

(11) Each Fund's fixed-income investment portfolio will meet the listing criteria for index-based, fixed-income exchange-traded funds contained in NYSE Arca Equities Rule 5.2(j)(3), Commentary .02.

(12) Each Fund's investments will be consistent with that Fund's investment objective and will not be used to enhance leverage.

(13) A minimum of 100,000 Shares of each Fund will be outstanding at the commencement of trading on the Exchange.

This approval order is based on all of the Exchange's representations, including those set forth above and in the Notice, and the Exchange's description of the Funds.

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act<sup>51</sup> and the rules and regulations thereunder applicable to a national securities exchange.

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>52</sup> that the proposed rule change (SR-NYSEArca-2013-101), be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>53</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

[FR Doc. 2013-29491 Filed 12-10-13; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-70999; File No. SR-NSCC-2013-02]

### Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change, as Modified by Amendment Nos. 1, 2, and 3, To Institute Supplemental Liquidity Deposits to Its Clearing Fund Designed To Increase Liquidity Resources To Meet Its Liquidity Needs

December 5, 2013.

#### I. Introduction

On March 21, 2013, National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934

("Exchange Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> proposed rule change SR-NSCC-2013-02 ("Proposed Rule Change") to institute supplemental liquidity deposits to NSCC's Clearing Fund designed to increase liquidity resources to meet NSCC's liquidity needs ("SLD Proposal").<sup>3</sup> On April 10, 2013, the Commission published notice of the Proposed Rule Change for comment in the **Federal Register**.<sup>4</sup> On April 19, 2013, NSCC filed with the Commission Amendment No. 1 to the Proposed Rule Change,<sup>5</sup> which the Commission published for comment in the **Federal Register** on May 29, 2013 and designated a longer period for Commission action on the Proposed Rule Change, as amended.<sup>6</sup> The Commission received 12 comment letters, including the NFS Letter, to the SLD Proposal as initially filed and as modified by Amendment No. 1.<sup>7</sup>

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

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

<sup>3</sup> NSCC also filed the SLD Proposal contained in the Proposed Rule Change as advance notice SR-NSCC-2013-802 ("Advance Notice"), as modified by Amendment No. 1, pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010 and Rule 19b-4(n)(1)(i) thereunder. See Release No. 34-69451 (Apr. 25, 2013), 78 FR 25496 (May 1, 2013). On May 20, 2013, the Commission extended the period of review of the Advance Notice, as modified by Amendment No. 1. Release No. 34-69605 (May 20, 2013), 78 FR 31616 (May 24, 2013). On June 11, 2013, NSCC filed Amendment No. 2 to the Advance Notice, as previously modified by Amendment No. 1. Release No. 34-69954 (Jul. 9, 2013), 78 FR 42127 (Jul. 15, 2013). On October 4, 2013, NSCC filed Amendment No. 3 to the Advance Notice, as previously modified by Amendment Nos. 1 and 2. Release No. 34-70689 (Oct. 15, 2013) 78 FR 62893 (Oct. 22, 2013). On December 5, 2013, the Commission issued a Notice of No Objection to the Advance Notice, as modified by Amendment Nos. 1, 2, and 3, to Institute Supplemental Liquidity Deposits to Its Clearing Fund Designed to Increase Liquidity Resources to Meet Its Liquidity Needs. Release No. 34-71000.

<sup>4</sup> Release No. 34-69313 (Apr. 4, 2013), 78 FR 21487 (Apr. 10, 2013) ("Notice").

<sup>5</sup> NSCC filed Amendment No. 1 to the Proposed Rule Change and Advance Notice filings to include as Exhibit 2 a comment letter from National Financial Services ("NFS"), a Fidelity Investments ("Fidelity") company, to NSCC, dated March 19, 2013, regarding the SLD Proposal prior to NSCC filing the SLD Proposal with the Commission ("NFS Letter"). See Release No. 34-69620 (May 22, 2013), 78 FR 32292 (May 29, 2013) ("Notice of Amendment No. 1") and see Exhibit 2 to File No. SR-NSCC-2013-02 (<http://www.sec.gov/rules/sro/nsc/2013/34-69620-ex2.pdf>).

<sup>6</sup> Notice of Amendment No. 1, 78 FR 32292.

<sup>7</sup> See NFS Letter. See letters to Elizabeth M. Murphy, Secretary, Commission from: John C. Nagel, Esq., Managing Director and General Counsel, Citadel Securities ("Citadel"), dated April 18, 2013 ("Citadel Letter I") and June 13, 2013 ("Citadel Letter II"); Peter Morgan, Senior Vice President & Deputy General Counsel, Charles Schwab & Co., Inc., ("Charles Schwab") dated April 22, 2013 ("Charles Schwab Letter I") and May 1, 2013 ("Charles Schwab Letter II"); Thomas Price, Managing Director, Operations, Technology & BCP, Securities Industry and Financial Markets

Association ("SIFMA"), dated April 23, 2013 ("SIFMA Letter I"); Julian Rainero, Bracewell & Giuliani LLP, on behalf of Investment Technology Group, Inc. ("ITG"), dated April 25, 2013 ("ITG Letter I"); Matthew S. Levine, Managing Director, Co-Chief Compliance Officer, Knight Capital Americas LLC ("Knight Capital"), dated April 25, 2013 ("Knight Capital Letter"); Giovanni Favretti, CFA, Managing Director, Deutsche Bank, dated April 25, 2013 ("Deutsche Bank Letter"); Scott C. Goebel, Senior Vice President, General Counsel, Fidelity, dated April 25, 2013 ("Fidelity Letter I"); and Chief Financial Officer & Executive Managing Director, ConvergeX Execution Solutions LLC ("ConvergeX"), dated May 2, 2013 ("ConvergeX Letter I") and May 22, 2013 ("ConvergeX Letter II").

On June 11, 2013, NSCC filed with the Commission Amendment No. 2 to the Proposed Rule Change, as previously modified by Amendment No. 1 ("Amended SLD Proposal"), which the Commission published for comment in the **Federal Register** on July 15, 2013, with an order instituting proceedings to determine whether to approve or disapprove the Proposed Rule Change ("Order Instituting Proceedings").<sup>8</sup> The Commission received nine comment letters to Amendment No. 2 and the Order Instituting Proceedings.<sup>9</sup> On September 25, 2013, the Commission designated a longer period of review for Commission action on the Order Instituting Proceedings.<sup>10</sup> On October 7, 2013, NSCC filed Amendment No. 3 to the Proposed Rule Change ("Final SLD Proposal"), as previously modified by Amendment Nos. 1 and 2, which the Commission published for comment on October 15, 2013.<sup>11</sup> The Commission received two comment letters to the Final SLD Proposal (i.e., Amendment No. 3).<sup>12</sup>

<sup>8</sup> Release No. 34-69951 (Jul. 9, 2013), 78 FR 42140 (Jul. 15, 2013) ("Notice of Amendment No. 2").

