SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-78774; File No. SR-DTC-2016-003)

September 6, 2016

Self-Regulatory Organizations; The Depository Trust Company; Notice of Filing of Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as Modified by Amendment No. 1, to Impose Deposit Chills and Global Locks and Provide Fair Procedures to Issuers

I. Introduction

On May 27, 2016, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-DTC-2016-003 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] and Rule 19b-4 thereunder.[2] The proposed rule change was published in the Federal Register on June 9, 2016.[3] The Commission received eight comment letters to the proposed rule change from five commenters, including two response letters from DTC.[4]

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 77991 (June 3, 2016), 81 FR 37232 (June 9, 2016) (SR-DTC-2016-003) ("Notice").

4 See letter from Charles V. Rossi, Chairman, The Securities Transfer Association ("STA"), Inc. Board Advisory Committee, dated June 30, 2016, to Brent J. Fields, Secretary, Commission ("STA Letter I"); letter from Dorian Deyet, dated June 30, 2016 ("Deyet Letter"); letter from Ann K. Shuman, Managing Director and Deputy General Counsel, DTC, dated July 21, 2016, to Brent J. Fields, Secretary, Commission ("DTC Letter I"); letter from Harvey Kesner ("Kesner"), Sichenzia, Ross, Friedman, Ference, dated August 11, 2016, to Brent J. Fields, Secretary, Commission ("Kesner Letter I"); letter from Isaac Montal, Managing Director and Deputy General Counsel, DTC, dated August 22, 2016, to Brent J. Fields, Secretary, Commission ("DTC Letter II"); letter from Charles V. Rossi, Chairman, STA Board Advisory Committee, dated August 29, 2016, to Brent J. Fields, Secretary, Commission ("STA Letter II"); letter from Kesner, Sichenzia, Ross, Friedman, Ference, dated August 30, 2016, to Brent J. Fields, Secretary, Commission ("Kesner Letter II"); and letter from Norman B. Arnoff ("Arnoff"),

Pursuant to Section 19(b)(2) of the Act,[5] on July 21, 2016, the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.[6] On July 29, 2016, DTC filed Amendment No. 1 to the proposed rule change, as discussed below.

The Commission is publishing this notice and order to solicit comments on Amendment No. 1 from interested persons and to institute proceedings under Section 19(b)(2)(B) of the Act[7] to determine whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1. The institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved, nor does it mean that the Commission will ultimately disapprove the proposed rule change. Rather, the Commission seeks and encourages interested persons to provide additional comment on the proposed rule change to inform the Commission's analysis of whether to approve or disapprove the proposed rule change.

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dated September 4, 2016 to Secretary Fields ("Arnoff Letter"). See comments on the proposed rule change (SR-DTC-2016-003), https://www.sec.gov/comments/sr-dtc-2016-003/dtc2016003.shtml.

5 15 U.S.C. 78s(b)(2).

6 See Securities Exchange Act Release No. 78379 (July 21, 2016), 81 FR 49309 (July 27, 2016). The Commission designated September 7, 2016, as the date by which it should approve, disapprove, or institute proceedings to determine whether to disapprove the proposed rule change.

7 15 U.S.C. 78s(b)(2)(B).

II. Description of the Proposed Rule Change and Notice of Filing of Amendment No. 1

The proposed rule change, as modified by Amendment No. 1, would add Rule 33 to the Rules, By-Laws and Organization Certificate of DTC ("Rules") to establish: (i) the circumstances under which DTC would impose and release a restriction on Deposits of an Eligible Security ("Deposit Chill") or on book-entry services for an Eligible Security ("Global Lock"); and (ii) the fair procedures for notice and an opportunity for the issuer of the Eligible Security ("Issuer") to challenge the Deposit Chill or Global Lock (each, a "Restriction"), as described below.[8]

A. Background

i. DTC

DTC stated that it is the nation's central securities depository, registered as a clearing agency under Section 17A of the Act,[9] and that its deposit and book-entry transfer services help facilitate the operation of the nation's securities markets. According to DTC, by serving as registered holder of trillions of dollars of Securities, on a daily basis, DTC processes enormous volumes of securities transactions facilitated by book-entry movement of interests, without the need to transfer physical certificates.

