and clear of claims against, and interests in, DTC, except to the extent expressly provided in the court's order.<sup>40</sup>

DTC states that in order to effect a timely transfer of its services and minimize the market and operational disruption of such transfer, DTC would expect to transfer all of its critical

services and any non-critical services that are ancillary and beneficial to a critical service, or that otherwise have substantial user demand from the continuing membership. Given the transfer of the securities inventory and the establishment on the books of the Transferee Participant and Pledgee securities accounts, DTC anticipates that, following the transfer, it would not itself continue to provide any services, critical or not. Following the transfer, the Wind-down Plan would anticipate that the Transferee and its continuing membership would determine whether to continue to provide any transferred non-critical service on an ongoing basis, or terminate the non-critical service following some transition period. DTC's Wind-down Plan would anticipate that the Transferee would enter into a transition services agreement with DTCC so that DTCC would continue to provide the shared services it currently provides to DTC, including staffing, infrastructure and operational support. The Wind-down Plan would also anticipate the assignment of DTC's "inbound" link arrangements to the Transferee. The Wind-down Plan would provide that in the case of "outbound" links, DTC would seek to have the linked FMIs agree, at a minimum, to accept the Transferee as a link party for a transition period.<sup>41</sup>

The Wind-down Plan would provide that, following the effectiveness of the transfer to the Transferee, the wind-down of DTC would involve addressing any residual claims against DTC through the bankruptcy process and liquidating the legal entity. The Wind-down Plan does not contemplate DTC continuing to provide services in any capacity following the transfer time, and any services not transferred would be terminated.

The Wind-down Plan would also identify the key dependencies for the effectiveness of the transfer, which include regulatory approvals that would permit the Transferee to be legally qualified to provide the transferred services from and after the transfer, and approval by the applicable bankruptcy court of, among other things, the

proposed sale, assignments, and transfers to the Transferee.

The Wind-down Plan would address governance matters related to the execution of the transfer of DTC's business and its wind-down. The Wind-down Plan would address the duties of the Board to execute the wind-down of DTC in conformity with (1) the Rules, (2) the Board's fiduciary duties, which mandate that it exercise reasonable business judgment in performing these duties, and (3) DTC's regulatory obligations under the Act as a registered clearing agency. The Wind-down Plan would also identify certain factors the Board may consider in making these decisions, which would include, for example, whether DTC could safely stabilize the business and protect its value without seeking bankruptcy protection, and DTC's ability to continue to meet its regulatory requirements.

The Wind-down Plan would describe (1) actions DTC or DTCC may take to prepare for wind-down in the period before DTC experiences any financial distress, (2) actions DTC would take both during the recovery phase and the Runway Period to prepare for the execution of the Wind-down Plan, and (3) actions DTC would take upon commencement of bankruptcy proceedings to effectuate the Wind-down Plan.

Finally, the Wind-down Plan would include an analysis of the estimated time and costs to effectuate the R&W Plan, and would provide that this estimate be reviewed and approved by the Board annually. In order to estimate the length of time it might take to achieve a recovery or orderly wind-down of DTC's critical operations, as contemplated by the R&W Plan, the Wind-down Plan would include an analysis of the possible sequencing and length of time it might take to complete an orderly wind-down and transfer of critical operations, as described in earlier sections of the R&W Plan. The Wind-down Plan would also include in this analysis consideration of other factors, including the time it might take to complete any further attempts at recovery under the Recovery Plan. The Wind-down Plan would then multiply this estimated length of time by DTC's average monthly operating expenses, including adjustments to account for changes to DTC's profit and expense profile during these circumstances, over the previous twelve months to determine the amount of LNA that it should hold to achieve a recovery or orderly wind-down of DTC's critical operations. The estimated wind-down costs would constitute the Recovery/

<sup>38</sup> Arrangements with FAST Agents and DRS Agents (each as defined in proposed Rule 32(A)) and with Settling Banks would also be assigned to the Transferee, so that the approach would be transparent to issuers and their transfer agents, as well as to Settling Banks.

<sup>39</sup> 11 U.S.C. 101 *et seq.*

<sup>40</sup> See 11 U.S.C. 363.

<sup>41</sup> The proposed transfer arrangements outlined in the Wind-down Plan do not contemplate the transfer of any credit or funding agreements, which are generally not assignable by DTC. However, to the extent the Transferee adopts rules substantially identical to those DTC has in effect prior to the transfer, DTC states that it would have the benefit of any rules-based liquidity funding. The Wind-down Plan contemplates that no Participants Fund would be transferred to the Transferee, as it is not held in a bankruptcy remote manner and it is the primary prefunded liquidity resource to be accessed in the recovery phase.

Wind-down Capital Requirement under the Capital Policy.<sup>42</sup> Under that policy, the General Business Risk Capital Requirement is calculated as the greatest of three estimated amounts, one of which is this Recovery/Wind-down Capital Requirement.<sup>43</sup>

DTC states that the R&W Plan is designed as a roadmap, and the types of actions that may be taken both leading up to and in connection with implementation of the Wind-down Plan would be primarily addressed in other supporting documentation referred to therein.

