

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-73787; File No. SR-FICC-2014-06)

December 8, 2014

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change to Amend the Rules of the Government Securities Division and the Mortgage-Backed Securities Division on Insolvency and Ceasing to Act

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”)¹, and Rule 19b-4 thereunder,² notice is hereby given that on November 25, 2014, Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the clearing agency. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

The proposed rule change consists of amendments to the rules of the Government Securities Division (“GSD Rules”) of FICC and the rules of the Mortgage-Backed Securities Division (“MBSD Rules”) of FICC (each of GSD and MBSD, a “Division” of FICC) on insolvency and ceasing to act that simplify in certain respects FICC’s process in a cease to act situation and provide greater legal certainty for FICC and its members, particularly in an intra-day cease to act situation.

II. Clearing Agency’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.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

FICC has prepared summaries, set forth in sections A, B and C below, of the most significant aspects of such statements.

A. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to amend the GSD Rules and the MBSD Rules on insolvency and ceasing to act in order to simplify in certain respects FICC’s process in a cease to act situation and provide greater legal certainty for FICC and its members, particularly in an intra-day cease to act situation.

Background

In connection with lessons learned from a recent close-out simulation exercise conducted by The Depository Trust & Clearing Corporation, FICC’s parent company, in which FICC participated, and related review of the GSD Rules and the MBSD Rules, certain potential challenges with administering certain aspects of the GSD Rules and the MBSD Rules on insolvency and ceasing to act described below, particularly in an intra-day cease to act situation, were identified.

“Time of Insolvency” and “Cut-Off Time”

Currently, GSD and MBSD include in their insolvency rules (GSD Rule 22, MBSD Rule 16) and cease to act rules (GSD Rule 22A, MBSD Rule 17) the concept of a “Time of Insolvency”, which is defined to mean the time at which FICC determines to its reasonable satisfaction that a member is “insolvent” within the meaning of GSD Rule 22 or MBSD Rule 16, respectively.

This “Time of Insolvency” concept is separate from the time at which FICC ceases to act for a member, and such “Time of Insolvency” is currently used in the GSD Rules and the MBSD

Rules as a line of demarcation when determining FICC’s obligations with respect to pending transactions involving the insolvent member. Specifically, transactions with the insolvent member that are not compared or deemed compared in accordance with the GSD Rules or the MBSD Rules, respectively, prior to the “Time of Insolvency” are not eligible to be part of the close-out process, unless otherwise determined by the Board of Directors of FICC in order to promote orderly settlement.

For a non-insolvency cease to act situation, the GSD Rules and the MBSD Rules on ceasing to act (GSD Rule 22A, MBSD Rule 17) currently include the concept of a “Cut-Off Time”, which is defined to mean a time specified in advance by FICC in a notice to its membership at which it will cease to act for a member. Like the “Time of Insolvency” concept, “Cut-Off Time” is currently used in the GSD Rules and the MBSD Rules when determining FICC’s obligations with respect to pending transactions involving the defaulted member.

Identifying an exact time at which a member has become “insolvent” for purposes of establishing a “Time of Insolvency” may pose potential challenges for FICC in circumstances where the member is deemed “insolvent” based upon the determination or action of a third party, such as the member’s regulator, supervisory authority or a court of competent jurisdiction. In an intra-day cease to act situation where transaction data is being submitted to FICC in real-time, these potential challenges with identifying an exact “Time of Insolvency” may create a lack of legal certainty for FICC and its members regarding FICC’s obligations with respect to pending transactions involving the insolvent member. In light of the foregoing, FICC proposes to remove the “Time of Insolvency” concept from the GSD Rules and the MBSD Rules and instead simply rely on the single time it ceases to act for an insolvent member for purposes of determining its obligations with respect to pending transactions involving such insolvent member.

In order to also simplify its process in non-insolvency cease to act situations, FICC

proposes to remove the separate “Cut-Off Time” concept from the GSD Rules and the MBSD Rules and instead rely on the single time it ceases to act for a defaulted member for purposes of determining its obligations with respect to pending transactions involving such defaulted member.³

Transactions Deemed Compared Based Solely on Non-Defaulting Member Data

Currently, the provisions of the GSD Rules and the MBSD Rules on ceasing to act (GSD Rule 22A, MBSD Rule 17), and the related prongs of the “Compared Trade” definition in Rule 1 of each of the Division’s Rules, provide that, in the context of FICC ceasing to act for a member, a transaction involving such member that would not otherwise be compared or deemed compared under the GSD Rules or the MBSD Rules, respectively, may, in certain circumstances, be deemed a compared trade based solely on data submitted by a non-defaulting member. The determination of whether such a transaction should be deemed a compared trade is currently based on a multi-pronged facts and circumstances-based test, including determinations as to whether the transaction was executed prior to FICC ceasing to act for the defaulted member, whether the transaction was entered into in good faith and not primarily in order to take advantage of the defaulted member’s financial condition and whether the transaction is an Off-the-Market Transaction as defined in Rule 1 of each of the Division’s Rules.