DTC performs services and maintains Securities Accounts for its Participants, primarily banks and broker dealers, pursuant to its Rules and Procedures. Participants

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8 The description of the proposed rule change herein is based on the statements prepared by DTC in the Notice. Notice, supra note 3, 81 FR at 37232–36. Each capitalized term not otherwise defined herein has its respective meaning as set forth in the Rules, available at http://www.dtcc.com/legal/rules-and-procedures.aspx.

9 See Securities Exchange Act Release No. 20221 (September 23, 1983), 48 FR 45167 (October 3, 1983) (600-1).

agree to be bound by DTC's Rules and Procedures as a condition of their DTC membership.[10] DTC allows a Participant to present Securities to be made eligible for DTC's depository and book-entry services. If a Security is accepted by DTC as meeting DTC's eligibility requirements for services[11] and is deposited with DTC for credit to the Securities Account of a Participant, it becomes an Eligible Security. Thereafter, DTC explained, Participants may deposit shares of that Eligible Security into their respective DTC accounts. To facilitate book-entry transfers and other services that DTC provides for its Participants with respect to Deposited Securities, DTC explained that the Deposited Securities are generally registered on the books of the Issuer (typically, in a register maintained by a transfer agent) in DTC's nominee name, Cede & Co. DTC further explained that Deposited Securities that are eligible for book-entry services are maintained in "fungible bulk," (i.e., each Participant whose Securities of an issue have been credited to its Securities Account has a pro rata (proportionate) interest in DTC's entire inventory of that issue, but none of the Securities on deposit are identifiable to or "owned" by any particular Participant).[12]

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10 See supra note 8.

11 See Rule 5, supra note 8; DTC Operational Arrangements (Necessary for Securities to Become and Remain Eligible for DTC Services), January 2012 (the "Operational Arrangements"), Section 1, available at http://www.dtcc.com/~/media/Files/Downloads/legal/issue-eligibility/eligibility/operational-arrangements.pdf.

12 See Securities Exchange Act Release No. 19678 (April 15, 1983), 48 FR 17603, 17605, n.5 (April 25, 1983) (describing fungible bulk); see also N.Y. UNIFORM COMMERCIAL CODE, § 8-503, OFF. CMT 1 (". . . all entitlement holders have a pro rata interest in whatever positions in that financial asset the [financial] intermediary holds").

ii. Deposit Chills and Global Locks: Prior Procedures

According to DTC, previously, upon detecting suspiciously large deposits of a thinly traded Eligible Security, DTC imposed or proposed to impose a Deposit Chill as a measure to maintain the status quo while, pursuant to its Operational Arrangements,[13] DTC would then require the Issuer to confirm by legal opinion of independent counsel that the Eligible Security fulfilled the requirements for eligibility. DTC explained that the Deposit Chill would be maintained until the Issuer provided a satisfactory legal opinion, and that the Deposit Chill could remain in place for years, due to an Issuer's non-responsiveness, refusal, or inability to submit the required legal opinion.

With respect to Global Locks, DTC explained that it previously imposed a Global Lock on an Eligible Security when a governmental or regulatory authority commenced a proceeding or action alleging violations of Section 5 of the Securities Act of 1933, as amended, with respect to such Eligible Security. A Global Lock could be released when the underlying enforcement action was withdrawn, dismissed on the merits with prejudice, or otherwise resolved in a final, non-appealable judgment in favor of the defendants allegedly responsible for the violations of federal securities laws. However, DTC stated that many enforcement actions are only resolved after several years[14] and commonly without any definitive determination of wrongdoing.[15]

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13 See Operational Arrangements, Section I.A, supra note 11.