The Wind-down Plan would address proposed Rule 32(A) (Wind-down of the Corporation), which would be adopted to facilitate the implementation of the Wind-down Plan, as discussed below.

### B. Proposed Rules

In connection with the adoption of the R&W Plan, DTC proposes to adopt the Proposed Rules, each of which is described below. DTC states that the Proposed Rules are designed to facilitate the execution of the R&W Plan and are designed to provide Participants with transparency as to critical aspects of the R&W Plan, particularly as they relate to the rights and responsibilities of both DTC and its Participants. DTC also states that the Proposed Rules are designed to provide a legal basis to these aspects of the R&W Plan.

#### 1. Rule 32(A) (Wind-Down of the Corporation)

DTC states that the proposed Rule 32(A) (“Wind-down Rule”) is designed to facilitate the execution of the Wind-down Plan. The Wind-down Rule would include a proposed set of defined terms that would be applicable only to the provisions of this Proposed Rule. DTC states that the Wind-down Rule is designed to make clear that a wind-down of DTC’s business would occur (1) after a decision is made by the Board, and (2) in connection with the transfer of DTC’s services to a Transferee, as described therein. DTC states that, generally, the proposed Wind-down Rule is designed to create clear mechanisms for the transfer of Eligible Participants and Pledges, Settling Banks, DRS Agents, and FAST Agents (as these terms would be defined in the Wind-down Rule), and DTC’s inventory of financial assets in order to provide for continued access to critical services and to minimize disruption to the markets in the event the Wind-down Plan is initiated.

#### (i) Wind-Down Trigger

First, DTC states that the Proposed Rule is designed to make clear that the Board is responsible for initiating the Wind-down Plan, and would identify the criteria the Board would consider when making this determination. As provided for in the Wind-down Plan and in the proposed Wind-down Rule, the Board would initiate the Wind-down Plan if, in the exercise of its business judgment and subject to its fiduciary duties, it has determined that the execution of the Recovery Plan has not or is not likely to restore DTC to viability as a going concern, and the implementation of the Wind-down Plan, including the transfer of DTC’s business, is in the best interests of DTC, its Participants and Pledges, its shareholders and creditors, and the U.S. financial markets.

#### (ii) Identification of Critical Services; Designation of Dates and Times for Specific Actions

The Proposed Rule would provide that, upon making a determination to initiate the Wind-down Plan, the Board would identify the critical and non-critical services that would be transferred to the Transferee at the Transfer Time (as defined in the Proposed Rule), as well as any non-critical services that would not be transferred to the Transferee. The proposed Wind-down Rule would establish that any services transferred to the Transferee will only be provided by the Transferee as of the Transfer Time, and that any non-critical services that are not transferred to the Transferee would be terminated at the Transfer Time. The Proposed Rule would also provide that the Board would establish (1) an effective time for the transfer of DTC’s business to a Transferee (“Transfer Time”), and (2) the last day that instructions in respect of securities and other financial products may be effectuated through the facilities of DTC (the “Last Activity Date”). DTC states that the Proposed Rule is designed to make clear that DTC would not accept any transactions for settlement after the Last Activity Date. Any transactions to be settled after the Transfer Time would be required to be submitted to the Transferee, and would not be DTC’s responsibility.

#### (iii) Notice Provisions

The proposed Wind-down Rule would provide that, upon a decision to implement the Wind-down Plan, DTC would provide its Participants, Pledges, DRS Agents, FAST Agents, Settling Banks and regulators with a

notice that includes material information relating to the Wind-down Plan and the anticipated transfer of DTC’s Participants and business, including, for example, (1) a brief statement of the reasons for the decision to implement the Wind-down Plan; (2) identification of the Transferee and information regarding the transaction by which the transfer of DTC’s business would be effected; (3) the Transfer Time and Last Activity Date; and (4) identification of Participants and the critical and non-critical services that would be transferred to the Transferee at the Transfer Time, as well as those Non-Eligible Participants (as defined below and in the Proposed Rule) and any non-critical services that would not be included in the transfer. DTC would also make available the rules and procedures and membership agreements of the Transferee.

#### (iv) Transfer of Membership

The proposed Wind-down Rule would address the expected transfer of DTC’s membership to the Transferee, which DTC would seek to effectuate by entering into an arrangement with a Failover Transferee, or by using commercially reasonable efforts to enter into such an arrangement with a Third Party Transferee. Thus, under the proposal, in connection with the implementation of the Wind-down Plan and with no further action required by any party:

(1) Each Eligible Participant would become (i) a Participant of the Transferee and (ii) a party to a Participants agreement with the Transferee;

(2) each Participant that is delinquent in the performance of any obligation to DTC or that has provided notice of its election to withdraw as a Participant (a “Non-Eligible Participant”) as of the Transfer Time would become (i) the holder of a transition period securities account maintained by the Transferee on its books (“Transition Period Securities Account”) and (ii) a party to a Transition Period Securities Account agreement of the Transferee;

(3) each Pledgee would become (i) a Pledgee of the Transferee and (ii) a party to a Pledgee agreement with the Transferee;

(4) each DRS Agent would become (i) a DRS Agent of the Transferee and (ii) a party to a DRS Agent agreement with the Transferee;

(5) each FAST Agent would become (i) a FAST Agent of the Transferee and (ii) a party to a FAST Agent agreement with the Transferee; and

(6) each Settling Bank for Participants and Pledges would become (i) a

<sup>42</sup> See *supra* note 12.

