

[Release No. 34-38197; File No. SR-DCC-96-13]

**Self-Regulatory Organizations; Delta Clearing Corp.; Notice of Filing of Proposed Rule Change Amending the Definitions of Trading Limits and Maximum Potential System Exposure**

January 23, 1997.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on November 26, 1996, Delta Clearing Corp. ("DCC") filed with the Securities and Exchange Commission ("Commission") and on January 10, 1997, filed an amendment to the proposed rule change as described in Items I, II, and III below, which items have been prepared primarily by DCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

DCC is proposing amendments to its over the counter options trading system procedures and its procedures for repurchase and reverse repurchase agreements ("repo"). In addition, DCC is proposing to issue a new policy statement 96-02.<sup>2</sup> The amendments would provide DCC greater flexibility to address credit or liquidity difficulties with its participants by providing that DCC would not be obligated to reject a transaction which exceeds a participant's "exposure limits" if DCC determines that the additional risk of such transaction to the system is *de minimis*. The amendments also clarify and limit the circumstances under which margin funds due and owing from participants may be deducted for purposes of determining the "maximum potential system exposure" ("MPSE").

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

In its filing with the Commission, DCC 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. DCC has prepared summaries, set forth in sections (A), (B),

and (C) below, of the most significant aspects of such statements.<sup>3</sup>

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

The proposed rule change amends four DCC's procedures and the issuance of Policy Statement 96-02. First, the term "trading limit" will be changed to "exposure limit." Second, the consequences of a participant exceeding its exposure limit are clarified so that a participant may continue to effect trades for clearance and settlement in the repo clearing system or the options clearing system if DCC determines that the risk involved is *de minimis* (i.e., the additional exposure is less than 5%). The processes for rejecting trades, for notification of the affected participants, and for related matters are described in proposed Policy Statement 96-02. In the event that a participant exceeds its exposure limit twice or more in one month, the revised rule would obligate DCC to review with the participant and the insurer, if necessary, whether to change the participant's exposure limit. These changes would clarify the intent that the scope of DCC's procedures is on the regulation of trade clearance and settlement through DCC's facilities and not on the general trading activities of participants. These changes also would provide greater flexibility to DCC to address credit or liquidity difficulties with its participants. Third, Sections 204 and 2204, and the definitions of "exposure limit" in Section 101 and 2101, are amended to clarify that each participant has one exposure limit applicable to all transactions in the system. Fourth, the definition of MPSE in the procedures is revised to clarify and limit the circumstances under which margin funds due and owing from participants may be deducted for purposes of determining MPSE. Under the proposed amendment, DCC would continue to include as a credit in calculating MPSE those margin funds due and owing from such participants at or before the immediately succeeding settlement time that were called for by DCC in the ordinary course of entering trades into the options or repo clearing systems, that were reflected in the daily margin report and that were not an additional margin requirement pursuant to Section 603 or 2603 of DCC procedures. This clarification should reduce the possibility that margin calls designed to reduce DCC's credit

exposure inadvertently compound that exposure.

DCC believes that the proposed rule change is consistent with Section 17A of the Act and the rules and regulations thereunder applicable to DCC, and in particular with Section 17A(b)(3)(F) of the Act<sup>4</sup> which requires that a clearing agency be organized and its rules be designed, among other things, to promote the prompt and accurate clearance and settlement of securities transactions, to safeguard funds and securities in DCC's possession and control, and to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions. DCC believes the proposed rule change will permit wider utilization of the system by providing greater flexibility to address credit or liquidity difficulties with its participants.

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

DCC does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

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

Written comments were neither solicited nor received.

**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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street N.W.,

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

<sup>2</sup> Policy Statement 96-02, which describes the remedial steps DCC will take to correct a participant's violation of its exposure limits is attached as Exhibit A to this notice.

<sup>3</sup> The Commission has modified parts of these statements.

<sup>4</sup> 15 U.S.C. 78q-1(b)(3)(F).

Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room in Washington, D.C. Copies of such filing will also be available for inspection and copying at the principal office of DCC. All submissions should refer to the file number SR-DCC-96-13 and should be submitted by February 20, 1997.

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

Margaret H. McFarland,  
Deputy Secretary.