14 See, e.g., SEC v. Kahlon,12-CV-517 (E.D. Tex., filed August 14, 2012); SEC v. Bronson, 12-cv-06421-KMK (S.D.N.Y., filed August 22, 2012). As of the date of this filing, neither case has been resolved.

15 See, e.g., SEC v. Reiss, 13-cv-01537, dkt no. 10 (S.D.N.Y. 2014) (issuing a final judgment against the defendant in an enforcement action, without the defendant admitting or denying the allegations).

DTC stated that the above describes, in part, the proposed procedures filed by DTC on December 5, 2013,[16] in response to the Commission's opinion and order in In re International Power Group, Ltd. ("IPWG") directing DTC to "adopt procedures that accord with the fairness requirements of Section 17A(b)(3)(H)."[17] DTC withdrew the proposed rule change on August 18, 2014.[18]

According to DTC, as a result of its experiences following the IPWG decision and in connection with the previous proposal, DTC has determined that its proposed procedures for imposing Deposit Chills and Global Locks are more appropriately directed to current trading halts or suspensions imposed by the Commission, the Financial Industry Regulatory Authority, Inc. ("FINRA"), or a court of competent jurisdiction, and therefore will be more effective in targeting suspected securities fraud that is ongoing at the time the Restriction is imposed. In particular, with respect to Deposit Chills imposed pursuant to DTC's previous procedures, DTC believed that wrongdoers have seemingly taken into account DTC's Restriction process, and have been avoiding it by shortening the timeframe in which they complete their scheme, dump their shares into the market, and move on to another issue.

Additionally, DTC stated that Global Locks were typically being imposed on the basis of a Commission enforcement action alleging securities law violations that had

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16 See Securities Exchange Act Release No. 71132 (December 18, 2013); 78 FR 77755 (December 24, 2013) (SR-DTC-2013-11).

17 See Securities Exchange Act Release No. 66611 (March 15, 2012), 2012 SEC LEXIS 844 at *32 (March 15, 2012) (Admin. Proc. File No. 3-13687).

18 See Securities Exchange Act Release No. 72860 (August 18, 2014), 79 FR 49825 (August 22, 2014) (SR-DTC-2013-11).

occurred in the past, and so could not affect the violative behavior (unless the alleged securities law violations were ongoing). According to DTC, by the time of an enforcement action, the wrongdoers have long since transferred the subject securities. In addition, although a Global Lock bars book-entry settlements within DTC, it does not affect the trading of the issue, which occurs outside of DTC.

B. Proposed Rule Change

i. Proposed Basis for the Imposition of Restrictions

Under Sections 1(a) and (b) of the proposed rule change, if either FINRA or the Commission halts or suspends trading of an Eligible Security, respectively, DTC would impose a Global Lock. Similarly, under Section 1(c) of the proposed rule change, DTC would impose a Global Lock if ordered to do so by a court of competent jurisdiction. DTC states that its facilities should not be available to settle transactions otherwise prohibited by the Commission, FINRA, or a court of competent jurisdiction. DTC also stated that the imposition of a Global Lock on an Eligible Security for which trading is halted or suspended would prevent settlement of trades that continue despite the halt or suspension, and prevent the liquidation of a halted or suspended position through DTC.

Notwithstanding Sections 1(a) and (b) of the proposed rule change, according to DTC, there may be certain limited circumstances where a Global Lock would not further the regulatory purpose of such trading halt or suspension. Therefore, DTC stated that if it reasonably determines that such is the case, DTC may decline to impose a Global Lock.

