

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-52446; File Nos. SR-DTC-2005-04, SR-FICC-2005-10, and SR-NSCC-2005-05)

September 15, 2005

Self-Regulatory Organizations; The Depository Trust Company, Fixed Income Clearing Corporation, and National Securities Clearing Corporation; Order Approving Proposed Rule Change to Establish a Fine for Members Failing to Conduct Connectivity Testing

I. Introduction

On May 13, 2005, May 3, 2005, and on May 4, 2005, respectively, The Depository Trust Company (“DTC”), the Fixed Income Clearing Corporation (“FICC”), and the National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule changes SR-DTC-2005-04, SR-FICC-2005-10, and SR-NSCC-2005-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”).<sup>1</sup> On June 7, 2005, NSCC amended its proposed rule change. Notice of the proposals, as amended, was published in the Federal Register on July 21, 2005.<sup>2</sup> No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule changes.

II. Description

DTC, FICC, and NSCC are imposing a fine on any member that is required to conduct connectivity testing for business continuity purposes and fails to do so.

In the aftermath of September 11, 2001, and in conjunction with a financial industry white paper, DTC, FICC, and NSCC require connectivity testing each year for critical (“Top Tier”) members.<sup>3</sup> The criteria used by DTC, FICC, and NSCC to identify their respective Top

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

<sup>2</sup> Securities Exchange Act Release No. 52043 (July 15, 2005), 70 FR 42122.

<sup>3</sup> The Federal Reserve, Office of the Comptroller of the Currency, and the Commission issued “Interagency Paper on Sound Practices to Strengthen the

Tier members were revenues, clearing fund contributions, settlement amounts, and trading volumes. Connectivity testing for the Top Tier members was initiated on January 1, 2004. Due to the critical importance of being able to assess whether a Top Tier member has sufficient operational capabilities, DTC, FICC, and NSCC have determined that they need the ability to fine any Top Tier member that does not test.<sup>4</sup>

Currently, each member of DTC, FICC, and NSCC that is designated as Top Tier is advised of this status and is provided with information on the testing requirements. Under DTC, FICC, and NSCC's current procedures, if testing is not completed by a Top Tier member by the

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Resilience of the U.S. Financial System.” [68 FR 17809 (April 11, 2003)]. This document provided guidelines that required core clearing and settlement organizations, such as DTC, FICC, and NSCC, and others in the financial industry to manage business continuity capabilities. DTC, FICC, and NSCC developed their testing of Top Tier firms based on the guidelines outlined in the white paper.

<sup>4</sup> Pursuant to DTC Rule 2, “Participants and Pledges,” participants must furnish, upon DTC’s request, information sufficient to demonstrate operational capability. In addition, DTC Rule 21, “Disciplinary Sanctions,” allows DTC to impose fines on participants for any error, delay or other conduct detrimental to the operations of DTC.

Pursuant to GSD Rule 3, “Responsibility, Operational Capability, and Other Membership Standards of Comparison-Only Members and Netting Members,” the GSD may require members to fulfill operational testing requirements as the GSD may at any time deem necessary. Pursuant to MBSD Rule 1, Section 3 of Article III, all MBSD applicants and members agree to fulfill operational testing requirements and related reporting requirements that may be imposed to ensure the continuing operational capability of the applicant.

Pursuant to NSCC Rule 15, “Financial Responsibility and Operational Capability,” members must furnish to NSCC adequate assurances of their financial responsibility and operational capability as NSCC may at any time deem necessary. In addition, NSCC Rule 48, “Disciplinary Procedures,” allows NSCC to impose a fine on participants for any error, delay, or other conduct that is determined to be detrimental to the operations of NSCC.

end of June, a reminder notice is sent to the member. Thereafter, another reminder notice is sent in October and, if necessary, again in December.

The reminder notice sent in December will advise that if testing is not completed by December 31, a fine of \$10,000 will be imposed. These fines will be collected from members in January of the following year. The Membership and Risk Management Committee will be notified of all members that were fined for failing to complete connectivity testing.

In the event that any member fails to complete connectivity testing for two successive years, the fine that will be imposed at that time will be \$20,000. Failure to complete testing for more than two successive years will result in disciplinary action, including potential termination of membership.

### III. Discussion

Section 17A(b)(3)(F) of the Act requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible.<sup>5</sup> The Commission finds that DTC, FICC, and NSCC's proposed rule changes are consistent with this requirement because the implementation of the fines should help DTC, FICC, and NSCC to enforce compliance with their connectivity testing rules for business continuity purposes and as a result should better enable them to ensure the safeguarding of securities and funds which are in their custody or control.

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<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

IV. Conclusion

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

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule changes (File Nos. SR-DTC-2005-04, SR-FICC-2005-10, and SR-NSCC-2005-05) be and hereby are approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>6</sup>

Jonathan G. Katz  
Secretary

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<sup>6</sup> 17 CFR 200.30-3(a)(12).