Administering such a multi-pronged facts and circumstances-based test for individual transactions in a cease to act situation, particularly an intra-day cease to act situation where transaction data is being submitted to FICC in real-time, may pose potential challenges to FICC

³ It should be noted that this proposed change will more closely align the GSD Rules and the MBSD Rules with the rules of FICC’s affiliate, National Securities Clearing Corporation (“NSCC”). Under its Rule 18 (Procedures for When the Corporation Declines or Ceases to Act), NSCC relies on the time it declines or ceases to act for a member when determining which transactions involving such member will be excluded from its operations, rather than on a separate “Time of Insolvency” or “Cut-Off Time”, as applicable.

and create a lack of legal certainty for FICC and its members regarding FICC's obligations with respect to individual pending transactions involving the insolvent or otherwise defaulted member. In order to simplify FICC's process in a cease to act situation and provide FICC and its members with greater ex ante legal certainty regarding the rules applicable to pending transactions involving an insolvent or otherwise defaulted member, FICC proposes to remove the multi-pronged facts and circumstances-based test and the related provisions of each of the Division's Rules and instead simply rely on the compared trade definitions under each of the Division's Rules, subject to the discretion of the Board of Directors of FICC to determine otherwise in order to promote orderly settlement with respect to transactions the data on which have been submitted only by non-defaulting members.

Proposed GSD Rule Changes

FICC is proposing to amend the GSD Rules as follows:

In Rule 1 – “Definitions”, the following definitions have been revised:

The term “Compared Trade” is revised to remove the prong of the definition which provides that, in the context of FICC ceasing to act for a member under GSD Rule 22A, a transaction involving such member that would not otherwise be a Compared Trade under the GSD Rules may, in certain circumstances, be deemed a Compared Trade based solely on data submitted by a non-defaulting member.

The term “Off-the-Market Transaction” is revised to conform the text and the numbering of the definition with the text and numbering of the parallel “Off-the-Market Transaction” definition in the MBSD Rules.

In Rule 3A – “Sponsoring Members and Sponsored Members”, Sections 15(a) and 16(a) are revised to remove references to Rule 22, current Section 3 (Notification of Insolvency) and related conforming changes to the text of such sections are made. Section 15(b) is revised to

remove the reference to the “Time of Insolvency” concept and to align the text regarding the actions taken by FICC in connection with the insolvency of a Sponsored Member with the parallel text included in Section 16 relating to the actions taken by FICC in connection with the insolvency of a Sponsoring Member. Consistent with the numbering of Section 15, Section 16(a) is revised to make the second paragraph a new subsection (b). New Section 16(b) is also revised to align the text regarding the actions taken by FICC in connection with the insolvency of a Sponsoring Member with the parallel text included in Section 15(b) relating to the actions taken by FICC in connection with the insolvency of a Sponsored Member.

In Rule 22 – “Insolvency of a Member”, current Section 3, which provides for FICC to notice its membership and the Securities and Exchange Commission (SEC) regarding the insolvency of a member, is removed in order to clarify that the membership and the SEC will only receive one notice from FICC at the time it ceases to act for a member in accordance with the provisions of Section 1 of Rule 22A (Procedures for When the Corporation Ceases to Act), whether FICC ceases to act for the member for insolvency or non-insolvency related reasons. Section 4 (Ceasing to Act for the Member) is renumbered as new Section 3 and revised to remove the reference to the “Time of Insolvency” concept.

In Rule 22A – “Procedures for When the Corporation Ceases to Act”, Section 1 (Notification) is revised to clarify that FICC will notice the SEC as well as its membership of every decision to cease to act for a member. Section 1 is further revised to remove the requirement that FICC establish a separate “Time of Insolvency”, in the event it ceases to act because of a member’s insolvency, or “Cut-Off Time”, in the event it ceases to act for a member for non-insolvency related reasons.

Sections 2, 2(a) and 2(b) are revised remove the “Time of Insolvency” and “Cut-Off Time” concepts, and instead rely on the time FICC ceases to act for a member for purposes of

determining its obligations with respect to pending transactions involving such member. Section 2(a) is further revised to use the defined term “Compared Trade” for purposes of clarifying which transactions are eligible to be part of the close-out process as of the time FICC ceases to act for a member, subject to the discretion of the Board of Directors of FICC to determine otherwise in order to promote orderly settlement.