Finally, under Section 1(d) of the proposed rule change, DTC would impose a Restriction when it becomes aware of a need for immediate action to avert an imminent harm, injury, or other such material adverse consequence to DTC or its Participants that

could arise from further Deposits of, or continued book-entry services with respect to, an Eligible Security. DTC explained that, while it is impossible to anticipate all possible scenarios that could give rise to the need for action by DTC under Section 1(d) to avoid imminent harm, DTC does not anticipate that it would impose Restrictions pursuant to this formulation frequently. Examples given by DTC where this provision could be invoked include, but are not limited to, if DTC became aware that marketplace actors were about to deposit Securities at DTC in connection with an ongoing corporate hijacking, market manipulation, or in violation of other applicable laws; if an Issuer or its agent provides DTC with plausible information that Security certificates were stolen and were about to be deposited; or if an Issuer notifies DTC that shares of a Security had just been issued erroneously upon a conversion of previously satisfied notes.

ii. Proposed Basis for the Release of Restrictions

As part of DTC's process for imposing Restrictions premised on direct court or regulatory agency intervention or the prospect of imminent adverse consequences to DTC or its Participants, the proposed rule change provided corresponding criteria for releasing such Restrictions. In the case of a Global Lock imposed pursuant to Sections 1(a) and (b) of the proposed rule change (i.e., when either FINRA or the Commission issues a trading halt or suspension, respectively), DTC proposed that it would release the Global Lock when the halt or suspension of trading of the Eligible Security has been lifted. In the case of a Restriction imposed pursuant to Section 1(c) of the proposed rule change (i.e., an order from a court of competent jurisdiction), DTC proposed that it would release the Restriction when a court of competent jurisdiction orders DTC to release the Restriction. DTC explained that because trading would no longer be prohibited by FINRA, the

Commission, or a court order, there should not be any settlement restrictions, other than those otherwise provided in the Rules.

In the case of a Restriction imposed pursuant to Section 1(d) of the proposed rule change, DTC proposed that it would release the Restriction when DTC reasonably determines that the release of the Restriction would not pose a threat of imminent adverse consequences to DTC or its Participants, obviating the original basis for the Restriction. While DTC stated that it is impossible to anticipate all possible scenarios that could give rise to a release of a Restriction under this basis, DTC anticipated that it would release a Restriction imposed pursuant to Section 1(d) of the proposed rule change in a number of circumstances, including, without limitation, when DTC determined that the perceived harm has passed or is significantly remote, when the basis for the Restriction no longer exists, or when an Eligible Security had been previously Globally Locked based on a Commission enforcement action but there is no indication that illegally distributed Securities are about to be deposited.

Lastly, DTC proposed that it would release a Restriction when DTC reasonably determined that its imposition of the Restriction was based on a clerical mistake.

iii. Proposed Fair Procedures for Notice of and Opportunity to Challenge Restrictions

Pursuant to the proposed rule change, DTC would send written notice ("Restriction Notice") to the Issuer's last known business address and to the last known business address of the Issuer's transfer agent, if any, on record with DTC. The Restriction Notice would be sent within three Business Days of imposition of a Restriction and would set forth (i) the basis for the Restriction; (ii) the date the Restriction was imposed; (iii) that the Issuer may submit a written response to DTC

detailing the basis for release of the Restriction under the proposed rule change ("Restriction Response"); and (iv) that the Restriction Response must be received by DTC within 20 Business Days of delivery of the Restriction Notice. The proposed rule change also provided that, in response to the Restriction Response, DTC may reasonably request additional information or documentation from the Issuer.

Once the Restriction Response is received by DTC, the proposed rule change provided that it would be reviewed by a DTC officer who did not have responsibility for the imposition of the Restriction ("Review Officer"). After the Review Officer completes the review, DTC would provide a written decision ("Restriction Decision") to the Issuer. Within 10 Business Days of delivery of the Restriction Decision, the Issuer may submit a "Supplement" for the sole purpose of establishing that DTC made a clerical mistake or mistake arising from an oversight or omission in reviewing the Restriction Response. If the Issuer submits a Supplement, the Review Officer would provide a "Supplement Decision" within 10 Business Days after the Supplement was delivered.

The proposed rule change also provided that the Restriction Notice, the Restriction Response, the Restriction Decision, the Supplement, the Supplement Decision, and any other documents submitted in connection with the proposed procedures would constitute the record for purposes of any appeal to the Commission.