<sup>43</sup> See *supra* note 12.

Settling Bank for Participants and Pledges of the Transferee and (ii) a party to a Settling Bank Agreement with the Transferee.

Further, DTC states that the Proposed Rule is designed to make clear that it would not prohibit (1) Non-Eligible Participants from applying for membership with the Transferee, (2) Non-Eligible Participants that have become holders of Transition Period Securities Accounts (“Transition Period Securities Account Holders”) of the Transferee from withdrawing as a Transition Period Securities Account Holder from the Transferee, subject to the rules and procedures of the Transferee, and (3) Participants, Pledges, DRS Agents, FAST Agents, and Settling Banks that would be transferred to the Transferee from withdrawing from membership with the Transferee, subject to the rules and procedures of the Transferee. Under the Proposed Rule, Non-Eligible Participants that have become Transition Period Securities Account Holders of the Transferee shall have the rights and be subject to the obligations of Transition Period Securities Account Holders set forth in special provisions of the rules and procedures of the Transferee applicable to such Transition Period Securities Account Holder. Specifically, Non-Eligible Participants that become Transition Period Securities Account Holders must, within the Transition Period (as defined in the Proposed Rule), instruct the Transferee to transfer the financial assets credited to its Transition Period Securities Account (i) to a Participant of the Transferee through the facilities of the Transferee or (ii) to a recipient outside the facilities of the Transferee, and no additional financial assets may be delivered versus payment to a Transition Period Securities Account during the Transition Period.

(v) Transfer of Inventory of Financial Assets

The proposed Wind-down Rule would provide that DTC would enter into arrangements with a Failover Transferee, or would use commercially reasonable efforts to enter into arrangements with a Third Party Transferee, providing that, in either case, at Transfer Time:

(1) DTC would transfer to the Transferee (i) its rights with respect to its nominee Cede & Co. (“Cede”) (and thereby its rights with respect to the financial assets owned of record by Cede), (ii) the financial assets held by it at the FRBNY, (iii) the financial assets held by it at other CSDs, (iv) the financial assets held in custody for it

with FAST Agents, (v) the financial assets held in custody for it with other custodians and (vi) the financial assets it holds in physical custody.

(2) The Transferee would establish security entitlements on its books for Eligible Participants of DTC that become Participants of the Transferee that replicate the security entitlements that DTC maintained on its books immediately prior to the Transfer Time for such Eligible Participants, and DTC would simultaneously eliminate such security entitlements from its books.

(3) The Transferee would establish security entitlements on its books for Non-Eligible Participants of DTC that become Transition Period Securities Account Holders of the Transferee that replicate the security entitlements that DTC maintained on its books immediately prior to the Transfer Time for such Non-Eligible Participants, and DTC would simultaneously eliminate such security entitlements from its books.

(4) The Transferee would establish pledges on its books in favor of Pledges that become Pledges of the Transferee that replicate the pledges that DTC maintained on its books immediately prior to the Transfer Time in favor of such Pledges, and DTC shall simultaneously eliminate such pledges from its books.

(vi) Comparability Period

DTC states that the proposed automatic mechanism for the transfer of DTC’s membership is intended to provide DTC’s membership with continuous access to critical services in the event of DTC’s wind-down, and to facilitate the continued prompt and accurate clearance and settlement of securities transactions. The proposed Wind-down Rule would provide that DTC would enter into arrangements with a Failover Transferee, or would use commercially reasonable efforts to enter into arrangements with a Third Party Transferee, providing that, in either case, with respect to the critical services and any non-critical services that are transferred from DTC to the Transferee, for at least a period of time to be agreed upon (“Comparability Period”), the business transferred from DTC to the Transferee would be operated in a manner that is comparable to the manner in which the business was previously operated by DTC.

Specifically, the proposed Wind-down Rule would provide that: (1) The rules of the Transferee and terms of Participant, Pledge, DRS Agent, FAST Agent and Settling Bank agreements would be comparable in substance and effect to the analogous Rules and

agreements of DTC, (2) the rights and obligations of any Participants, Pledges, DRS Agents, FAST Agents, and Settling Banks that are transferred to the Transferee would be comparable in substance and effect to their rights and obligations as to DTC, and (3) the Transferee would operate the transferred business and provide any services that are transferred in a comparable manner to which such services were provided by DTC.