#### Policy Statement 96-02

#### Exposure Limit Violations; Corrective Action Steps

##### Introduction

The purpose of this Policy Statement is to describe the remedial steps risk management and clearing personnel will take to correct a Participant's violation of such Participant's Exposure Limit. All capitalized terms, unless the context otherwise requires, shall have the meanings set forth in the Procedures for Option Contracts and Procedures for Repurchase and Reverse Repurchase Agreements ("Repos"). The Participant's Exposure Limit is prescribed at the time such Participant's is admitted to the System based on a credit and liquidity analysis of the Participant by Risk Management personnel in consultation with CapMac and may be changed from time to time at the direction of risk management personnel and in consultation with CapMac. An Exposure Limit represents the aggregate incremental margin which may be due from a Participant for a prospective Business Day one Business Day hence as a consequence of such Participant's net Short Positions and Exercised Options with respect to Option Contracts and net Long and/or Short Positions with respect to Repos.

Each day, before accepting trades for submission in the clearing systems, Delta will determine whether a Participant's potential incremental margin due with respect to positions and trades exceeds each Participant's pre-set Exposure Limit." Such Exposure

Limit is the mathematical net of the exposure derived from Option Contracts and Repos. Risk management shall be delegated with the authority to monitor each Participant's compliance with remaining at or below such Participant's assigned Exposure Limit. In the event a Participant exceeds their assigned Exposure Limit, risk management personnel shall be responsible for taking remedial action to correct such violation.

##### Remedial Steps

Risk management personnel shall take the following sequential steps to address and/or correct a violation of a prescribed Exposure Limit:

1. Determine that a violation has taken place by first, reviewing the Participant's open positions and second, by comparing the effect any newly executed positions may have on such previously outstanding open positions.

2. Previously open positions may exacerbate the Exposure Limit violation due to market changes in the securities underlying such open positions or, alternatively, market changes with respect to such open positions may have ameliorated the effect of the Exposure Limit violation.

3. After determining the effect of market changes on open positions, risk management personnel shall determine the residual magnitude of the remaining excess, if any, over the Participant's Exposure Limit.

4. Risk management personnel shall determine if the Participant has maintained any excess margin in such Participant's Account. Such excess margin may take the form of collateral held and not yet returned to such Participant at the request of such Participant. In the event such Participant has maintained such excess margin, risk management shall determine whether such excess margin is sufficient to cover the Exposure Limit violation.

5. In the event there is no excess margin, risk management personnel shall determine whether the magnitude of the violation is material or *de minimus*. As a general matter, a *de minimus* violation shall be construed to be 5% or less of such Participant's Exposure Limit.

6. If the violation is determined to be *de minimus*, no further remedial action is required. If the violation is determined to be material (i.e. in excess of 5% of such Participant's Exposure Limit), then further remedial action is required. If a *de minimus* exposure limit occurs more than twice within thirty days, Risk Management Personnel will

consider whether to change the Exposure Limit.

7. Risk management personnel are authorized to inform the Participant that such Participant may not submit any additional transactions unless such transactions have the effect of reducing such Participant's Exposure Limit. In addition, risk management personnel are authorized and shall request intra-day margin from the Participant. In the event intra-day margin is not forthcoming, risk management personnel are authorized to reject transactions which resulted in the Participant exceeding their Exposure Limit which are otherwise not liquidating transactions. Risk management personnel shall inform the Participant subject to the Exposure Limit violation that no additional transactions may be submitted by such Participant, unless such transactions have the effect of reducing or eliminating the violation. Risk management personnel shall also inform Authorized Brokers that all transaction effected by the violation Participant shall be rejected unless such transactions have the effect of reducing or eliminating the violation until further notice. Accordingly, each such transaction effected by an Authorized Broker shall be reviewed on a trade by trade basis.

8. In the interests of minimizing the financial impact on Participants, including those Participants in good standing who have executed transactions opposite a Participant subject to an Exposure Limit Violation, risk management personnel shall first reject the most recently executed but not yet settled forward start Repo trades. In the event the Participant has not effected any unsettled forward start Repo trades or the rejection of such trades does not result in the elimination of the Exposure Limit violation, risk management shall then reject all Option Contract transactions executed during the current business Day. Risk management personnel shall promptly contact other Participant, including Authorized Brokers, in order to identify a replacement party for the Participant subject to the Exposure Limit violation. Such replacement Participant assume the rejected transactions on the terms under which the trade was originally executed. In the event a replacement Participant cannot be identified, risk management personnel shall be authorized to contact the executing counterparty opposite the Participant subject to an Exposure Limit violation and inform such executing counterparty that the subject transaction has been rejected for clearance.