<sup>9</sup> See letters to Elizabeth M. Murphy, Secretary, Commission from: Thomas Price, Managing Director, Operations, Technology & BCP, SIFMA, dated June 24, 2013 ("SIFMA Letter II") and August 7, 2013 ("SIFMA Letter III"); Scott C. Goebel, Senior Vice President, General Counsel, Fidelity, dated June 26, 2013 ("Fidelity Letter II"); Peter Morgan, Senior Vice President & Deputy General Counsel, Charles Schwab, dated August 5, 2013 ("Charles Schwab Letter III") and September 11, 2013 ("Charles Schwab Letter IV"); Paul T. Clark and Anthony C.J. Nuland, Seward & Kissel, LLP (representing Charles Schwab), dated August 5, 2013 ("Charles Schwab Letter V"); John C. Nagel, Esq., Managing Director and General Counsel, Citadel, dated August 5, 2013 ("Citadel Letter III") and September 5, 2013 ("Citadel Letter IV"); and Mark Solomon, Managing Director and Deputy General Counsel, ITG, dated August 5, 2013 ("ITG Letter II").

<sup>10</sup> Release No. 34-70501 (Sep. 25, 2013), 78 FR 60347 (Oct. 1, 2013).

<sup>11</sup> Release No. 34-70688 (Oct. 15, 2013), 78 FR 62846 (Oct. 22, 2013) ("Notice of Amendment No. 3").

<sup>12</sup> See letters to Elizabeth M. Murphy, Secretary, Commission from: Managing Director and Deputy General Counsel, ITG, dated November 1, 2013 ("ITG Letter III"); and Scott C. Goebel, Senior Vice President, General Counsel, Fidelity, dated November 5, 2013 ("Fidelity Letter III").

<sup>51</sup> 15 U.S.C. 78f(b)(5).

<sup>52</sup> 15 U.S.C. 78s(b)(2).

<sup>53</sup> 17 CFR 200.30-3(a)(12).

By this order, the Commission approves the Final Proposed Rule Change.

## II. Background

### A. Purpose of the SLD Proposal

NSCC filed the SLD Proposal to ensure that it would maintain sufficient liquid financial resources to withstand, at a minimum, a default by its single clearing member or clearing member family ("Clearing Member") to which it has the largest exposure ("Cover One"), in compliance with Commission Rule 17Ad-22(b)(3)<sup>13</sup> and a long-standing NSCC policy.

### B. Development of the SLD Proposal

As originally filed, the SLD Proposal would have created two related funding obligations: (1) for the 30 Clearing Members that presented NSCC with the largest peak liquidity requirements on days that did not coincide with quarterly options expiration periods ("Regular Periods"), a liquidity deposit calculated based on the Clearing Member's pro rata portion of NSCC's aggregate liquidity requirements from the 30 Clearing Members during Regular Periods ("Regular SLD"); and (2) for a subset of the 30 Clearing Members that present NSCC with a peak liquidity requirement above NSCC's total liquidity resources on days that coincide with quarterly options expiration periods ("Special Periods"), a liquidity deposit calculated based on each Clearing Member's individual contribution to NSCC's liquidity requirement above its liquidity resources during Special Periods ("Special SLD").<sup>14</sup>

Regular SLD would have been satisfied in cash only; however, a Clearing Member would have received a dollar-for-dollar reduction of its Regular SLD funding obligation to the extent that it contributed to NSCC's line-of-credit ("Credit Facility").<sup>15</sup> Special SLD could only be satisfied with cash.<sup>16</sup>

On June 11, 2013, in response to comments received, NSCC filed the Amended SLD Proposal so that, in summary: (1) Special Periods were expanded to include monthly options expirations periods along with quarterly options expiration periods; (2) Clearing Members could designate a commercial lender to commit to the Credit Facility on the Clearing Member's behalf, enabling the Clearing Member to receive the dollar-for-dollar reduction of its Regular SLD; (3) any commitments to

the Credit Facility made in excess of a Clearing Member's Regular SLD would be allocated ratably among all 30 Clearing Members that would be required to make a Regular SLD funding obligation; and (4) "liquidity exposure reports" would be provided to all NSCC members, so that members, particularly Clearing Members, could better assess their liquidity exposure to NSCC.<sup>17</sup>

On October 4 and 7, 2013, in response to further comments received, NSCC filed the Final SLD Proposal.<sup>18</sup> Among other things, the Final SLD Proposal eliminated the Regular SLD funding obligation.

### III. Description of the Final SLD Proposal

The Final SLD Proposal would add Rule 4A to NSCC's Rules and Procedures<sup>19</sup> to establish a supplemental liquidity funding obligation designed to cover the liquidity exposure attributable to those Clearing Members that regularly incur the largest gross settlement debits over a settlement cycle during times of increased trading and settlement activity that arise around Special Periods. More specifically, the obligation applies to a subset of the 30 Clearing Members that present NSCC with historic peak liquidity needs on days that coincide with Special Periods above NSCC's current total liquidity resources. For this subset, NSCC will require a liquidity deposit based on the proportion of the historic peak liquidity exposure that is presented by each Clearing Member in excess of NSCC's then-available total liquidity resources. NSCC will hold deposits made in satisfaction of a Special SLD funding obligation in its Clearing Fund for a period of seven days after the end of the Special Period.

Additionally, if a Clearing Member believes its current trading activity will present a liquidity need to NSCC above NSCC's total liquidity resources, it may voluntarily deposit funds with NSCC to cover the shortfall ("Prefund Deposit"). NSCC will hold Prefund Deposit funds for a period of seven days after the end of the Special Period. If a Clearing Member presents NSCC with a liquidity need above total liquidity resources that is not funded by a Special SLD funding obligation or a Prefund Deposit the Final SLD Proposal will empower NSCC

to call from that Clearing Member the amount of the shortfall, or that Clearing Member's share if caused by more than one Clearing Member, and hold it for 90 days ("Call Deposit").

### IV. Summary of Comments Received and NSCC's Responses

The Commission received 23 comment letters to the SLD Proposal<sup>20</sup> from eight commenters,<sup>21</sup> including the NFS Letter.<sup>22</sup> Commenters include bank affiliated and non-bank affiliated NSCC members, as well as one industry trade group, SIFMA.<sup>23</sup> NSCC also submitted two responses to comment letters received.<sup>24</sup> The Commission has reviewed and taken into full consideration all of the comments received.

All eight commenters express support for NSCC's overall goal of maintaining sufficient financial resources to withstand a default by a Clearing Member (i.e., Cover One).<sup>25</sup> One commenter, who previously supported approval of the Amended SLD Proposal, supports approval of the Final SLD Proposal.<sup>26</sup> The remaining seven commenters oppose the original SLD Proposal and the Amended SLD Proposal, as discussed in more detail below.<sup>27</sup> One of those seven

<sup>20</sup> Since the SLD Proposal was filed as both the Proposed Rule Change and the Advance Notice, the Commission considered all comments received on the proposal, regardless of whether the comments were submitted to the Proposed Rule Change or the Advance Notice. See NFS Letter, Citadel Letter I, Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, ITG Letter III, Knight Capital Letter, Deutsche Bank Letter, Fidelity Letter I, Fidelity Letter II, Fidelity Letter III, ConvergEx Letter I, and ConvergEx Letter II.