DTC states that the purpose of these provisions and the intended effect of the proposed Wind-down Rule is to facilitate a smooth transition of DTC’s business to a Transferee and to provide that, for at least the Comparability Period, the Transferee (1) would operate the transferred business in a manner that is comparable in substance and effect to the manner in which the business was operated by DTC, and (2) would not require sudden and disruptive changes in the systems, operations and business practices of the new Participants, Pledges, DRS Agents, FAST Agents, and Settling Banks of the Transferee.

(vii) Subordination of Claims Provisions and Miscellaneous Matters

The proposed Wind-down Rule would include a provision addressing the subordination of unsecured claims against DTC of its Participants who fail to participate in DTC’s recovery efforts (*i.e.*, firms delinquent in their obligations to DTC or elect to retire from DTC in order to minimize their obligations with respect to the allocation of losses, pursuant to the Rules). DTC states that this provision is designed to incentivize Participants to participate in DTC’s recovery efforts.<sup>44</sup>

The proposed Wind-down Rule would address other ex-ante matters, including provisions providing that its Participants, Pledges, DRS Agents, FAST Agents and Settling Banks (1) will assist and cooperate with DTC to effectuate the transfer of DTC’s business to a Transferee, (2) consent to the provisions of the rule, and (3) grant DTC power of attorney to execute and deliver on their behalf documents and instruments that may be requested by the Transferee. Finally, the Proposed Rule would include a limitation of liability for any actions taken or omitted

<sup>44</sup> Nothing in the proposed Wind-down Rule would seek to prevent a Participant that retired its membership at DTC from applying for membership with the Transferee. Once its DTC membership is terminated, however, such firm would not be able to benefit from the membership assignment that would be effected by this proposed Wind-down Rule, and it would have to apply for membership directly with the Transferee, subject to its membership application and review process.

to be taken by DTC pursuant to the Proposed Rule.

DTC states that the purpose of the limitation of liability is to facilitate and protect DTC's ability to act expeditiously in response to extraordinary events. Such limitation of liability would be available only following triggering of the Wind-down Plan. In addition, and as a separate matter, DTC states that the limitation of liability provides Participants with transparency for the unlikely situation when those extraordinary events could occur, as well as supporting the legal framework within which DTC would take such actions. DTC states that these provisions, collectively, are designed to enable DTC to take such acts as the Board determines necessary to effectuate an orderly transfer and wind-down of its business should recovery efforts prove unsuccessful.

## 2. Rule 38 (Market Disruption and Force Majeure)

The proposed Rule 38 ("Force Majeure Rule") would address DTC's authority to take certain actions upon the occurrence, and during the pendency, of a Market Disruption Event, as defined therein. DTC states that the Proposed Rule is designed to clarify DTC's ability to take actions to address extraordinary events outside of the control of DTC and of its membership, and to mitigate the effect of such events by facilitating the continuity of services (or, if deemed necessary, the temporary suspension of services). To that end, under the proposed Force Majeure Rule, DTC would be entitled, during the pendency of a Market Disruption Event, to (1) suspend the provision of any or all services, and (2) take, or refrain from taking, or require its Participants and Pledges to take, or refrain from taking, any actions it considers appropriate to address, alleviate, or mitigate the event and facilitate the continuation of DTC's services as may be practicable.

The proposed Force Majeure Rule would identify the events or circumstances that would be considered a Market Disruption Event. The proposed Force Majeure Rule would define the governance procedures for how DTC would determine whether, and how, to implement the provisions of the rule. A determination that a Market Disruption Event has occurred would generally be made by the Board, but the Proposed Rule would provide for limited, interim delegation of authority to a specified officer or management committee if the Board would not be able to take timely action. In the event such delegated authority is exercised, the proposed Force Majeure

Rule would require that the Board be convened as promptly as practicable, no later than five Business Days after such determination has been made, to ratify, modify, or rescind the action. The proposed Force Majeure Rule would also provide for prompt notification to the Commission, and advance consultation with Commission staff, when practicable, including notification when an event is no longer continuing and the relevant actions are terminated. The Proposed Rule would require Participants and Pledges to notify DTC immediately upon becoming aware of a Market Disruption Event, and, likewise, would require DTC to notify its Participants and Pledges if it has triggered the Proposed Rule and of actions taken or intended to be taken thereunder.

Finally, the Proposed Rule would address other related matters, including a limitation of liability for any failure or delay in performance, in whole or in part, arising out of the Market Disruption Event. DTC states that the purpose of the limitation of liability would be similar to the purpose of the analogous provision in the proposed Wind-down Rule, which is to facilitate and protect DTC's ability to act expeditiously in response to extraordinary events.