9. In the event the rejection of forward start Repo trades and current Business Day Option Contact trades are insufficient to eliminate the Exposure Limit violation, risk management personnel shall be authorized to create a Liquidating Settlement Account for such Participant. Upon the creation of such an account, risk management personnel shall begin the process of closing such Participant's outstanding positions. Such authority to initiate the liquidation process is predicated on the Participant's inability or unwillingness to affirmatively respond to a previously executed intra-day margin call pursuant to the Procedures.

[FR Doc. 97-2259 Filed 1-29-97; 8:45 am]  
BILLING CODE 8010-01-M

[Release No. 34-38198; File No. SR-DCC-96-12]

**Self-Regulatory Organizations; Delta Clearing Corp.; Notice of Filing of a Proposed Rule Change to Amend Procedures Relating to Monitoring and Limiting Exposure From Repurchase Agreements**

January 23, 1997.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on November 26, 1996, the Delta Clearing Corp. ("DCC") filed with the Securities and Exchange Commission ("Commission") and on January 10, 1997, amended the proposed rule change (File No. SR-DCC-96-12) as described in Items I, II, and III below, which items have been prepared primarily by DCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

DCC is proposing to amend the margining of overnight repurchase agreements ("repos"). DCC's policy statement 96-01, attached as Exhibit 1 to this notice, describes the proposed amendments in greater detail.

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

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

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

The purpose of the proposed rule change is to amend DCC's procedures for monitoring and limiting its exposure from the clearance and settlement of its participants' overnight repos. First, the proposed rule change will establish DCC's participants' core margin requirement as either \$1 million dollars par amount of U.S. Treasury securities or a greater amount as determined by DCC based upon exposures arising out of overnight repo agreements effected by the participant.<sup>2</sup> DCC will calculate weekly the core margin requirement for each participant by using the most recent eight weeks (if available) of overnight repo transactions and will notify each participant of its core margin requirement. If DCC notifies a participant that the participant is required to deposit additional core margin, the participant by 11 a.m. on the business day following the notice must deposit with DCC's clearing bank U.S. Treasury securities whose market value equals or exceeds the participant's additional margin requirement.

Second, the proposed rule change will amend Section 2602 of DCC's rules to require DCC to provide each participant with a supplemental daily margin report by 3 p.m. of each business day. The supplemental daily margin report will indicate (i) the participant's overnight repo positions established during that business day, (ii) the net mark-to-market valuations for the participant's overnight repo positions,<sup>3</sup> (iii) the core margin and excess unreturned margin on deposit, and (iv) the amount of additional margin that the participant must deposit with DCC's clearing bank. In the event that the net mark-to-market valuation exceeds 65% of the sum of the participant's core requirement and unreturned margin on deposit, DCC will

<sup>2</sup> Overnight repos will be defined as repo agreements whose off-date is the immediately succeeding business day following the on-date for such transactions. Term repos will be defined as repos agreements whose off-date is two or more business days following the on-date for such transactions.

<sup>3</sup> Net mark-to-market means the arithmetic sum resulting from the estimated cost to liquidate a participant's under margined positions in overnight repos offset by the estimated proceeds from liquidating a participant's over margined positions in overnight repos.

require the participant to deposit additional margin in the amount of such excess. The additional margin must be deposited with DCC no later than 5 p.m. of that business day. Failure to deposit the amount of any margin deficit shown on the supplemental daily margin report will be grounds for suspension and sanctions pursuant to Section 2608 of DCC's rules.

Third, the proposed rule change will amend DCC's rules to eliminate the collection of performance margin for overnight repos. The daily margin report will reflect only the margin required on the participant's term repo positions.

DCC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act<sup>4</sup> and the rules and regulations thereunder because the proposed rule change will better enable DCC to safeguard the funds and securities under its possession and control by amending DCC's procedures to assure that it has adequate collateral to address a participant's default of insolvency.

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

DCC does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purpose of the Act.

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

Comments were neither solicited nor received.

**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 DCC 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. Persons making written submissions should file six copies thereof with the

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

<sup>4</sup> 15 U.S.C. 78q-1.