

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-52552; File No. SR-NSCC-2005-13)

October 3, 2005

Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Proposed Rule Change to Modify and Consolidate Clearing Fund Rules

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> notice is hereby given that on September 20, 2005, the National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II, and III below, which items have been prepared primarily by NSCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested parties.

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

NSCC is seeking to modify Procedure XV (Clearing Fund Formula and Other Matters) and make related technical changes.

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

In its filing with the Commission, NSCC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NSCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.<sup>2</sup>

---

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

<sup>2</sup> The Commission has modified the text of the summaries prepared by NSCC.

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

1. Clearing Fund Formula Enhancements

NSCC's clearing fund formula consists of a number of components designed to calculate the exposure to NSCC of participants' unsettled portfolios. For CNS and Balance Order transactions, the components include a mark-to-market calculation and a volatility calculation.<sup>3</sup>

The current mark-to-market calculation includes trades that have not yet reached Settlement Date, thus excluding from the calculation trades that have reached T+3 and CNS fail positions (*i.e.*, net positions that did not settle on Settlement Date). NSCC is proposing to enhance the mark-to-market calculation by including trades that have reached Settlement Date and net CNS fail positions to more accurately cover the mark-to-market exposure of participants' unsettled portfolios in the event of an intraday insolvency of a participant. When making this calculation, NSCC may but is not required to take into account securities that a participant has delivered to CNS in the night cycle.

The volatility component of the clearing fund formula rule provides that NSCC may exclude from volatility calculations net unsettled positions in classes of securities whose volatility is either less amenable to statistical analysis such as OTC Pink Sheet issues trading below \$5.00, or amenable to such analysis only in a complex manner such as municipal or corporate bonds. The amount of clearing fund required to satisfy the volatility component for these positions is determined as a percentage haircut (currently 2% for municipal and corporate bonds).

---

<sup>3</sup> The other components for CNS and Balance Order activity are a CNS fail charge, a charge for market maker domination, and special charges.

NSCC is proposing to enhance its volatility formula and replace the 2% haircut for corporate and municipal bonds with a fixed income volatility calculation. NSCC would continue to use a haircut for fixed income securities in circumstances it deems appropriate such as where sufficient market or security information is not available.

## 2. Technical Clarifications

When NSCC revised its clearing fund formula in 2001 to move to a risk-based calculation,<sup>4</sup> it applied the revised formula to participants on a rolling basis. To accommodate this transition, NSCC's rules retained two versions of Addendum B (Standards of Financial Responsibility and Operational Capability) and Procedure XV: Version 1 (non-risk-based) and Version 2 (risk-based). Version 2 is currently located in Appendix 1.

With limited exception, all participants are now subject to the clearing fund provisions of Version 2 of Procedure XV and Version 2 of Addendum B. Accordingly, in order to simplify the rules and enable participants to locate provisions applicable to them more readily, NSCC proposes to restructure its Addendums, Procedures, and Rules.

As Version 1 of Procedure XV now has limited applicability, NSCC is proposing to re-designate this as proposed Version 2 of Procedure XV and move it to Appendix 1. NSCC would retain only those provisions thereof (and of Version 1 of Addendum B<sup>5</sup>) that remain applicable.

---

<sup>4</sup> Securities Exchange Act Release No. 44431 (June 15, 2001), 66 FR 33280.

<sup>5</sup> Both versions of Addendum B are substantially identical, with the exception of certain provisions of current Version 1 relating to the timing for calculating and collecting clearing fund. The substance of those provisions of current Version 1 of Addendum B are added as a note to the current Version 1 of Procedure XV that would be moved to Appendix 1 and would be renamed Version 2. The rest of Version 1 of Addendum B would be deleted. All participants remain subject to the provisions of the current Version 2 of Addendum B, which NSCC is

Because the current Version I of Procedure XV always contained a mark-to-market component, it is also being revised to include in the mark-to-market calculation trades that have reached T+3 and CNS fail positions. The current provisions of Appendix 1 (Version 2 of Procedure XV and Version 2 of Addendum B) would be moved into the body of the rules in place of current Version 1 of Procedure XV and current Version 1 of Addendum B where they would appear in numerical order.

As part of these clarifications, Rule 4 (Clearing Fund) is also being corrected to make clear that participants may request a return of any excess clearing fund on any day that NSCC has determined that the participant's Actual Deposit exceeds its Required Deposit (qualifying bonds would still be valued at their collateral value). Finally, certain technical corrections are proposed to Rule 4 and the clearing fund formula to provide consistent terminology and delete obsolete references.

NSCC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act<sup>6</sup> and the rules and regulations thereunder applicable to NSCC because it will permit NSCC to assure the safeguarding of funds and securities which are in its custody or control or for which it is responsible by allowing NSCC to more precisely identify the risks posed by a participant's unsettled portfolio and, as a result, more quickly adjust and collect additional clearing fund requirements than the current formula. As a result NSCC should be better protected from the possibility of a participant's default because the clearing fund deposits it collects should more accurately reflect NSCC's exposure.

---

proposing to move to the body of its rules from Appendix 1 and rename Version 1.

<sup>6</sup> 15 U.S.C. 78q-1.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NSCC does not believe that the proposed rule change will have any impact or impose any burden on competition.

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

NSCC has not solicited or received any written comments on this proposal. NSCC will notify the Commission of any written comments it receives.

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

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

(A) by order approve such proposed rule change or

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

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an E-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NSCC-2005-13 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NSCC-2005-13. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of NSCC and on NSCC's Web site at [www.nsccl.com/legal](http://www.nsccl.com/legal). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-NSCC-2005-13 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>7</sup>

Jonathan G. Katz  
Secretary

---

<sup>7</sup> 17 CFR 200.30-3(a)(12).