Finally, the proposed rule change clarified that such Rules would not affect DTC's ability to (i) lift or modify a Restriction; (ii) operationally restrict book-entry services, Deposits, or other services in the ordinary course of business, as such restrictions do not constitute Deposit Chills or Global Locks for purposes of the proposed rule change; (iii) communicate with the Issuer or its transfer agent or representative, if

any, provided that substantive communications are memorialized in writing to be included in the record for purposes of any appeal to the Commission; or (iv) send out a Restriction Notice prior to the imposition of a Restriction.

iv. Notice of Filing of Amendment No. 1

As originally proposed, Section 3 of the proposed rule change did not provide a specified period of time for the Review Officer to complete the review of the Restriction Response and for DTC to issue a Restriction Decision. DTC filed Amendment No. 1 to modify Section 3 of the proposed rule change to provide that DTC would issue a Restriction Decision within 10 Business Days after receiving a Restriction Response, which may be extended for a reasonable period of time (i) if DTC requests additional information or documents from the Issuer, or (ii) by consent of the Issuer or the transfer agent.

III. Summary of Comments Received

The Commission received eight comment letters in response to the proposed rule change.[19] One comment letter generally supported the proposed rule change.[20] Four comment letters by two commenters, STA and Kesner, objected to the proposed rule change.[21] Two comment letters from DTC responded to the objections raised by STA

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19 See supra, note 4.

20 See Arnoff Letter.

21 See STA Letters I and II, and Kesner Letters I and II.

and Kesner,[22] and one comment letter did not specifically comment on any aspect of the proposed rule change.[23]

A. Supporting Comment

But for the points that are addressed in footnote 29, below, Arnoff fully endorsed the proposed rule change, stating that the proposed fair notice and opportunity to challenge procedures would prevent and mitigate harm to both issuers and innocent shareholders.[24]

B. Objecting Comments

STA and Kesner expressed general concerns with DTC, as a monopoly in the clearance and settlement of securities, exercising discretion to deny access to its services.[25]

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22 See DTC Letters I and II.

23 See Deyet Letter.

24 See Arnoff Letter.

25 STA Letter I at 1; Kesner Letter I at 1. Commenters also raised other points about the proposed rule change, but they did not explain how those points render the proposed rule change inconsistent with the Act. For example, STA stated that (i) the proposed rule change was not a "good faith attempt" by DTC to comply with IPWG, and (ii) any record could not be "complete" for Commission review if the issuer does not have the ability to compel evidence from third parties that may be the cause of DTC's concern (STA Letter I at 3); while Kesner stated, for example, that (i) DTC's imposition of Restrictions, in many cases, are only based upon "flimsy legal footing, notice of commencement of an investigation or inquiry, anecdotal observations or even unproven news stories," (ii) the proposed rule change does not address the "unfortunate results that befall innocents caught up by a [Restriction], nor the immensity of the costs and burdens placed on issuers and investors seeking to clear a [Restriction]," and (iii) that the Commission has not "direct[ed] DTC to adopt[] rules to protect DTC or DTC's financial institution owners and DTC has not articulated how exercising discretionary authority satisfies its obligation for a process." Kesner Letter I at 2, 3; Kesner Letter II at 1. Because these points and other similar points made in the comment letters do not

Proposed Basis for Imposition of Restrictions Is Vague and Discretionary

STA stated that the proposed rule change suffers from vague, ambiguous standards and procedural problems.[26] Specifically, STA asserted that the authority to impose Restrictions under Section 1(d) of the proposed rule change is overly broad, arbitrary, permits DTC to exercise unfettered discretion, and would allow DTC to take action without any real evidence of the likelihood of actual harm or violation of objective standards.[27] STA also asserted that if DTC is concerned about imminent adverse

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raise a legal issue with respect to whether the proposed rule change is consistent with the Act, they are not further summarized in this notice and order.