<sup>21</sup> See Comments to the Proposed Rule Change (File No. SR-NSCC-2013-02), <http://sec.gov/comments/sr-nsc-2013-02/nsc201302.shtml>, and the Advance Notice (File No. SR-NSCC-2013-802) (<http://sec.gov/comments/sr-nsc-2013-802/nsc2013802.shtml>) ("Comments Received"). For purposes of discussion, the Commission considers the comment submitted by Seward & Kissel on behalf of Charles Schwab as a Charles Schwab comment, see Charles Schwab Letter V, *supra* note 9, and the NFS Letter as a Fidelity comment. See NFS Letter.

<sup>22</sup> See NFS Letter.

<sup>23</sup> See Comments Received, *supra* note 21.

<sup>24</sup> See letters to Elizabeth M. Murphy, Secretary, Commission from Larry E. Thompson, Managing Director and DTCC General Counsel, dated June 10, 2013 ("NSCC Letter I") and August 20, 2013 ("NSCC Letter II").

<sup>25</sup> See NFS Letter, Citadel Letter III, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter V, SIFMA Letter II, SIFMA Letter III, Knight Capital Letter, Deutsche Bank Letter, Fidelity Letter I, Fidelity Letter II, ConvergEx Letter I, ConvergEx Letter II, ITG Letter II.

<sup>26</sup> See Fidelity Letter II, Fidelity Letter III.

<sup>27</sup> See NFS Letter, Citadel Letter I, Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles

<sup>17</sup> See Notice of Amendment No. 2, 78 FR at 42127.

<sup>18</sup> NSCC filed the Final Proposed Rule Change on October 7, 2013, three days after NSCC filed Amendment No. 3 to the Advance Notice.

<sup>19</sup> See Exhibit 5 to File No. SR-NSCC-2013-02, <http://www.sec.gov/rules/sro/nsc/2013/34-70688-ex5.pdf>.

<sup>13</sup> 17 CFR 240.17Ad-22(b)(3).

<sup>14</sup> See Notice, 78 FR at 21487-88.

<sup>15</sup> *Id.* at 21489.

<sup>16</sup> *Id.*

commenters submitted the sole comment letter in opposition to the Final SLD Proposal.<sup>28</sup>

#### A. Comments Expressing Support for the Provision of Adequate Liquidity at NSCC

As mentioned above, all eight commenters to the SLD Proposal agreed that NSCC must have access to sufficient liquidity and capital to meet the Cover One standard, and some stated NSCC's critical role as a national clearance and settlement system.<sup>29</sup> For example, one commenter states "that a clearing agency performing central counterparty services is essential to the proper functioning of the capital markets, and that ensuring the clearing agency is well capitalized and financially sound serves to benefit both the clearing agency's members and the capital markets as a whole."<sup>30</sup> The commenter goes on to state that it "appreciates the need for the NSCC, both as a central counterparty and as a financial market utility that has been designated by the Financial Stability Oversight Council as systemically important, to maintain sufficient financial resources to withstand a default by the NSCC member or family of affiliated members to which the NSCC has the largest exposure . . . [and] also understands the NSCC's desire to broaden the base of support for its liquidity needs beyond the small group of firms that has historically supported these needs through participation in the NSCC's revolving credit facility, and believes it is important to enable all of the NSCC's members to help the NSCC maintain sufficient financial resources."<sup>31</sup> Another commenter notes that "NSCC should have the resources it needs to be a source of strength for the national clearing and settlement system . . ."<sup>32</sup> Additionally, another commenter states that it "appreciates the importance of NSCC's critical role as a [c]entral [c]ounterparty . . . and supports NSCC's goal in ensuring that it has access to sufficient capital in the event that is largest participant fails."<sup>33</sup>

Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, ITG Letter III, Knight Capital Letter, Deutsche Bank Letter, Fidelity Letter I, ConvergEx Letter I, and ConvergEx Letter II.

<sup>28</sup> See ITG Letter III.

<sup>29</sup> See *supra* note 25.

<sup>30</sup> See SIFMA Letter II.

<sup>31</sup> *Id.*

<sup>32</sup> See Charles Schwab Letter III, Charles Schwab Letter V.

<sup>33</sup> See ConvergEx Letter II.

#### B. Opposing Comments Received Prior to the Final SLD Proposal

##### 1. Comments Inapplicable to the Final SLD Proposal

The seven commenters opposed to approval of the SLD Proposal objected to the SLD Proposal for various reasons, as discussed below.<sup>34</sup> Additionally, five of the seven commenters that oppose the SLD Proposal, as well as the commenter in support of the Final SLD Proposal, suggested potential alternative mechanisms for NSCC to satisfy its liquidity needs.<sup>35</sup>

Many of the commenters opposed to the original SLD Proposal and Amended SLD Proposal raised concerns with a component of the proposal that NSCC eliminated in the Final SLD Proposal.<sup>36</sup> Those comments included concerns about: (1) The anticipated costs for Clearing Members as a result of implementation of Regular SLD funding obligation, including costs imposed by a quick implementation period;<sup>37</sup> (2) Clearing Members' inability to accurately predict or control their funding obligation and the effects thereof, including broker-dealers' inability to plan for funding and liquidity risks as provided in FINRA Reg. Notice 10-57;<sup>38</sup> (3) distributional effects associated with implementation

<sup>34</sup> See Citadel Letter I, Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, ITG Letter III, Knight Capital Letter, Deutsche Bank Letter, ConvergEx Letter I, and ConvergEx Letter II.

<sup>35</sup> Alternatives included, but were not limited to: NSCC should issue long-term debt to increase its liquidity resources; NSCC should increase intra-day margin calls; NSCC should increase Clearing Member fees; NSCC should reduce the settlement cycle; NSCC should reduce the volume of unsettled trades; NSCC should establish a bilateral third-party bank committed facility; and NSCC should change its capital structure. See NFS Letter, Citadel Letter II, Citadel Letter III, Charles Schwab Letter II, Charles Schwab Letter III, SIFMA Letter II, SIFMA Letter III, ITG Letter II, Fidelity Letter II, Fidelity Letter III and ConvergEx Letter II. The Commission notes that these comments are beyond the subject of the Final SLD Proposal by NSCC that is before the Commission for approval under Section 19(b) of the Act (which provides that the Commission shall approve a proposed rule change if it finds that such proposed rule change is consistent with the requirements of this title and the applicable rules and regulations issued thereunder).

<sup>36</sup> See Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, Knight Capital Letter, Deutsche Bank Letter, ConvergEx Letter I, ConvergEx Letter II.

<sup>37</sup> See, e.g., ITG Letter I, ITG Letter II, Citadel Letter III.

<sup>38</sup> See Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles Schwab Letter II, SIFMA Letter I, SIFMA Letter II, ITG Letter II, Knight Capital Letter, Deutsche Bank Letter, ConvergEx Letter II.

of the Regular SLD funding obligation, manifested in particular by an anti-competitive and disparate impact on non-bank affiliated Clearing Members compared to bank affiliated Clearing Members with regard to the offsetting commitments to the Credit Facility;<sup>39</sup> and (4) perceived mechanical flaws with the application of the Regular SLD funding obligation.<sup>40</sup>

Since NSCC has eliminated the aspect of the SLD Proposal to which these comments were made, the Commission believes these comments are not relevant for its determination on the Final SLD Proposal.

