

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54682; File No. SR-FICC-2006-15)

November 1, 2006

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change to Modify its Rules to Diversify and Standardize Clearing Fund Collateral Requirements Across the Divisions to Improve Liquidity and Minimize Risk for its Members

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on October 4, 2006, the Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II, and III below, which items have been prepared primarily by FICC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested parties.

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

The proposed rule change seeks to modify the rules of both of the Government Securities Division (“GSD”) and the Mortgage-Backed Securities Division (“MBSD”) (collectively, the “Divisions”) of FICC to diversify and standardize Clearing Fund³ collateral requirements across the Divisions in order to improve liquidity and minimize risk for FICC and its members.⁴

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ The GSD Rules refer to member collateral deposits as the “Clearing Fund” while the MBSD rules refer to these deposits as the “Participants Fund.” The term “Clearing Fund” in this rule filing will refer to both.

⁴ This rule filing also proposes to make a minor technical change to Rule 4 of the GSD rules. Section 2 of Rule 4 has been relettered to accommodate changes made in an earlier FICC rule filing, SR-FICC-2006-12.

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

In its filing with the Commission, FICC 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. FICC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.⁵

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

Presently, both GSD and MBSD members may satisfy their Clearing Fund requirement with cash deposits. Members may also satisfy a portion of their deposits with an open account indebtedness fully secured by certain types of securities and/or letters of credit. FICC proposes to modify its rules as detailed below to: 1) expand the types of securities which members may deposit to satisfy their Clearing Fund requirement ("Eligible Clearing Fund Securities") to secure their open account indebtedness; 2) establish concentration requirements with regard to members' use of Eligible Clearing Fund Securities; 3) create a correlating range of haircuts to be applied to the expanded types of Eligible Clearing Fund Securities; and 4) eliminate letters of credit as a generally acceptable form of collateral securing members' open account Clearing Fund indebtedness.

⁵ The Commission has modified the text of the summaries prepared by FICC.

1. Revised Clearing Fund Components

(a) Cash

Currently the rules of GSD require that the greater of \$100,000 or ten percent of a member's Clearing Fund requirement with a maximum of \$500,000 be made in the form of cash.⁶ The rules of MBSD currently do not contain a minimum cash requirement. For both Divisions, the proposed new cash collateral component will be the lesser of \$500,000 or ten percent of a member's Clearing Fund requirement with a minimum of \$100,000.

(b) Securities

Currently each Division of FICC accepts different types of securities as Clearing Fund collateral. For example, GSD accepts Agency securities but not mortgage-backed securities, and MBSD accepts mortgage-backed securities but not Agency securities. In addition, there are currently no concentration requirements placed on the securities deposited at either Division. In an effort to standardize the securities which are eligible as Clearing Fund collateral across the Divisions, FICC proposes to modify the rules of both Divisions by adding a definition to each Division's rules for "Eligible Clearing Fund Securities" (with respect to GSD) and "Eligible Participants Fund Securities" (with respect to MBSD). As defined, these securities will be unmatured bonds which are either an "Eligible Clearing Fund Agency Security," an "Eligible Clearing Fund Mortgage-Backed Security" or an "Eligible Clearing Fund Treasury Security."⁷ "Eligible Clearing Fund Agency Security" would be defined as a direct obligation of those U.S. agencies or government sponsored enterprises as FICC may designate from time to time that

⁶ GSD Rule 4, Section 2(b)(ii).

⁷ In the MBSD Rules, these terms would be as follows: "Eligible Participants Fund Agency Security," "Eligible Participants Fund Mortgage-Backed Security," and "Eligible Participants Fund Treasury Security."

satisfies the criteria set forth in notices issued by FICC from time to time. “Eligible Clearing Fund Mortgage-Backed Security” would be defined as a mortgage-backed pass through obligation issued by those U.S. agencies or government sponsored enterprises as FICC may designate from time to time that satisfies the criteria set forth in notices issued by FICC from time to time. “Eligible Clearing Fund Treasury Security” would be defined as a direct obligation of the U.S. government that satisfies the criteria set forth in notices issued by FICC from time to time.