## II. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act<sup>45</sup> directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. After careful review, the Commission finds that the Proposed Rule Change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to DTC. In particular, the Commission finds that the Proposed Rule Change is consistent with Section 17A(b)(3)(F) of the Act,<sup>46</sup> Rules 17Ad-22(e)(2)(i), (iii), and (v) under the Act,<sup>47</sup> Rule 17Ad-22(e)(3)(ii) under the Act,<sup>48</sup> and Rules 17Ad-22(e)(15)(i) and (ii) under the Act.<sup>49</sup>

### A. Consistency With Section 17A(b)(3)(F) of the Act

Section 17A(b)(3)(F) of the Act requires, in part, that a registered clearing agency have rules designed to

promote the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible.<sup>50</sup>

First, the Commission believes that the R&W Plan, generally, is designed to help DTC promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds which are in the custody or control of DTC or for which it is responsible by providing DTC with a roadmap for actions it may employ to monitor and manage its risks, and, as needed, to stabilize its financial condition in the event those risks materialize. Specifically, as described above, the Recovery Plan would establish a number of triggers for the potential application of a number of recovery tools described in the Recovery Plan. The Commission believes that establishing such triggers alongside a list of available recovery tools would help DTC to more promptly determine when and how it may need to manage a significant stress event, and, as needed, stabilize its financial condition.

Similarly, the Force Majeure Rule is designed to provide a roadmap to address extraordinary events that may occur outside of DTC's control. Specifically, as described above, the Force Majeure Rule would define a Market Disruption Event and provide governance around determining when such an event has occurred. The Force Majeure Rule also would describe DTC's authority to take actions during the pendency of a Market Disruption Event that it deems appropriate to address such an event and facilitate the continuation of DTC's services, if practicable. By defining a Market Disruption Event and providing such governance and authority, the Commission believes that the Force Majeure Rule would help DTC improve its ability to identify and manage a force majeure event, and, as needed, to stabilize its financial condition so that DTC can continue to operate.

The Commission believes that the Recovery Plan and the Force Majeure Rule would allow for a more considered and comprehensive evaluation by DTC of a stressed market situation and the ways in which DTC could apply available recovery tools in a manner intended to minimize the potential negative effects of the stress situation for DTC, its membership, and the broader financial system. Therefore, the

<sup>45</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>46</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>47</sup> 17 CFR 240.17Ad-22(e)(2)(i), (iii), and (v).

<sup>48</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>49</sup> 17 CFR 240.17Ad-22(e)(15)(i) and (ii).

<sup>50</sup> 15 U.S.C. 78q-1(b)(3)(F).

Commission believes that the Recovery Plan and the Force Majeure Rule are designed to help DTC promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds which are in the custody or control of DTC or for which it is responsible by establishing a means for DTC to best determine the most appropriate way to address such stress situations in an effective manner.

Second, the Commission believes that the R&W Plan, generally, is designed to help DTC to promote the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds which are in the custody or control of DTC or for which it is responsible by providing a roadmap to wind-down that is designed to ensure the availability of DTC's critical services to the marketplace, while reducing disruption to the operations of Participants and financial markets that might be caused by DTC's failure. Specifically, as described above, the Wind-down Plan, as facilitated by the Wind-down Rule, would provide for the wind-down of DTC's business and transfer of membership and critical services if the recovery tools do not successfully return DTC to financial viability. Accordingly, critical services, such as services that lack alternative providers or products as well as services that are interconnected with other participants and processes within the U.S. financial system would be able to continue in an orderly manner while DTC is seeking to wind-down its services. By designing the Wind-down Plan and the Wind-down Rule to enable the continuity of DTC's critical services and membership in an orderly manner while DTC is seeking to wind-down its services, the Commission believes these proposed changes would help DTC to promote the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds which are in the custody or control of DTC or for which it is responsible in the event the Wind-down Plan is implemented.

By better enabling DTC to promote the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds which are in the custody or control of DTC or for which it is responsible, as described above, the Commission finds that the Proposed Rule Change is consistent with Section 17A(b)(3)(F) of the Act.<sup>51</sup>

<sup>51</sup> 15 U.S.C. 78q-1(b)(3)(F).

### *B. Consistency With Rules 17Ad-22(e)(2)(i), (iii), and (v) Under the Act*

Rule 17Ad-22(e)(2)(i) under the Act requires a covered clearing agency<sup>52</sup> to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that are clear and transparent.<sup>53</sup> Rule 17Ad-22(e)(2)(iii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that support the public interest requirements in Section 17A of the Act<sup>54</sup> applicable to clearing agencies, and the objectives of owners and participants.<sup>55</sup> Rule 17Ad-22(e)(2)(v) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that specify clear and direct lines of responsibility.<sup>56</sup>

As described above, the R&W Plan is designed to identify clear lines of responsibility concerning the R&W Plan including (1) the ongoing development of the R&W Plan; (2) ongoing maintenance of the R&W Plan; (3) reviews and approval of the R&W Plan; and (4) the functioning and implementation of the R&W Plan. As described above, the R&R Team, which reports to the Management Committee, is responsible for maintaining the R&W Plan and for the development and ongoing maintenance of the overall recovery and wind-down planning process. Meanwhile, the Board, or such committees as may be delegated authority by the Board from time to time pursuant to its charter, would review and approve the R&W Plan biennially, and also would review and approve any changes that are proposed to the R&W Plan outside of the biennial review. Moreover, the R&W Plan would state the stages of escalation required to manage recovery under the Recovery Plan or to