##### 2. Comments Applicable to the Final SLD Proposal and NSCC's Responses Thereto

Seven of the eight commenters raised concerns with the SLD Proposal that, while not necessarily directly associated with the Special SLD funding obligation, could apply to elements of the Special SLD funding obligation and thus are relevant for the Commission's consideration of the Final SLD Proposal.<sup>41</sup> Four commenters argued that the SLD Proposal is arbitrary and capricious because it applies to no more than 30 Clearing Members.<sup>42</sup> Six commenters argued that the SLD Proposal would have unintended consequences of forcing a number of Clearing Members to terminate their membership and thereby concentrating the broker clearing business in fewer Clearing Members, potentially increasing systemic risk.<sup>43</sup> One

<sup>39</sup> See Citadel Letter II, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, Knight Capital Letter, ConvergEx Letter I, ConvergEx Letter II.

<sup>40</sup> See ITG Letter II.

<sup>41</sup> See Citadel Letter II, Citadel Letter III, Citadel Letter IV, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, ITG Letter III, Knight Capital Letter, Deutsche Bank Letter, ConvergEx Letter I, ConvergEx Letter II.

<sup>42</sup> See Citadel Letter II, ITG Letter I, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter III, ITG Letter II, ITG Letter III. All four commenters argue that the imposition of a funding obligation to no more than 30 Clearing Members was arbitrary and capricious referred to the Regular SLD funding obligation, in which a Regular SLD funding obligation is satisfied pro rata by 30 Clearing Members irrespective of whether each Clearing Member presented a peak liquidity need above NSCC total available liquidity resources. One of the four commenters claims that the same argument persists for the Special SLD Funding Obligation; as such, the Commission will consider the comment here. See Charles Schwab Letter V.

<sup>43</sup> See Citadel Letter II, Charles Schwab Letter II, Charles Schwab Letter III, SIFMA Letter I, SIFMA Letter II, SIFMA Letter III, ITG Letter I, ITG Letter II, Knight Capital Letter, ConvergEx Letter II.

commenter stated that historic peak liquidity needs, which would be used by NSCC to determine the liquidity need presented by each Clearing Member, is not necessarily predictive of future liquidity needs.<sup>44</sup> Three commenters argued that NSCC incorrectly calculates its liquidity needs in the SLD Proposal, either because the liquidity need is calculated using Clearing Member gross settlement debits instead of net settlement debits or because the settlement debits were aggregated over a four-day cycle.<sup>45</sup> Seven commenters stated that treatment of funds delivered to NSCC to satisfy a funding obligation under the SLD Proposal for Commission Rule 15c3-1 purposes was unclear.<sup>46</sup>

In response to comments that imposition of a funding obligation is arbitrary and capricious, NSCC revised the SLD Proposal to eliminate the Regular SLD funding obligation component,<sup>47</sup> which would have: (i) Assigned a funding obligation to the 30 Clearing Members that presented NSCC with the largest peak liquidity needs irrespective of whether the peak liquidity need itself would have surpassed NSCC available liquidity resources, and (ii) allocated a funding obligation to each of those 30 Clearing Members driven substantially by the peak liquidity need presented to NSCC by the largest Clearing Member.<sup>48</sup> In response to comments regarding unintended consequences of the SLD Proposal, such as Clearing Members terminating their membership, NSCC stated that the Clearing Member is in the best position to monitor and manage the liquidity risks presented by its own activity.<sup>49</sup> Similarly, NSCC states that the maintenance of adequate liquidity resources at NSCC is a key element in the reduction of systemic risk at a systemically-important financial market utility and also a key component of NSCC's ability to prevent the failure of a Clearing Member from having a cascading effect on other Clearing Members.<sup>50</sup>

NSCC agreed that historic peak liquidity needs are not necessarily predictive of future liquidity needs, and as a result NSCC has proposed a

mechanism whereby Clearing Members may voluntarily prefund liquidity needs that the Clearing Member anticipates will surpass total liquidity resources available at NSCC through the Prefund Deposit.<sup>51</sup> Furthermore, in the event a Clearing Member does not elect to prefund potential liquidity needs but does present a liquidity need to NSCC above total liquidity resources that is not accounted for by a Special SLD funding obligation, NSCC has proposed a mechanism to require the Clearing Member to fund the liquidity need through the Call Deposit.<sup>52</sup> With respect to comments that NSCC incorrectly calculates its liquidity need by using gross settlement debits instead of net settlement debits, NSCC responded that, as a central counterparty for its members, its risk-exposure is reflected by the gross settlement debits presented to it, not net settlement debits, in the event of a Clearing Member default.<sup>53</sup> Furthermore, NSCC stated that calculating liquidity obligations over a four-day settlement cycle is consistent with NSCC's practical liquidity obligation in the event of a Clearing Member default.<sup>54</sup> Finally, in response to comments that the treatment of funds posted in satisfaction of an SLD funding obligation for Rule 15c3-1 purposes is unclear, NSCC stated that it structured the SLD Proposal so that deposits made pursuant to an SLD funding obligation would constitute Clearing Fund deposits, which have clear regulatory capital treatment under Rule 15c3-1.<sup>55</sup>

Six commenters stated that the SLD Proposal did not provide a sufficient evaluation of its burden on competition and lacked necessary detail so as to elicit meaningful comment.<sup>56</sup> Many of these commenters argued that, while they supported NSCC's need for liquidity resources generally, NSCC did not demonstrate a specific need for additional liquidity in connection with the SLD Proposal.<sup>57</sup> Five commenters argued the SLD Proposal lacked sufficient Clearing Member input prior to submitting the proposal.<sup>58</sup> Three

commenters also argued that the SLD Proposal did not adequately protect investors.<sup>59</sup> One commenter argued that the fact that NSCC submitted the SLD Proposal without Clearing Member input is indicative of a lack of fair representation for Clearing Members in the governance of NSCC.<sup>60</sup> One commenter stated that NSCC did not take into account the potential impact of other central counterparties instituting similar liquidity provisions.<sup>61</sup> Five commenters argued in opposition of cash being the only source by which a Clearing Member could satisfy a supplemental liquidity deposit.<sup>62</sup>

In response to comments received regarding insufficient detail of the SLD Proposal, NSCC provided detail regarding the specific need for liquidity resources,<sup>63</sup> implementation timeframes for the SLD Proposal,<sup>64</sup> and a suite of tools, such as monthly and daily reports, to enable Clearing Members to more accurately predict a potential Regular SLD funding obligation.<sup>65</sup> NSCC stated that it would work with Clearing Members to help them understand and develop tools to forecast liquidity exposure and mitigate their peak liquidity exposure.<sup>66</sup> NSCC also stated that it would provide monthly and daily reports to Clearing Members that would show liquidity exposure during relevant periods.<sup>67</sup> NSCC also stated that fluctuating peak activity recently has exceeded NSCC available total liquidity resources.<sup>68</sup> NSCC believes these liquidity needs are largely driven by industry consolidation, developments in

<sup>59</sup> See Deutsche Bank Letter, Charles Schwab Letter II, Charles Schwab IV, Charles Schwab Letter V, SIFMA Letter II.

