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November 1, 2013

**Via Electronic Mail**

Elizabeth Murphy  
Secretary  
Securities and Exchange Commission  
100 F. Street, N.E.  
Washington, DC 20549-1090

Re: **SR-NSCC-2013-02 and SR-NSCC-2013-802; Notice of Filing Amendment No. 3 to a Proposed Rule Change, as Previously Modified by Amendment Nos. 1 and 2, to Institute Supplemental Liquidity Deposits to Its Clearing Fund Designed to Increase Liquidity Resources to Meet Its Liquidity Needs**

Ms. Murphy:

ITG Inc. (“ITG”),<sup>1</sup> a registered broker-dealer and member of National Securities Clearing Corporation (“NSCC”), appreciates the opportunity to submit this comment letter supplementing our prior letters<sup>2</sup> on the above referenced proposal by NSCC (the “SLD Proposal” or the “Proposed Rule”)<sup>3</sup> and in response to letters submitted by The Depository Trust & Clearing Corporation (“DTCC”). In response to strong objections

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<sup>1</sup> ITG (NYSE: ITG) is an independent execution and research broker that partners with global portfolio managers and traders to provide unique data-driven insights throughout the investment process. From investment decision through trading and settlement, ITG helps clients understand market trends, improve performance, mitigate risk and navigate increasingly complex markets. ITG is headquartered in New York with offices in North America, Europe, and Asia Pacific.

<sup>2</sup> ITG’s comment letters dated April 25<sup>th</sup> and August 5<sup>th</sup> are available at: <http://www.sec.gov/comments/sr-nsc-2013-02/nsc201302.shtml>

<sup>3</sup> Securities Exchange Act Release Nos. 34-69313 (April 4, 2013), 78 FR 21487 (April 10, 2013); 34-69451 (April 25, 2013), 78 FR 25496 (May 1, 2013); 34-70688 (October 15, 2013), 78 FR 62893 (October 22, 2013).

from numerous commenters regarding the SLD Proposal, NSCC recently filed Amendment No. 3 to remove all provisions from the Proposed Rule that collectively would impose Regular Activity Liquidity Obligations on certain NSCC clearing members. This is a very positive development. At the same time, however, NSCC also proposes to maintain the provisions from the SLD Proposal that impose Special Activity Liquidity Obligations for activity relating to monthly options expiry periods. ITG continues to join other commenters in urging NSCC to fully withdraw the Proposed Rule so that work may begin on a better liquidity solution from the ground up for NSCC and the markets that it serves.

ITG supports NSCC's withdrawal of the aspects that collectively impose Regular Activity Liquidity Obligations. The withdrawal, together with NSCC's formation of the Clearing Agency Liquidity Council ("CALC"), are two steps firmly in the right direction. Less encouraging, however, is NSCC's refusal to withdraw the entire SLD Proposal. Failure to do so advances flawed concepts about which commenters have repeatedly identified serious operational, legal, and systemic concerns. It also restricts the ability of the CALC and NSCC to comprehensively redesign a liquidity framework that is safer, more responsible, and more effective. Without any emergency justification by NSCC to rush in place these left over pieces from the SLD Proposal, implementing the Special Activity Liquidity Obligation would be counterproductive to the work of the CALC<sup>4</sup>. The opportunity is needed for a holistic and collaborative approach to this issue. If the CALC is truly meant to promote authentic two-way dialogue about liquidity and liquidity-related financing options (including matters of concern already raised by commenters on the SLD Proposal), all artifacts from the SLD Proposal should be cleared away to let NSCC and the CALC build from the strongest and cleanest foundation.

#### I. The CALC

Subject to some structural concerns, ITG supports the CALC as a welcome answer to calls from clearing members for a more fair voice in designing an enhanced NSCC liquidity framework that they will ultimately help fund. DTCC's aim of selecting CALC members to achieve a diverse representation in terms of industry segment and member impact is a great start and is generally consistent with the requirement for NSCC's policies and procedures to be reasonably designed to support the objectives of

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<sup>4</sup> To be clear, ITG does not object in principle to the concept of supplemental funding around options expiration dates if it is determined that such funding is necessary from a systemic risk perspective, but rather to the implementation of such a requirement by way of the Proposed Rule with its attendant operational, legal and systemic issues.



owners and participants and promote the effectiveness of NSCC’s risk management procedures.<sup>5</sup> ITG looks forward to participating in the CALC and to working with NSCC and other CALC members. However, there are shortcomings in how the CALC is allowed to contribute to the DTCC governance process and promote effective risk management.