<sup>52</sup> A "covered clearing agency" means, among other things, a clearing agency registered with the Commission under Section 17A of the Exchange Act (15 U.S.C. 78q-1 *et seq.*) that is designated systemically important by the Financial Stability Oversight Counsel ("FSOC") pursuant to the Clearing Supervision Act (12 U.S.C. 5461 *et seq.*). See 17 CFR 240.17Ad-22(a)(5)-(6). On July 18, 2012, FSOC designated DTC as systemically important. U.S. Department of the Treasury, "FSOC Makes First Designations in Effort to Protect Against Future Financial Crises," available at <https://www.treasury.gov/press-center/press-releases/Pages/tg1645.aspx>. Therefore, DTC is a covered clearing agency.

<sup>53</sup> 17 CFR 240.17Ad-22(e)(2)(i).

<sup>54</sup> 15 U.S.C. 78q-1.

<sup>55</sup> 17 CFR 240.17Ad-22(e)(2)(iii).

<sup>56</sup> 17 CFR 240.17Ad-22(e)(2)(v).

invoke DTC's wind-down under the Wind-down Plan, which would range from relevant business line managers up to the Board. The R&W Plan would identify the parties responsible for certain activities under both the Recovery Plan and the Wind-down Plan, and would describe their respective roles. The R&W Plan also would specify the process DTC would take to receive input from various parties at DTC, including management committees and the Board.

In considering the above, the Commission believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that are clear and transparent because it would specify lines of control. The Commission also believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that support the public interest requirements in Section 17A of the Act<sup>57</sup> applicable to clearing agencies, and the objectives of owners and participants because the R&W Plan specifies the process DTC would take to receive input from various DTC stakeholders. In addition, the Commission believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that specify clear and direct lines of responsibility because it specifies who is responsible for the ongoing development, maintenance, reviews, approval, functioning, and implementation of the R&W Plan.

Therefore, the Commission finds that the R&W Plan is consistent with Rules 17Ad-22(e)(2)(i), (iii), and (v) under the Act.<sup>58</sup>

### *C. Consistency With Rule 17Ad-22(e)(3)(ii) Under the Act*

Rule 17Ad-22(e)(3)(ii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the covered clearing agency, which includes plans

<sup>57</sup> 15 U.S.C. 78q-1.

<sup>58</sup> 17 CFR 240.17Ad-22(e)(2)(i), (iii), and (v).

for the recovery and orderly wind-down of the covered clearing agency necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.<sup>59</sup>

As described above, the R&W Plan's Recovery Plan provides a plan for DTC's recovery necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses by defining the risk management activities, stress conditions and indicators, and tools that DTC may use to address stress scenarios that could eventually prevent DTC from being able to provide its critical services as a going concern. More specifically, through the framework of the Crisis Continuum, which identifies tools that can be employed to mitigate losses and mitigate or minimize liquidity needs as the market environment becomes increasingly stressed, the Recovery Plan would identify measures that DTC may take to manage risks of credit losses and liquidity shortfalls, and other losses that could arise from a Participant Default. The Recovery Plan also would address DTC's management of general business risks and other non-default risks that could lead to losses by identifying potential non-default losses and the resources available to DTC to address such losses, including recovery triggers and tools to mitigate such losses. Therefore, the Commission believes that the R&W Plan's Recovery Plan helps DTC establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by DTC, which includes a recovery plan necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.

As described above, the R&W Plan's Wind-down Plan provides a plan for orderly wind-down of DTC, which would be triggered by a determination by the Board that recovery efforts have not been, or are unlikely to be, successful in returning DTC to viability as a going concern. Once triggered, the Wind-down Plan sets forth mechanisms for the transfer of DTC's membership and business, and it is designed to maintain continued access to DTC's critical services and to minimize market impact of the transfer while DTC is seeking to ultimately wind-down its services. Specifically, the Wind-down Plan would provide for the transfer of

DTC's business, assets, securities inventory, and membership to another legal entity with such transfer being effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code.<sup>60</sup> After effectuating this transfer, DTC would liquidate any remaining assets in an orderly manner in bankruptcy proceedings.

Although the Commission is not opining on the Wind-down Plan's consistency with the U.S. Bankruptcy Code, in reviewing the proposed changes, the Commission believes that DTC's intent to use bankruptcy proceedings to achieve an orderly liquidation of assets after any transfer of DTC's business appears reasonable, in light of the provisions of the Bankruptcy Code that address the liquidation and distribution of a debtor's property among creditors and interest holders.<sup>61</sup> Under many circumstances, Section 363 of the Bankruptcy Code provides for the sale of property "free and clear of any interest in such property of an entity other than the estate[.]"<sup>62</sup> The Commission believes that DTC's analysis regarding the applicability of these provisions, while not free from doubt, presents a reasonable approach to liquidation in light of the circumstances and the available alternatives.<sup>63</sup> Therefore, the Commission believes that the R&W Plan's Wind-down Plan helps DTC establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by DTC, which includes a wind-down plan necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.