<sup>60</sup> See Citadel Letter III.

<sup>61</sup> See Charles Schwab Letter II, Charles Schwab Letter III. Additionally, one commenter argued that NSCC attempted to improperly amend the SLD Proposal through a response to comments. See Charles Schwab Letter V. The Commission notes that NSCC filed the Final SLD Proposal subsequent to the Commission's receipt of this comment in accordance with the rule filing process. See Notice of Amendment No. 3, 78 FR 62846.

<sup>62</sup> See NFS Letter, Charles Schwab Letter II, Charles Schwab Letter III, Citadel Letter II, Citadel Letter III, SIFMA Letter I, Fidelity Letter II, ITG Letter II.

<sup>63</sup> See NSCC Letter II (stating that "NSCC has seen continued increases in potential liquidity needs, driven by consolidation in the industry, developments in trading techniques (including a rise in high frequency trading), and a reduction in volatility from the post-[2008] crisis highs which result in reduced Clearing Fund requirements").

<sup>64</sup> See Notice of Amendment No. 3, 78 FR 62846 (stating that the Final SLD Proposal would be implemented on February 1, 2014).

<sup>65</sup> See NSCC Letter I, NSCC Letter II, Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846.

<sup>66</sup> See NSCC Letter I.

<sup>67</sup> See NSCC Letter I, NSCC Letter II.

<sup>68</sup> See NSCC Letter II.

<sup>51</sup> See Notice of Amendment No. 3, 78 FR at 62847.

<sup>52</sup> See Notice, 78 FR at 21489.

<sup>53</sup> See NSCC Letter I.

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

<sup>55</sup> *Id.*

<sup>56</sup> See Citadel Letter II, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter V, SIFMA Letter II, ITG Letter I, ITG Letter II, Knight Capital Letter, ConvergEx Letter I, ConvergEx Letter II.

<sup>57</sup> See Citadel Letter II, Citadel Letter III, SIFMA Letter II, SIFMA Letter III, ITG Letter II, ITG Letter III, ConvergEx Letter II.

<sup>58</sup> See Citadel Letter III, Charles Schwab Letter I, ITG Letter I, ITG Letter II, Knight Capital Letter, Deutsche Bank Letter.

<sup>44</sup> See ITG Letter II.

<sup>45</sup> See Citadel Letter III, ITG Letter II, ConvergEx Letter I, ConvergEx Letter II.

<sup>46</sup> See 17 CFR 240.15c3-1. See, e.g., Citadel Letter II, Citadel Letter III, Charles Schwab Letter II, Charles Schwab Letter III, SIFMA Letter II, ITG Letter I, ITG Letter II, ITG Letter III, Knight Capital Letter, ConvergEx Letter II.

<sup>47</sup> See Notice of Amendment No. 3, 78 FR at 62847.

<sup>48</sup> *Id.* at 62846-47.

<sup>49</sup> NSCC Letter I.

<sup>50</sup> See NSCC Letter I, NSCC Letter II.

trading techniques, including an increased use of high frequency trading, and a reduction in volatility from post-2008 financial crisis levels, generally resulting in a reduction in Clearing Fund requirements.<sup>69</sup> In response to comments received regarding insufficient analysis of the burden on competition that might ensue from implementation of the SLD Proposal, NSCC substantially revised the SLD Proposal twice to expand its analysis of the burden on competition to include, for example, individual subsections specifically addressing competition concerns raised by commenters,<sup>70</sup> and to reduce any disparate impact on Clearing Members stemming from implementation of the SLD Proposal, first to provide a mechanism by which non-bank affiliated Clearing Members could contribute to Credit Facility, and second to eliminate the Regular SLD from the Final SLD Proposal.<sup>71</sup>

In response to comments regarding the lack of Clearing Member input in the SLD Proposal and that the development of the SLD Proposal without Clearing Member input was indicative of a lack of fair representation of all Clearing Members at NSCC, NSCC stated that it engaged in discussions with Clearing Members likely to be impacted by the SLD Proposal, including more than 100 meetings with Clearing Members to enhance Clearing Members' understanding of liquidity risks presented to NSCC and the SLD Proposal generally.<sup>72</sup> The Proposed Rule Change and subsequent amendments were published for comment four times, so Clearing Members had an opportunity to comment, and NSCC also substantially revised the SLD Proposal twice as a direct response to comments received on the SLD Proposal.<sup>73</sup> Finally, on September 18, 2013, NSCC announced to its membership that it was forming the Clearing Agency Liquidity Council ("CALC"), an advisory group to continue the dialogue between NSCC and its Clearing Members regarding liquidity issues in a

formal setting.<sup>74</sup> According to NSCC, the CALC intends to explore additional liquidity resources in advance of the 2014 renewal of NSCC's Credit Facility, in order to address, for example, NSCC's liquidity needs outside of Special Periods and the refinancing risk associated with the annual renewal of the Credit Facility.<sup>75</sup> According to NSCC, twenty-four Clearing Members joined the CALC, including all eight commenters to the SLD Proposal, which has met on multiple occasions since its inception.

NSCC responded to comments that the SLD Proposal did not contain sufficient information by amending the SLD Proposal twice to further identify the potential impact of the SLD Proposal on Clearing Members and to make substantive revisions to the SLD Proposal to address those concerns.<sup>76</sup> NSCC responded to comments that the SLD Proposal did not protect investors by stating that the maintenance of adequate liquidity resources at NSCC, a designated systemically-important financial market utility<sup>77</sup> that plays a fundamental role in the United States cash equities market, will protect against the transmission of systemic risk among Clearing Members in the event of a failure of one Clearing Member, thereby promoting the prompt and accurate settlement of securities transactions and the protection of investors.<sup>78</sup> NSCC responded to the comment that it did not take into account other central counterparties imposing similar liquidity requirements by stating that such a concern was unlikely given the difference in liquidity risk between cash market central counterparties (i.e., NSCC), where potential liquidity needs typically are orders of magnitude greater than the market risk that their margin collections are designed to cover, and

derivatives central counterparties, where liquidity needs generally are more closely aligned to market risk of members' portfolios and the members' margin requirements.<sup>79</sup> In response to comments opposed to cash being the sole funding source by which a Clearing Member could satisfy a supplemental liquidity deposit, NSCC eliminated Regular SLD, thereby eliminating concern relating to disparate treatment that might ensue by requiring Clearing Members that do not make a commitment to lend to NSCC through the Credit Facility to make their Regular SLD funding obligation in cash, and NSCC states that the CALC will evaluate potential alternative collateral approaches that could be used to fund a portion of a Clearing Member's funding obligation.<sup>80</sup>

### C. Comments to the Final SLD Proposal

The Commission received two comments on the Final SLD Proposal. Both commenters supported NSCC's decision to eliminate the Regular SLD funding obligation from the SLD Proposal.<sup>81</sup> One commenter argued for approval of the Final SLD Proposal, since the Final SLD Proposal "is a helpful development in the process of determining how best to increase NSCC's liquidity resources to meet its liquidity needs."<sup>82</sup> Moreover, the commenter believes that "NSCC has addressed the area of greatest [m]ember concern in removing provisions of the [SLD] Proposal that collectively deal with the imposition of the Regular [SLD]."<sup>83</sup> One commenter argued for disapproval of the Final SLD Proposal, stating that flawed concepts remain and approval would unnecessarily inhibit the development of ideas from NSCC's CALC.<sup>84</sup> NSCC did not submit a response to comments received after submission of the Final SLD Proposal.