Under the CALC Charter, the CALC has no decision making authority and the DTCC Group Chief Risk Officer determines whether any information relating to meetings, discussions and/or notes warrants escalation to the DTCC board or members of DTCC’s executive management.<sup>6</sup> This marginalizes CALC participation in DTCC’s governance through total intermediation and is unnecessary. As a group of skilled industry experts representing participants, the CALC should be able to directly provide information and recommendations to DTCC’s board and/or board committees. In support of a more direct line of communication with the board, ITG agrees with the Commission’s recognition in adopting Rule 17Ad-22(d)(8) that a clearing agency utility model, like that of NSCC, does not negate the need for governance arrangements that support the objectives of owners and participants and that “the board should reflect the interests of the full range of stakeholders to be effective.”<sup>7</sup> With these regulatory objectives in mind, DTCC should modify the CALC Charter to allow the CALC to communicate its views to the DTCC board and relevant committees.

## II. Moving Forward on the SLD Proposal

In moving toward an improved liquidity framework, there are several key points of emphasis on which ITG believes NSCC and the CALC should focus to help ensure the viability of a new solution and as guideposts to avoid pitfalls from the SLD Proposal. These are explained briefly below. We believe it is particularly important to emphasize these points in advance of NSCC’s redevelopment efforts because it is reasonable to expect that familiar ideas from the SLD Proposal will resurface for further discussion and evaluation. To that end, we do not believe that DTCC’s letters and amendments prior to the recent withdrawal either responded to or solved many of the concerns ITG expressed in its comment letters.

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<sup>5</sup> 17 CFR 240.17Ad-22(d)(8).

<sup>6</sup> See DTCC Important Notice, Creation of DTCC Clearing Agency Liquidity Council and nomination process dated September 18, 2013, [http://dtcc.com/downloads/legal/imp\\_notices/2013/nscc/a7706.pdf](http://dtcc.com/downloads/legal/imp_notices/2013/nscc/a7706.pdf)

<sup>7</sup> See Securities Exchange Act Release No. 34-68080 (Oct. 22, 2012), 77 FR 66220, 66252 (Nov. 2, 2012).

First, any revised approach to supplemental liquidity must avoid the preferential Credit Facility treatment for members with affiliate banks that was baked into the SLD Proposal. As ITG explained in detail in its earlier letters, NSCC's decision to intertwine the Credit Facility and Regular Activity Liquidity Obligations and to extend a dollar-for-dollar credit to members that provided Commitments as Lenders imposed an undue burden on clearing members that do not have bank affiliates.

At DTCC's own acknowledgment, NSCC's ability to significantly increase the size of the Credit Facility in 2013 was in large part because clearing members anticipated the need to comply with the coming demands of the SLD Proposal.<sup>8</sup> In response to commenters, including ITG, DTCC contended that the dollar-for-dollar credit incentive could not be preferential to bank affiliated clearing members because banks have legal obligations to deal with affiliates at arms' length.<sup>9</sup> In practice, however, the basic structure meant that a clearing member, its bank affiliate, and corporate family were confronted with a choice to commit to the Credit Facility and avoid cash contributions for the Regular Activity Liquidity Obligation or to pay cash to NSCC that could otherwise be used in the clearing member's core business. From this view, the structure necessarily created a framework where decisions by affiliate banks and corporate families could not be disinterested—and the result was the 2013 spike in funding for the Credit Facility that DTCC documented. DTCC's expansion of the designated lender definition through Amendment No. 2 to permit a clearing member to find a designated lender to commit on its behalf was of value, but it did not unwind the fundamental advantage given to bank affiliate members or adequately establish a meaningful framework in NSCC's rules to give non-bank affiliate clearing members reliable access to participation in the Credit Facility. Going forward, ITG continues to stress that if NSCC can demonstrate a need for supplemental liquidity that exceeds the size of the Credit Facility, then the funding obligation for clearing members required to contribute to that need should be limited to allocations that are designed in the aggregate to meet the amount of the shortfall.