In addition, commenters raised other points beyond the scope of the proposed rule change. For example, STA stated that the proposed rule change should also apply to transfer agents seeking initial access to DTC's facilities (STA Letter I at 4); while Kesner stated, for example, that (i) the Commission should not act on the proposed rule change without (a) specific comments from major exchanges and OTCLink regarding coordination with DTC, and (b) the Commission concluding that DTC's actions under the proposed rule change would not interfere with the objectives of exchanges and other regulators and not hamper the functioning of the markets, (ii) DTC would need to give up its immunity from lawsuits in order for there to be a potentially fair process in the imposition and appeal of Restrictions, (iii) investors should have standing to appeal a Restriction, and (iv) the Commission should require DTC to undertake a study and submit all of its statistics surrounding Restrictions. Kesner Letter I at 4, 6; Kesner Letter II at 3. Similar to Kesner, Arnoff asserted that the proposed rule change should clarify that DTC should not be immune from civil liability, particularly if DTC cannot establish that it acted in good faith and with reasonable judgment, because DTC is not acting in a governmental capacity in the settlement and clearance process. Arnoff Letter. Moreover, Arnoff stated that because DTC is not infallible and the risk of error always exists, DTC should be required to purchase "errors and omissions insurance" to protect innocent issuers and investors and to add an "additional dimension of loss prevention." Arnoff Letter. Because these points and other similar points made in the comment letters are not germane to the proposed rule change and/or are beyond the scope of the proposed rule change, they are not further summarized in this notice and order.

[26] STA Letter I at 2; see also STA Letter II at 2.

[27] STA Letter I at 1-3; see also STA Letter II at 2.

consequences to itself or its Participants, it should limit its Restriction, under Section 1(d) of the proposed rule change, to only a single ten-day period, with any "fair process" occurring during that ten-day Restriction.[28] Furthermore, STA states that, during the ten-day period, DTC could resolve concerns based on a "misunderstanding" or inform the Commission or FINRA of its concerns, allowing either organization to take further action to protect DTC, its Participants, or investors from the imminent harm.[29]

Kesner believed that the basis for imposing Restrictions under Sections 1(a), (b), and (c) of the proposed rule change is consistent with the approach of DTC being directed by a regulator or court.[30] However, similar to STA, Kesner expressed concern that Section 1(d) of the proposed rule change would give authority to DTC to impose Restrictions merely upon the initiation of an investigation or enforcement proceeding where it concludes a threat is imminent requiring immediate action.[31] According to Kesner, DTC cannot be "fair" and cannot satisfy the requirements set forth in IPWG if DTC sets its own standards and acts on its own accord to impose a Restriction not directed by a traditional regulator or court because DTC does not have the resources, technical expertise, or "commitment to fairness" to undertake such an expansive role in the substantive regulation of securities Issuers or to become a "super-gatekeeper."[32] Rather, the imposition of Restrictions would best be left to exchanges and other

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28 STA Letter I at 3.

29 Id. at 4.

30 Kesner Letter I at 6.

31 Id.

32 Id. at 2, 4-5; see also STA Letter II at 3.

"regulatory bodies" that have sufficient resources and could direct DTC to impose a service restriction when warranted.[33] Kesner further stated that DTC's imposition of Restrictions under Section 1(d) of the proposed rule change, if approved, should include specific methods by which an Issuer can successfully appeal and require DTC to remove the chill (or provide for automatic removal after a short period) that are fair and reasonable and that do not burden smaller Issuers with excessive costs or delays during the denial of the DTC's essential services.[34]

Proposed Procedures for Notice of and Opportunity to Challenge Restrictions Are Not Fair

STA contended that Section 3, as originally proposed, of the proposed rule change is procedurally deficient because there are no time periods specified in the proposed rule change for the DTC Review Officer's review to be completed. Thus, in some cases Issuers and investors could be harmed for an indefinite period while waiting for DTC to reach a decision.[35] Moreover, STA expressed concern that the Review Officer tasked with reviewing a Restriction Response may be located in an office near the person that imposed the Restriction, may have been involved in imposing the Restriction, and may be charged with overturning the decision made by a colleague.[36] Similarly, Kesner questioned the independence of the Review Officer and asserted that IWPG requires that appeals should be heard by parties independent of DTC and suggests that "representatives

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33 Kesner Letter I at 6.