### V. Discussion and Commission Findings

After careful review, the Commission finds that the Final SLD Proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a registered clearing agency.<sup>85</sup> In particular, the

<sup>69</sup> *Id.*

<sup>70</sup> See Notice of Amendment No. 2, 78 FR 42140. See also NSCC Letter I. NSCC argued that the SLD Proposal would apply fairly across Clearing Members and, while recognizing potential competitive impacts on such members, believed the SLD Proposal addressed important financial resource requirements. NSCC also stated that it was revising the SLD Proposal to address competition concerns.

<sup>71</sup> See Notice of Amendment No. 3, 78 FR 62846. See also NSCC Letter II.

<sup>72</sup> See NSCC Letter I.

<sup>73</sup> See Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846. See also NSCC Letter II.

<sup>74</sup> DTCC Important Notice a7706, *Creation of DTCC Clearing Agency Liquidity Council and Nomination Process* (Sep. 18, 2013), [http://dtcc.com/downloads/legal/imp\\_notices/2013/nsccl/a7706.pdf](http://dtcc.com/downloads/legal/imp_notices/2013/nsccl/a7706.pdf).

<sup>75</sup> See NSCC Letter II. See also Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846.

<sup>76</sup> See Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846. See also NSCC Letter II.

<sup>77</sup> Financial Stability Oversight Council ("FSOC") 2012 Annual Report, Appendix A, <http://www.treasury.gov/initiatives/fsoc/Documents/2012%20Annual%20Report.pdf> ("FSOC Designation").

<sup>78</sup> See NSCC Letter I, NSCC Letter II. Designation as systemically-important by FSOC means that a failure of or disruption to its functioning could create, or increase, the risk of significant credit or liquidity problems spreading among financial institutions or markets, thereby threatening financial stability. See 12 U.S.C. 5462(9). See also FSOC Designation, *supra* note 77.

<sup>79</sup> See NSCC Letter II.

<sup>80</sup> *Id.* See also discussion below noting that any cash deposit is driven by the Clearing Member's own trading activity.

<sup>81</sup> See ITG Letter III, Fidelity Letter III.

<sup>82</sup> See Fidelity Letter III.

<sup>83</sup> *Id.*

<sup>84</sup> See ITG Letter III.

<sup>85</sup> In approving the Proposed Rule Change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f). Comments about

Commission finds that the Final SLD Proposal is consistent with the following provisions of the Act: (i) Section 17A(b)(3)(A),<sup>86</sup> which requires that a clearing agency “is so organized and has the capacity to be able to facilitate the prompt and accurate clearance and settlement of securities transactions . . . to safeguard securities and funds in its custody and control and for which it is responsible . . . and to enforce . . . compliance by its participants with the rules of the clearing agency;” (ii) Section 17A(b)(3)(F),<sup>87</sup> which requires that: the rules of a clearing agency not be designed to permit unfair discrimination among participants in the use of the clearing agency; and the rules of a clearing agency promote the prompt and accurate clearance and settlement of securities transactions and protect investors and the public interest; (iii) Section 17A(b)(3)(D),<sup>88</sup> which requires that the rules of a clearing agency provide for the equitable allocation of reasonable dues, fees, and other changes among its participants; and (iv) Section 17A(b)(3)(I),<sup>89</sup> which requires the rules of a clearing agency not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

The Commission’s Order Instituting Proceedings solicited comment on a number of issues. After carefully considering the Final SLD Proposal and the comments received on the SLD Proposal and NSCC responses thereto, the Commission finds that the Final SLD Proposal is consistent with the Exchange Act and therefore must be approved.

The Commission recognizes that some commenters did not support certain aspects of the SLD Proposal. The Commission, however, must approve a proposed rule change if it finds that the proposed rule change is consistent with the requirements of the Exchange Act and the applicable rules and regulations thereunder. No comments convinced the Commission that the Final SLD Proposal was not consistent with the Exchange Act and the applicable rules and regulations thereunder. The Commission believes that, overall, the Final SLD Proposal: (i) Will improve financial safety at NSCC by increasing its ability to meet its liquidity needs; (ii) provides for the equitable allocation of

the potential competitive impact of the Proposed Rule Change are addressed above and below.

<sup>86</sup> 15 U.S.C. 78q-1(b)(3)(A).

<sup>87</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>88</sup> 15 U.S.C. 78q-1(b)(3)(D).

<sup>89</sup> 15 U.S.C. 78q-1(b)(3)(I).

reasonable expenses; and (iii) does not permit unfair discrimination among Clearing Members in the use of NSCC or impose an unnecessary burden on competition. The Commission’s analysis of the comments applicable to the Final SLD Proposal and the Final SLD Proposal’s consistency with the Exchange Act are discussed below.

As stated above, several commenters argued that the original SLD Proposal suffered from certain defects, such as a failure of NSCC to consult with Clearing Members prior to submitting the SLD Proposal,<sup>90</sup> that the SLD Proposal contained an insufficient evaluation of the burden on competition, and an insufficient description of the SLD Proposal,<sup>91</sup> and that NSCC did not demonstrate a specific need for additional liquidity in connection with the SLD Proposal.<sup>92</sup>

The Commission believes that the Final SLD Proposal is consistent with the Exchange Act and the applicable rules and regulations thereunder. NSCC made substantial revisions to the SLD Proposal directly responsive to comments raised during the comment period, created the CALC to continue the dialogue between NSCC and Clearing Members regarding liquidity generally, and provided a more robust description of the SLD Proposal and its potential effects on the competition between Clearing Members,<sup>93</sup> in particular describing how the Final SLD Proposal addresses those potential effects.<sup>94</sup>

As stated above, all commenters expressed support for the notion that NSCC must have access to sufficient liquidity.<sup>95</sup> One commenter stated that “NSCC’s critical role as a national clearance and settlement system” made it so that adequate liquidity resources at NSCC was of paramount importance.<sup>96</sup> The Commission believes that NSCC’s maintenance of adequate Cover One liquidity resources helps ensure that orderly settlement can be completed notwithstanding the failure of its largest Clearing Member. The Commission further believes approval of the Final SLD Proposal is necessary to improve the overall financial safety of NSCC and its ability to complete settlement.

