

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50955; File No. SR-FICC-2004-05)

January 3, 2005

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Order Granting Approval of a Proposed Rule Change to Amend Rules Relating to the Participants Fund Deposit Requirements of its Mortgage-Backed Securities Division

I. Introduction

On March 3, 2004, the Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) and on March 11, 2004, amended proposed rule change File No. SR-FICC-2004-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”).¹ Notice of the proposed rule change was published in the Federal Register on November 22, 2004.² No comment letters were received. For the reasons discussed below, the Commission is now granting approval of the proposed rule change.

II. Description

The proposed rule change amends the rules of FICC’s Mortgage-Backed Securities Division (“MBSD”) to eliminate the basic deposit component of the Participants Fund deposit requirement for participants that are registered with the Commission as registered investment companies (“RICs”) pursuant to the Investment Company Act of 1940.³

In 2003, FICC received a no-action letter⁴ from the Commission’s Division of Investment Management (“IM”) stating that IM would not recommend to the Commission enforcement action

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 50665 (November 15, 2004), 69 FR 67972.

³ 15 U.S.C. 80a-1.

⁴ No-Action Letter under the Investment Company Act of 1940 – Section 17(f) and Rule 17f-4, to Fixed Income Clearing Corporation (March 13, 2003).

under Section 17(f) of the Investment Company Act of 1940 against any RIC or its custodian if the RIC or its custodian placed the RIC's cash and/or securities in the custody of the MBSD for purposes of meeting the Participants Fund requirements imposed by the MBSD. IM's no-action letter was based upon the fact that the main portions of the MBSD's Participants Fund, the "minimum market margin differential deposit" and the "market margin differential deposit," are intended to benefit the non-defaulting participants of the MBSD because these portions are intended to provide assurances that each participant's contributions to the Participants Fund will be adequate to satisfy all open commitments recorded with the MBSD. In contrast, the remaining portion of the Participants Fund, the "basic deposit," is designed to protect FICC by ensuring that each participant's fees owing to the MBSD will be paid if the participant is unable to meet such fee obligations.

In granting no-action relief to FICC, IM staff relied upon FICC's representation that RICs would be exempt from the basic deposit requirement. FICC determined that this representation would not subject it to undue risk because the basic deposit is a relatively minimal amount and because this exemption affects very few participants.⁵ The management of FICC returned the basic deposits posted by its RIC clearing members under perceived authority given to it under Article IV, Rule 1, Section 3 of its Rules. FICC nonetheless believes it would be prudent to expressly state in the MBSD Rules that RICs are exempt from the basic deposit requirement.⁶

⁵ Currently, the basic deposit is determined semiannually and is the greater of (a) \$1,000 or (b) the participant's average monthly bill (per account) with a maximum of \$10,000. The MBSD currently has only two RIC clearing members.

⁶ FICC will also state in the MBSD's Schedule of Charges that the basic deposit does not apply to RICs.

III. Discussion

Section 17A(b)(3)(F) of the Act requires among other things that the rules of a clearing agency be designed to assure the safeguarding of securities and funds in its custody or control or for which it is responsible.⁷ The Commission finds that FICC's proposed rule change is consistent with this requirement because by exempting RICs from its basic deposit requirement, FICC is enabling RICs to become participants while still doing so in a manner that allows FICC to safeguard the securities and funds in its custody or control or for which it is responsible.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular Section 17A of the Act and the rules and regulations thereunder.

⁷ 15 U.S.C. 78q-1(b)(3)(F).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁸ that the proposed rule change (File No. SR-FICC-2004-05) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁹

Jill M. Peterson
Assistant Secretary

⁸ 15 U.S.C. 78s(b)(2).

⁹ 17 CFR 200.30-3(a)(12).