34 Id.

35 Id.

36 Id.

of the securities bar, [STA], transfer agents, clearing and settlement firms, auditors, and business people, under the guidance of the DTC General Counsel, should constitute the panel of hearing officers making recommendations for imposition and removal of [Restrictions], continuations and appeals whenever DTC acts."[37]

STA also asserted that notice of a Restriction should occur prior to or, at least, contemporaneously with imposition of the Restriction, particularly in the case of a Restriction imposed based on DTC's assessment of imminent harm, under Section 1(d) of the proposed rule change, not three days after the Restriction is imposed.[38]

C. DTC's Response

Response to Comments by STA and Kesner that the Proposed Basis for Imposition of Restrictions Is Vague and Discretionary

In response to STA's comment that the basis for imposition of Restrictions under the proposed rule change is vague, DTC asserted that Sections 1(a)-(c) of the proposed rule change provided objective trigger events for imposing Restrictions and will be the primary focus of the Restriction program going forward.[39] DTC also stated that it does not anticipate imposing Restrictions pursuant to Section 1(d) frequently[40] and has provided examples of circumstances under which imminent harm could arise in the future as described above.[41] Further, DTC asserted that, STA's position that the Commission

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37 Kesner Letter II at 2.

38 STA Letter I at 4.

39 DTC Letter I at 2.

40 Id. at 2.

41 Id. at 3.

should not approve the proposed rule change if they include Section 1(d) would deny DTC the flexibility to impose Restrictions if necessary to avoid imminent harm to DTC or its Participants.[42] DTC stated that it needs the flexibility to protect itself from imminent harm that could arise from circumstances that would neither justify nor be impacted by a trading halt or suspension.[43]

In response to Kesner's comment that Section 1(d) of the proposed rule change would give authority to DTC to impose Restrictions merely upon the initiation of an investigation or enforcement proceeding where it concludes a threat is imminent requiring immediate action, DTC asserted that it is critical to the self-regulatory function of DTC to retain discretion to avert imminent harm, including the discretion to take action before providing notice to the Issuer, if necessary.[44] Similarly, in response to both STA's and Kesner's comments that Restrictions imposed under Section 1(d) of the proposed rule change should be automatically removed after a short period or expire after 10 days, DTC stated that it would not be effective, reasonable, or practical for it to premise its proposed rule change on the assumption that the Commission or FINRA would or could take action quickly enough to protect DTC, its Participants, or investors.[45] DTC explained further that imminent harm to DTC or its Participants could arise from circumstances that would not be addressed by or justify a trading halt or suspension, such

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42 Id. at 2.

43 Id. at 3.

44 DTC Letter II at 2.

45 DTC Letter I at 3; see also DTC Letter II at 2.

as the impending deposit of illegally distributed securities at DTC.[46] DTC also reiterated that it does not anticipate imposing Restrictions pursuant to Section 1(d) frequently.[47]

Response to Comments by STA and Kesner that the Proposed Procedures for Notice of and Opportunity to Challenge Restrictions Are Not Fair

In response to STA's specific claim that the proposal is procedurally deficient because it lacks a stated time period for the Review Officer to complete the review, DTC submitted Amendment No.1 to Section 3 of the proposed rule change, which, as described above, established a ten-business-day deadline, with limited extension, for the Review Officer to complete its review of the Restriction Response and DTC provide a Restriction Decision.[48]

In response to STA's and Kesner's comments on the independence of the Review Officer and STA's comment that notice of a Restriction should be at least contemporaneously with the imposition of the Restriction, DTC stated that it believes the proposed rule change is sufficiently clear to require that the Review Officer not be conflicted and that the Review Officer's decision would be unbiased and independent,[49] and that the Commission's decisions in both IPWG and In re Atlantis Internet Group

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46 Id.