The Commission also notes that NSCC has stated that fluctuating peak liquidity

needs presented to NSCC have exceeded total liquidity resources available to NSCC, emphasizing the need for NSCC to develop a mechanism to help ensure that it maintains adequate liquidity as soon as possible.<sup>97</sup> These liquidity needs are driven by Clearing Members’ trading activity, and the Final SLD Proposal is designed as a mechanism to allocate a funding obligation to those Clearing Members with peak liquidity needs that surpass NSCC available liquidity resources.

The Commission also believes that the Final SLD Proposal provides a mechanism to help ensure that NSCC maintains sufficient liquidity prospectively. The Commission agrees with commenters that have suggested that historic peak liquidity is not necessarily predictive of future liquidity needs. To this point, the Final SLD Proposal permits Clearing Members to use a Prefund Deposit in cases where a Clearing Member anticipates that its current trading activity will surpass total liquidity resources at NSCC. Furthermore, in the event that a Clearing Member does not elect to make a Prefund Deposit but does present a liquidity need to NSCC above total liquidity resources that is not accounted for by a Special SLD funding obligation, NSCC may require the Clearing Members to fund the liquidity need by making a Call Deposit. The Commission believes that these tools provide NSCC with the means to access sufficient liquidity prospectively. For the above reasons, the Commission believes the SLD Proposal is consistent with the requirements of Exchange Act Sections 17A(b)(3)(A) and (F) regarding the prompt and accurate settlement of securities transactions.

The Commission takes specific note of comments arguing that the costs of the Final SLD Proposal would have the unintended consequence of causing many Clearing Members to terminate their membership with NSCC and thereby concentrating the brokerage clearing business in fewer Clearing Members, potentially leading to an increase of systemic risk. The Commission recognizes that there are costs of the Final SLD Proposal for Clearing Members for which the Special SLD funding obligation applies. Clearing Members would be required to meet the Special SLD funding obligation in cash, which would be maintained by NSCC for a period of seven business days following the end of the Special Period.<sup>98</sup> Furthermore, funds delivered to NSCC pursuant to a Call Deposit will

<sup>90</sup> See *supra* note 58.

<sup>91</sup> See *supra* note 56.

<sup>92</sup> See *supra* note 57.

<sup>93</sup> See Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846, NSCC Letter I, NSCC Letter II.

<sup>94</sup> See Notice of Amendment No. 3, 78 FR 62846, NSCC Letter II.

<sup>95</sup> See *supra* note 25.

<sup>96</sup> See ConvergeEx Letter II.

<sup>97</sup> See NSCC Letter II.

<sup>98</sup> See Notice, 78 FR at 21490.

be maintained by NSCC for a period of 90 days.<sup>99</sup>

Under the Final SLD Proposal, Clearing Members would only be required to provide funding to the extent that the Clearing Member's trading activity during a two-year look-back period of correlated Special Period dates would have resulted in NSCC having insufficient liquidity resources to cover the default of that Clearing Member after taking into account all of NSCC's available liquidity resources at the time of default.<sup>100</sup> The Special SLD funding obligation provides for an allocation formula that ratably applies to a subset of the 30 Clearing Members that present largest peak liquidity needs to NSCC above NSCC's total liquidity resources during Special Periods.<sup>101</sup> By allocating the funding obligation to those Clearing Members that directly create the liquidity need, the Final SLD Proposal helps to ensure that those Clearing Members who impose equivalent liquidity burdens on NSCC bear equivalent financial costs and allows each Clearing Member to exercise a degree of control over the funding obligation it bears. Accordingly, and notwithstanding the views expressed by commenters, the Commission believes that applying a liquidity obligation only to those Clearing Members that present a liquidity need to NSCC based on a historical look-back period above the total liquidity resources available to NSCC is an equitable allocation of expenses as required by Exchange Act Section 17A(b)(3)(D).

NSCC's application of the Special SLD funding obligation to no more than the 30 Clearing Members that present the highest peak liquidity exposures over a two-year look-back period during Special Periods<sup>102</sup> prima facie has the effect of limiting that obligation to a subset of Clearing Members. However, a Special SLD funding obligation will not be imposed on a Clearing Member, irrespective of the rank of that Clearing Member's peak liquidity need vis-à-vis other Clearing Members, unless that Clearing Member's peak liquidity need surpassed NSCC's total liquidity resources.<sup>103</sup>

Since whether an individual Clearing Member will have a Special SLD funding obligation is dependent solely upon the liquidity needs presented by that Clearing Member during the look-back period in excess of NSCC's then-available total liquidity resources, the Commission believes that expanding the Special SLD funding obligation to all Clearing Members is not necessary given the practical application of the rule to a subset of the 30 Clearing Members. Accordingly, despite the views expressed by some commenters, the Commission believes that limiting application of the Special SLD requirement to no more than 30 Clearing Members is consistent with the requirement of Exchange Act Section 17A(b)(3)(D) that expenses be equitably allocated among Clearing Members.

As stated above, the Commission recognizes that costs will be imposed through the Final SLD Proposal on Clearing Members for which the Special SLD funding obligation applies. The Commission also recognizes that some Clearing Members may make an economic decision to terminate their NSCC membership to avoid these costs. The Commission believes, however, that the Final SLD Proposal is a reasonable measure of the associated liquidity expenses experienced by NSCC and that the associated costs are necessary and appropriate for NSCC to ensure that it has the liquidity resources required to continue to operate in a safe and sound manner.

Under the Final SLD Proposal, a funding obligation is generated when a Clearing Member's trading activity during a historic Special Period would have resulted in NSCC having insufficient liquidity resources to cover the default of that Clearing Member after taking into account all of NSCC's available liquidity resources at that time. As a result, a Special SLD funding obligation is the amount of the difference between a demonstrated peak total liquidity need created and current total liquidity resources available, which difference NSCC would be unable to account for through other liquidity resources.

As for the unintended consequences associated with the Final SLD Proposal, the Commission agrees with NSCC that the maintenance of adequate liquidity at NSCC is a fundamental element in addressing the goal of reducing the potential systemic risk posed by a systemically-important financial market utility<sup>104</sup> and also a key component of NSCC's ability to prevent the failure of a Clearing Member from having a

cascading effect on other Clearing Members. The Commission also believes that since Clearing Members exercise a degree of control over whether they will face an SLD funding obligation, they could explore alternatives to termination of membership to avoid incurring a Special SLD funding obligation, including changes to trading behavior so that their trading activity does not present a liquidity need to NSCC above NSCC's total available liquidity resources, as informed by the daily and monthly "liquidity transaction" reports to be provided by NSCC as part of the Final SLD Proposal.<sup>105</sup> Accordingly, the Commission believes the expenses charged by NSCC through imposition of the Special SLD funding obligation are reasonable as required by Exchange Act Section 17A(b)(3)(D).