Initial eligibility criteria for each type of Eligible Clearing Fund/Participant Fund Security will be announced to members through an Important Notice prior to the effective date of this proposed rule change. Any future changes to the eligibility criteria will also be announced to members through Important Notices in advance of such changes becoming effective.

(c) Security Concentration Provisions

FICC also proposes to establish security concentration provisions for Clearing Fund deposits. As proposed, a minimum of forty percent of a member’s required Clearing Fund deposit would have to be made in cash and Eligible Clearing Fund Treasury Securities. The remainder of a member’s deposit could be secured by cash and the pledge of Eligible Clearing Fund Securities in any combination of Eligible Clearing Fund Treasury Securities, Eligible Clearing Fund Agency Securities, and/or Eligible Clearing Fund Mortgage-Backed Securities. However 1) any deposits of Eligible Clearing Fund Agency Securities or Eligible Clearing Fund Mortgage-Backed Securities, respectively, in excess of twenty-five percent of a member’s required Clearing Fund deposit would be subject to an additional haircut equal to twice the percentage specified in the haircut schedule. Furthermore, no more than twenty percent of a member’s required Clearing Fund deposit could be secured by pledged Eligible Clearing Fund

Agency Securities of a single issuer. Lastly, no member would be permitted to post as Clearing Fund collateral Eligible Clearing Fund Agency Securities for which it is the issuer.⁸

(d) Letters of Credit and Other Adequate Assurances

The current provisions within FICC's Rules that pertain to Letter of Credit Issuers will be modified to reflect that letters of credit would no longer be accepted by FICC as a form of Clearing Fund collateral.⁹ Effective April 1, 2007 (which is the regular expiration date of letters of credit), members that have letters of credit posted as collateral (other than members, if any, that have been required to post letters of credit for legal risk), would be required to replace the portion of the Clearing Fund collateralized by letters of credit with either cash or Eligible Clearing Fund Securities.

(e) Implementation Timeframes

The foregoing rule changes would become effective thirty days after an Important Notice is issued to members informing them that FICC's systems are ready to accommodate such changes. The corresponding changes to FICC's rules would be made at that time.

⁸ However, a member would be permitted to pledge Eligible Clearing Fund Mortgage-Backed Securities for which it is the issuer subject to a haircut. The haircut would be fourteen percent as an initial matter. If the member exceeded the twenty-five percent concentration limit, the haircut would be twenty-one percent.

⁹ FICC has found that in practice letters of credit are not as liquid as cash and securities and therefore pose more risk to FICC and its members when pledged as Clearing Fund collateral. FICC will, however, reserve the right to require letters of credit from members in those instances where a particular member has been found, by FICC in its discretion, to present legal risk.

(f) Alternative Proportions of Eligible Collateral

As is currently the case under FICC's rules, FICC will continue to reserve the right to require different proportions of the Clearing Fund collateral components as necessary to address any heightened legal or insolvency risks presented by a member.¹⁰

FICC believes the proposed rule change is consistent with the requirements of Section 17A of the Act¹¹ and the rules and regulations thereunder because it will enable FICC to standardize acceptable forms of collateral across both of its Divisions, which should lead to an increase of liquidity and a decrease of risk to FICC and its members. As such, FICC believes it will better enable FICC to safeguard the securities or funds in its possession or control or for which it is responsible.

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

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

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

Written comments relating to the proposed rule change have not yet been solicited or received. FICC will notify the Commission of any written comments received by FICC.

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:

¹⁰ GSD Rule 4, Section 2(o), MBSD Rule 2, Section 4 of Article IV.

¹¹ 15 U.S.C. 78q-1.

- (A) by order approve such proposed rule change or
- (B) institute proceedings to determine whether the proposed rule change should be

disapproved.

IV. Solicitation of Comments

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

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FICC-2006-15 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FICC-2006-15. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section, 100 F

Street, NE, Washington, DC 20549. Copies of such filings also will be available for inspection and copying at the principal office of FICC and on FICC's Web site at <http://www.ficc.com/gov/notices/GOV115.06.htm?NS-query>. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FICC-2006-15 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission by the Division of Market Regulation, pursuant to delegated authority.¹²

Nancy M. Morris
Secretary

¹² 17 CFR 200.30-3(a)(12).