Therefore, the Commission finds that the R&W Plan is consistent with Rule 17Ad-22(e)(3)(ii) under the Act.<sup>64</sup>

#### *D. Consistency With Rules 17Ad-22(e)(15)(i)-(ii) Under the Act*

Rule 17Ad-22(e)(15)(i) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures

reasonably designed to identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that the covered clearing agency can continue operations and services as a going concern if those losses materialize, including by determining the amount of liquid net assets funded by equity based upon its general business risk profile and the length of time required to achieve a recovery or orderly wind-down, as appropriate, of its critical operations and services if such action is taken.<sup>65</sup> Rule 17Ad-22(e)(15)(ii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that the covered clearing agency can continue operations and services as a going concern if those losses materialize, including by holding liquid net assets funded by equity equal to the greater of either (x) six months of the covered clearing agency's current operating expenses, or (y) the amount determined by the board of directors to be sufficient to ensure a recovery or orderly wind-down of critical operations and services of the covered clearing agency, as contemplated by the plans established under Rule 17Ad-22(e)(3)(ii) under the Act,<sup>66</sup> discussed above.<sup>67</sup>

As discussed above, DTC's Capital Policy is designed to address how DTC holds LNA in compliance with these requirements,<sup>68</sup> while the Wind-down Plan would include an analysis to estimate the amount of time and cost to achieve a recovery or orderly wind-down of DTC's critical operations and services, and would provide that the Board review and approve this analysis and estimation annually. The Wind-down Plan also would provide that the estimate would be the Recovery/Wind-down Capital Requirement under the Capital Policy. Under that policy, the General Business Risk Capital Requirement, which is the amount of LNA that DTC plans to hold to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialize, is calculated as the greatest of three estimated amounts, one of

<sup>60</sup> 11 U.S.C. 101 *et seq.*

<sup>61</sup> *See, e.g.*, 11 U.S.C. 363, 726, and 1129(a)(7).

<sup>62</sup> *See* 11 U.S.C. 363(f).

<sup>63</sup> The Wind-down Plan would identify certain factors the Board may consider in evaluating alternatives, which would include, for example, whether DTC could safely stabilize the business and protect its value without seeking bankruptcy protection, and DTC's ability to continue to meet its regulatory requirements.

<sup>64</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>65</sup> 17 CFR 240.17Ad-22(e)(15)(i).

<sup>66</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>67</sup> 17 CFR 240.17Ad-22(e)(15)(ii).

<sup>68</sup> *Supra* note 12.

<sup>59</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

which is this Recovery/Wind-down Capital Requirement. Therefore, the Commission finds that the R&W Plan is consistent with Rules 17Ad-22(e)(15)(i) and (ii) under the Act.<sup>69</sup>

### III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act<sup>70</sup> and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>71</sup> that proposed rule change SR-DTC-2017-021, as modified by Amendment No. 1, be, and it hereby is, approved<sup>72</sup> as of the date of this order or the date of a notice by the Commission authorizing DTC to implement advance notice SR-DTC-2017-803, as modified by Amendment No. 1, whichever is later.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>73</sup>

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

[FR Doc. 2018-19054 Filed 8-31-18; 8:45 am]

BILLING CODE 8011-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-83971; File No. SR-NSCC-2017-018]

### Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, To Amend the Loss Allocation Rules and Make Other Changes

August 28, 2018.

On December 18, 2017, National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR-NSCC-2017-018 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder<sup>2</sup> to amend its loss allocation rules and make other conforming and technical

changes.<sup>3</sup> The proposed rule change was published for comment in the **Federal Register** on January 8, 2018.<sup>4</sup> On February 8, 2018, the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the proposed rule change.<sup>5</sup> On March 20, 2018, the Commission instituted proceedings to determine whether to approve or