Section 2(c), which provides that, in the context of FICC ceasing to act for a member, a transaction involving such member that would not otherwise be compared or deemed compared under the GSD Rules may, in certain circumstances, be deemed compared based solely on data submitted by a non-defaulting member, based on a multi-pronged facts and circumstances-based test, is removed. FICC would instead rely on the “Compared Trade” definition in GSD Rule 1 when determining its obligations with respect to pending transactions involving an insolvent or otherwise defaulted member, subject to the discretion of the Board of Directors of FICC to determine otherwise in order to promote orderly settlement with respect to transactions the data on which have been submitted only by non-defaulting members.

Proposed MBSD Rule Changes

FICC is proposing to amend the MBSD Rules as follows:

In Rule 1 – “Definitions”, the following definitions have been revised:

The term “Compared Trade” is revised to remove the prong of the definition which provides that, in the context of FICC ceasing to act for a member under MBSD Rule 17, a transaction involving such member that would not otherwise be compared or deemed compared under the MBSD Rules may, in certain circumstances, be deemed a Compared Trade based solely on data submitted by a non-defaulting member. The “Compared Trade” definition is further clarified to reference the specific MBSD Rules (Rule 5 and Rule 7) pursuant to which a transaction would be compared or deemed compared by MBSD.

In Rule 16 – “Insolvency of a Member”, current Section 3, which provides for FICC to notice its membership and the Securities and Exchange Commission (SEC) regarding the insolvency of a member, is removed in order to clarify that the membership and the SEC will only receive one notice from FICC at the time it ceases to act for a member in accordance with the provisions of Section 1 of Rule 17 (Procedures for When the Corporation Ceases to Act), whether FICC ceases to act for the member for insolvency or non-insolvency related reasons. Section 4 (Ceasing to Act for the Member) is renumbered as new Section 3 and revised to remove the reference to the “Time of Insolvency” concept.

In Rule 17 – “Procedures for When the Corporation Ceases to Act”, Section 1 (Notification) is revised to clarify that FICC will notice the SEC as well as its membership of every decision to cease to act for a member. Section 1 is further revised to remove the requirement that FICC establish a separate “Time of Insolvency”, in the event it ceases to act because of a member’s insolvency, or “Cut-Off Time”, in the event it ceases to act for a member for non-insolvency related reasons.

Sections 2, 2(a), 2(d) and 2(e) are revised to remove the “Time of Insolvency” and “Cut-Off Time” concepts, and instead rely on the time FICC ceases to act for a member for purposes of determining its obligations with respect to pending transactions involving such member.

Section 2(g), which provides that, in the context of FICC ceasing to act for a member, a transaction involving such member that would not otherwise be compared or deemed compared under the MBSD Rules may, in certain circumstances, be deemed compared based solely on data submitted by a non-defaulting member, based on a multi-pronged facts and circumstances-based test, is removed. FICC would instead rely on the compared trade definitions in the MBSD Rules when determining its obligations with respect to pending transactions involving an insolvent or otherwise defaulted member, subject to the discretion of the Board of Directors of FICC to

determine otherwise in order to promote orderly settlement with respect to transactions the data on which have been submitted only by non-defaulting members.

2. Statutory Basis

The proposed rule is consistent with Section 17A(b)(3)(F)⁴ of the Securities and Exchange Act of 1934, as amended, and the rules and regulations promulgated thereunder because it will promote the prompt and accurate clearance and settlement of securities transactions and remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions in that it will simplify in certain respects FICC's process in a cease to act situation and provide greater legal certainty for FICC and its members as to FICC's obligations with respect to pending transactions involving an insolvent or otherwise defaulted member, particularly in an intra-day cease to act situation.

B. Clearing Agency'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 because it relates to changes to FICC's insolvency and cease to act rules that would apply equally to all members of each Division of FICC.

C. Clearing Agency'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 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer

⁴ 15 U.S.C. 78q-1(b)(3)(F).

period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

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

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

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-comment@sec.gov. Please include File No. SR-FICC-2014-06 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FICC-2014-06. 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 website (<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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 am and 3:00 pm. Copies of the filing also will be available for inspection and copying at the principal office of FICC and on its website at <http://www.dtcc.com/~media/Files/Downloads/legal/rule-filings/2014/ficc/SR-FICC-2014-06.pdf>.

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 submission should refer to File Number SR-FICC-2014-06 and should be submitted on or before [insert 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁵

Kevin M. O'Neill
Deputy Secretary

⁵ 17 CFR 200.30-3(a)(12).