For these reasons stated above, the Commission believes that the Final Proposed Rule Change containing the Final SLD Proposal meets the Section 17A(b)(3)(D) Exchange Act standard of equitable allocation of reasonable dues, fees, and other charges among its participants. The Commission finds it equitable that Clearing Members address the liquidity exposure that they actually present to NSCC during Special Periods and that such liquidity exposure is not borne by Clearing Members whose trading activity does not generate the liquidity need. Similarly, the Commission finds the Final SLD Proposal equitable in that two Clearing Members that produce the same liquidity need in excess of NSCC's total liquidity resources will be assessed the same Special SLD funding obligation. Furthermore, the Final SLD Proposal is equitable because it allows Clearing Members to anticipate and manage their own liquidity exposure to the clearing agency by changing their trading behavior. Finally, the Commission believes that the limitation in NSCC's rules to apply the Special SLD funding obligation to not more than 30 Clearing Members is not arbitrary or capricious because a Clearing Member's Special SLD funding obligation will depend solely upon its trading activity in relation to NSCC's total liquidity resources.

Several commenters raised concerns regarding the perceived burdens on competition and asserted that there are

<sup>105</sup> See Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846, NSCC Letter II. With respect to the comments described above about NSCC requiring cash be deposited as collateral, the Commission believes that NSCC has addressed these comments and has stated that the CALC will evaluate potential alternative collateral approaches.

<sup>99</sup> See Exhibit 5 to File No. SR-NSCC-2013-02, <http://www.sec.gov/rules/sro/nscc/2013/34-70688-ex5.pdf>.

<sup>100</sup> *Id.* See also Notice, 78 FR at 21489.

<sup>101</sup> See Notice of Amendment No. 3, 78 FR at 62847.

<sup>102</sup> *Id.* See also Exhibit 5 to File No. SR-NSCC-2013-02, <http://www.sec.gov/rules/sro/nscc/2013/34-70688-ex5.pdf>.

<sup>103</sup> See Notice of Amendment No. 3, 78 FR at 62847.

<sup>104</sup> See NSCC Letter I.

unfair and discriminatory impacts of the SLD Proposal, in particular with respect to an aspect of the eliminated Regular SLD funding obligation.<sup>106</sup> However, no commenters argued that the Final SLD Proposal discriminated among Clearing Members in the use of the clearing agency or imposed an unnecessary or inappropriate burden on competition. Because a Special SLD funding obligation will be imposed only to the extent that an individual Clearing Member's trading activity over a two-year historical look-back period on corresponding days surpasses the total liquidity resources available to NSCC, only a small number of Clearing Members likely will incur a Special SLD funding obligation. While the Special SLD funding obligation will very likely only be met by a small number of Clearing Members, NSCC (i) will provide all members with a daily report regarding the liquidity exposure presented by such member, (ii) will provide similar monthly reports specifically to Clearing Members to help Clearing Members determine whether they should make Prefund Deposits or otherwise manage their liquidity exposure,<sup>107</sup> and (iii) has created the CALC to ensure that the Special SLD funding obligation will continue to only reasonably and fairly impose a requirement on those Clearing Members that can foresee the liquidity exposure that they may present to NSCC during Special Periods.<sup>108</sup>

As a result, the Commission believes that the Final SLD Proposal meets the requirements of Sections 17A(b)(3)(F) and (I) of the Exchange Act. To the extent the imposition of the Special SLD funding obligation results in a burden on competition because it levies a funding obligation on some Clearing Members but not others, such burden is necessary or appropriate for NSCC to ensure that it has the liquidity resources required to continue to operate in a safe and sound manner. Furthermore, the Special SLD funding obligation does not amount to unfair discrimination among Clearing Members in the use of the clearing agency because the funding requirement is correlated directly with trading activity that creates the actual liquidity need.

<sup>106</sup> See Citadel Letter II, Charles Schwab Letter I, Charles Schwab Letter II, Charles Schwab Letter III, Charles Schwab Letter IV, Charles Schwab Letter V, SIFMA Letter I, SIFMA Letter II, ITG Letter I, ITG Letter II, Knight Capital Letter, ConvergEx Letter I, ConvergEx Letter II.

<sup>107</sup> See Notice of Amendment No. 2, 78 FR 42140, Notice of Amendment No. 3, 78 FR 62846, NSCC Letter II.

<sup>108</sup> See NSCC Letter I, NSCC Letter II.

## VI. 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 and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>109</sup> that the proposed rule change SR–NSCC–2013–02, as modified by Amendment Nos. 1, 2, and 3, be and hereby is *approved*, as of the date of this order or the date of the “Notice of No Objection to Advance Notice Filing, as Modified by Amendment Nos. 1, 2, and 3, to Institute Supplemental Liquidity Deposits to [NSCC’s] Clearing Fund Designed to Increase Liquidity Resources to Meet Its Liquidity Needs,” SR–NSCC–2012–802, whichever is later.

By the Commission.

**Kevin M. O’Neill,**

*Deputy Secretary.*

[FR Doc. 2013–29497 Filed 12–10–13; 8:45 am]

**BILLING CODE 8011–01–P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–70991; File No. SR–BOX–2013–57]

### Self-Regulatory Organizations; BOX Options Exchange LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend Interpretive Material To Rule 5050 To Eliminate the Cap on the Number of Additional Series That May be Listed Per Expiration Month for Each Quarterly Options Series in Exchange-Traded Fund Options

December 5, 2013.

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> notice is hereby given that, on December 3, 2013, BOX Options Exchange LLC (the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule from interested persons.

<sup>109</sup> 15 U.S.C. 78s(b)(2).

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

<sup>2</sup> 17 CFR 240.19b–4.

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

The Exchange proposes to amend interpretive material to Rule 5050 (Series of Options Contracts Open for Trading) to eliminate the cap on the number of additional series that may be listed per expiration month for each Quarterly Option Series (“QOS”) in exchange-traded fund (“ETF”) options. The text of the proposed rule change is available from the principal office of the Exchange, at the Commission’s Public Reference Room and also on the Exchange’s Internet Web site at <http://boxexchange.com>.

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

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

#### 1. Purpose

The Exchange is proposing to amend Interpretive Material (“IM”) 5050–4 to Rule 5050 (Series of Options Contracts Open for Trading) to eliminate the cap on the number of additional series that may be listed per expiration month for each QOS in ETF options.<sup>3</sup> This is a competitive filing that is based on proposals recently submitted by NYSE Arca, Inc. (“NYSE Arca”) and NYSE MKT LLC (“NYSE MKT”) that were recently noticed by the Commission.<sup>4</sup> As set out in IM–5050–4, the Exchange

<sup>3</sup> A Quarterly Option Series is a series of an option class that is approved for listing and trading on the Exchange in which the series is opened for trading on any business day, and that expires at the close of business on the last business day of a calendar quarter. The Exchange lists series that expire at the end of the next consecutive four (4) calendar quarters, as well as the fourth quarter of the next calendar year. See Rule 100(a)(54) and IM–5050–4(a).

<sup>4</sup> See Securities Exchange Act Release Nos. 70855 (November 13, 2013) 78 FR 69493 (November 19, 2013) (Notice of Filing and Immediate Effectiveness of SR–NYSEArca–2013–120) and 070854 (November 13, 2013) 78 FR 69465 (November 19, 2013) (Notice of Filing and Immediate Effectiveness of SR–NYSEMKT–2013–90).