47 Id.

48 Prior to filing Amendment No. 1, DTC also contended in its response letter that a reasonable review by the Review Officer in a timely manner is implicit in the proposed process, recognizing that DTC is bound to perform a prompt review, and to do otherwise may conflict with its obligations under Section 17A of the Act. DTC Letter I at 4; 15 U.S.C. 78q-1.

49 DTC Letter I at 4.

("Atlantis")[50] recognize that DTC must retain discretion to avert imminent harm, including the discretion to take action before providing notice to the issuer, if necessary.[51]

IV. Proceedings to Determine Whether to Approve or Disapprove SR-DTC-2016-003, as Modified by Amendment No. 1, and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act[52] to determine whether the proposed rule change, as modified by Amendment No. 1, should be approved or disapproved. Institution of proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change. As noted above, institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, the Commission seeks and encourages interested persons to comment on the proposed rule change, and provide arguments to support the Commission's analysis as to whether to approve or disapprove the proposed rule change.

Pursuant to Section 19(b)(2)(B) of the Act,[53] the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of the proposed rule change's consistency with the Act and the rules thereunder. Specifically, the Commission believes that DTC's proposed rule change raises questions as to whether it is consistent with: (i) Section

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50 Atlantis, Securities Exchange Act Release. No. 75168 at 7-8, 2015 SEC LEXIS 2394 (June 12, 2015) (Admin. Proc. File No. 3-15432).

51 DTC Letter I at 3.

52 15 U.S.C. 78s(b)(2)(B).

53 15 U.S.C. 78s(b)(2)(B).

17A(b)(3)(F) of the Act,[54] which requires, in part, that clearing agency rules be designed to assure the safeguarding of securities in the custody or control of the clearing agency and, in general, protect investors and the public interest; and (ii) Section 17A(b)(3)(H) of the Act,[55] which requires clearing agency rules to be in accordance with the provisions of Section 17A(b)(5)(B) of the Act, and, in general, provide a fair procedure with respect to the prohibition or limitation by the clearing agency of any person with respect to access to services offered by the clearing agency.[56] Section 17A(b)(5)(B) of the Act[57] requires that, in any proceeding by a registered clearing agency to determine whether a person shall be denied participation or prohibited or limited with respect to access to services offered by the clearing agency, the clearing agency shall notify such person of, and give him an opportunity to be heard upon, the specific grounds for denial or prohibition or limitation under consideration and keep a record.[58] A determination by the clearing agency to deny participation or prohibit or limit a person with respect to access to services offered by the clearing agency shall be supported by a statement setting forth the specific grounds on which the denial or prohibition or limitation is based.[59]

V. Request for Written Comments

The Commission requests that interested persons provide written submissions of

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54 15 U.S.C. 78q-1(b)(3)(F).

55 15 U.S.C. 78q-1(b)(3)(H).

56 15 U.S.C. 78q-1(b)(3)(H).

57 15 U.S.C. 78q-1(b)(5)(B).

58 Id.

59 Id.

their views, data, and arguments with respect to the changes to the proposed rule change as set forth in Amendment No. 1, as well as any others they may have identified with the proposed rule change, as amended. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change, as modified by Amendment No. 1, is consistent with Sections 17A(b)(3)(F) and 17A(b)(3)(H) of the Act, or any other provision of the Act, or the rules and regulations thereunder.

Interested persons are invited to submit written data, views, and arguments on or before [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal on or before [insert 35 days from the date of publication in the Federal Register]. 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-DTC-2016-003 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-DTC-2016-003. 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 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of DTC and on DTCC's website (http://dtcc.com/legal/sec-rule-filings.aspx). 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-DTC-2016-003 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[60]

Robert W. Errett
Deputy Secretary

[60] 17 CFR 200.30-3(a)(12).