<sup>3</sup> On December 18, 2017, NSCC filed the proposed rule change as advance notice SR-NSCC-2017-806 with the Commission 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”) and Rule 19b-4(n)(1)(i) of the Act (“Advance Notice”). 12 U.S.C. 5465(e)(1) and 17 CFR 240.19b-4(n)(1)(i), respectively. The Advance Notice was published for comment in the **Federal Register** on January 30, 2018. In that publication, the Commission also extended the review period of the Advance Notice for an additional 60 days, pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act. 12 U.S.C. 5465(e)(1)(H); Securities Exchange Act Release No. 82584 (January 24, 2018), 83 FR 4377 (January 30, 2018) (SR-NSCC-2017-806). On April 10, 2018, the Commission required additional information from NSCC pursuant to Section 806(e)(1)(D) of the Clearing Supervision Act, which tolled the Commission’s period of review of the Advance Notice until 60 days from the date the information required by the Commission was received by the Commission. 12 U.S.C. 5465(e)(1)(D); see 12 U.S.C. 5465(e)(1)(E)(ii) and (G)(ii); see Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled “Commission’s Request for Additional Information,” available at <https://www.sec.gov/rules/sro/nscs-an.htm>. On June 28, 2018, NSCC filed Amendment No. 1 to the Advance Notice to amend and replace in its entirety the Advance Notice as originally filed on December 18, 2017, which was published in the **Federal Register** on August 6, 2018. Securities Exchange Act Release No. 83748 (July 31, 2018), 83 FR 38375 (August 6, 2018) (SR-NSCC-2017-806). NSCC submitted a courtesy copy of Amendment No. 1 to the Advance Notice through the Commission’s electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Advance Notice has been publicly available on the Commission’s website at <https://www.sec.gov/rules/sro/nscs-an.htm> since June 29, 2018. On July 6, 2018, the Commission received a response to its request for additional information in consideration of the Advance Notice, which, in turn, added a further 60 days to the review period pursuant to Section 806(e)(1)(E) and (G) of the Clearing Supervision Act. 12 U.S.C. 5465(e)(1)(E) and (G); see Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled “Response to the Commission’s Request for Additional Information,” available at <https://www.sec.gov/rules/sro/nscs-an.htm>. The Commission did not receive any comments. The proposal, as set forth in both the Advance Notice and the proposed rule change, each as modified by Amendments No. 1, shall not take effect until all required regulatory actions are completed.

<sup>4</sup> Securities Exchange Act Release No. 82428 (January 2, 2018), 83 FR 897 (January 8, 2018) (SR-NSCC-2017-018).

<sup>5</sup> Securities Exchange Act Release No. 82670 (February 8, 2018), 83 FR 6626 (February 14, 2018) (SR-DTC-2017-022, SR-FICC-2017-022, SR-NSCC-2017-018).

disapprove the proposed rule change.<sup>6</sup> On June 25, 2018, the Commission designated a longer period for Commission action on the proceedings to determine whether to approve or disapprove the proposed rule change.<sup>7</sup> On June 28, 2018, NSCC filed Amendment No. 1 to the proposed rule change to amend and replace in its entirety the proposed rule change as originally filed on December 18, 2017.<sup>8</sup> The Commission did not receive any comments. This order approves the proposed rule change, as modified by Amendment No. 1 (hereinafter, “Proposed Rule Change”).

### I. Description

The Proposed Rule Change consists of proposed changes to NSCC’s Rules and Procedures (“Rules”)<sup>9</sup> in order to (1) modify the loss allocation process; (2) align NSCC’s loss allocation rule among the three clearing agencies of The Depository Trust & Clearing Corporation (“DTCC”)—The Depository Trust Company (“DTC”), Fixed Income Clearing Corporation (“FICC”) (including the Government Securities Division (“FICC/GSD”) and the Mortgage-Backed Securities Division (“FICC/MBSD”)), and NSCC (collectively, the “DTCC Clearing Agencies”);<sup>10</sup> (3) reduce the time within which NSCC is required to return a former Member’s Clearing Fund deposit; and (4) make conforming and technical changes. Each of these proposed changes is described below. A detailed description of the specific rule text changes proposed in this Advance

<sup>6</sup> Securities Exchange Act Release No. 82910 (March 20, 2018), 83 FR 12968 (March 26, 2018) (SR-NSCC-2017-018).

<sup>7</sup> Securities Exchange Act Release No. 83510 (June 25, 2018), 83 FR 30791 (June 29, 2018) (SR-DTC-2017-022, SR-FICC-2017-022, SR-NSCC-2017-018).

<sup>8</sup> Securities Exchange Act Release No. 83633 (July 13, 2018), 83 FR 34227 (July 19, 2018) (SR-NSCC-2017-018) (“Notice of Amendment No. 1”). NSCC submitted a courtesy copy of Amendment No. 1 to the proposed rule change through the Commission’s electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the proposed rule change has been publicly available on the Commission’s website at <https://www.sec.gov/rules/sro/nscs-an.htm> since June 29, 2018.

<sup>9</sup> Each capitalized term not otherwise defined herein has its respective meaning as set forth in the Rules, available at [http://www.dtcc.com/~media/Files/Downloads/legal/rules/nscs\\_rules.pdf](http://www.dtcc.com/~media/Files/Downloads/legal/rules/nscs_rules.pdf).

<sup>10</sup> DTCC is a user-owned and user-governed holding company and is the parent company of DTC, FICC, and NSCC. DTCC operates on a shared services model with respect to the DTCC Clearing Agencies. Most corporate functions are established and managed on an enterprise-wide basis pursuant to intercompany agreements under which it is generally DTCC that provides a relevant service to a DTCC Clearing Agency.

<sup>69</sup> 17 CFR 240.17Ad-22(e)(15)(i) and (ii).

<sup>70</sup> 15 U.S.C. 78q-1.

<sup>71</sup> 15 U.S.C. 78s(b)(2).

<sup>72</sup> In approving the Proposed Rule Change, the Commission has considered the Proposed Rule Change’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>73</sup> 17 CFR 200.30-3(a)(12).

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

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