ITG also previously identified technical deficiencies with how the mechanics of the Proposed Rule would allocate Regular Activity Liquidity Obligations. In our letter of August 5<sup>th</sup>, we provided several numerical examples demonstrating in detail the ways in which the flawed nexus between the Credit Facility and the supplemental liquidity deposit requirements rendered the Proposed Rule arbitrary and capricious and

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<sup>8</sup> See Letter from Larry E. Thompson, Managing Director and General Counsel, DTCC, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, at 3 (August 20, 2013).

<sup>9</sup> *Id.* at pg. 10.

inconsistent with the standards of the Securities Exchange Act. In its letter of August 20, 2013, DTCC provided a numerical response in the form of Appendix A meant to demonstrate the intent of NSCC's allocation process. These calculations failed to resolve the questions ITG raised and the main formula in Appendix A that DTCC used to buttress the intended operation of the Proposed Rule was never included in the rule text itself. Going forward, any replacement liquidity solution must be fully and accurately reflected in NSCC's proposed rules. Intended operation cannot be accepted as actual operation. NSCC's rules have the force of law<sup>10</sup> and they should be crafted with the care and detail that is commensurate with that responsibility.

The future liquidity solution developed by NSCC and the CALC should also include a much more significant implementation period than was contemplated as part of the SLD Proposal. The implementation period needs to be calibrated to recognize that changes in the structure and costs of clearing have a very real impact on how clearing members run and structure their businesses. One of the last things a systemically important clearing agency like NSCC should do in moving to a new risk management approach is to do so with such speed that it risks causing a rushed and disorderly transition by market participants out of and into the clearing system. In addition to the need for an adequate transition plan, we note that there is still no guidance from the Commission concerning how clearing member deposits to a supplemental liquidity framework will be treated for net capital purposes. This includes clearing member deposits for the Special Activity Liquidity Obligations that NSCC has retained in the Proposed Rule and on which it still seeks Commission approval. The potential financial ramifications for clearing members of this regulatory uncertainty is yet another strong reason why NSCC should withdraw the SLD Proposal in full and not force into place its remaining pieces.

### III. Conclusion

NSCC's withdrawal of the Regular Activity Liquidity Obligation is a very important development toward a clear path for NSCC and the CALC to put in place a better and safer liquidity solution. ITG urges NSCC to create the best possible conditions for success by completely withdrawing the Proposed Rule and amending the CALC Charter. ITG welcomes the CALC and other opportunities to continue to engage with DTCC and other NSCC clearing members on these issues.

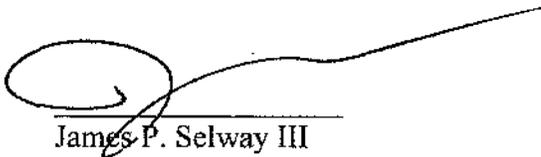
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<sup>10</sup> 15 U.S.C. 78s(g)(1)(C).

If you have any questions, please do not hesitate to call Jamie Selway at (212) 444-6306, or Mark Solomon at (212) 444-6201.

Sincerely,



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Managing Director  
Head of Electronic Brokerage



Mark Solomon  
Managing Director  
Deputy General Counsel

cc: The Honorable Mary Jo White, Chair  
The Honorable Luis A. Aguilar, Commissioner  
The Honorable Daniel M. Gallagher, Commissioner  
The Honorable Michael S. Piwowar, Commissioner  
The Honorable Kara M. Stein, Commissioner  
Mr. John Ramsay, Acting Director, Division of Trading and Markets  
Mr. Peter Curley, Associate Director, Division of Trading and Markets  
Mr. Michael Macchiaroli, Associate Director, Division of Trading and Markets  
Mr. Joseph Kamnik, Assistant Director, Division of Trading and Markets  
Mr. Larry E. Thompson, Managing Director and General Counsel, DTCC