

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-61618; File No. SR-NSCC-2010-01)

March 1, 2010

Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change to Eliminate Guarantee of Payment in Connection With the Envelope Settlement Service

I. Introduction

On January 4, 2010, the National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR-NSCC-2010-01 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”).¹ The proposed rule change was published for comment in the Federal Register on January 29, 2010.² No comment letters were received on the proposal. This order approves the proposal.

II. Description

NSCC’s the Envelope Settlement Service (“ESS”) allows an NSCC member to physically deliver through the facilities of NSCC a sealed envelope³ containing securities and such other items as NSCC may permit from time to time to a specified receiving member. NSCC then delivers the envelope to the receiving member. ESS is provided for primarily pursuant to Rule 9 and Addendum D with related provisions in Addendum D with related provisions in Addendum K and Procedure XV. The primary substantive changes of this proposed rule change are in Rule

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 61415 (January 25, 2010), 75 FR 4896.

³ Rule 9 provides that except as NSCC may determine to be appropriate or necessary, NSCC will not examine the contents of the envelopes or verify the amounts of money shown on the credit list, and it shall not be responsible with respect thereto except to deliver the envelopes accepted by it to the authorized representatives of the members to whom they are addressed.

9, Addendum D, and Addendum K with a conforming change to Procedure XV. Technical clean-up changes are also being made in each.

The delivering member must attach to each envelope, a credit list (in duplicate), which reflects the total money value, if any, of the envelope's contents. If after receipt of the envelope NSCC determines that the envelope is properly listed on the accompanying credit list, NSCC stamps the duplicate credit list and makes it immediately available to the delivering member's representative. An envelope listed on the credit list shall be deemed to have been accepted by NSCC when the duplicate credit list is stamped.

As a related feature of ESS, the payment shown on the credit list is processed as part of the members' daily end of day net money settlement obligations in reliance on the agreement between the delivering and receiving parties outside NSCC that the amount listed is the contract amount.

In order to protect the NSCC against the risk of member non-payment NSCC is amending Rule 9 and related provisions so that NSCC does not guarantee the payment obligation to the receiving member in an ESS delivery and so that the credits and debits of the payment amount of an envelope may be reversed. The payment reversal may be effected by NSCC even if the receiving member has taken possession of the envelope; however, if the receiving member has not yet taken possession of the envelope at the time of a payment reversal, NSCC will return the envelope to the delivering member. Any dispute between the delivering and receiving members must be resolved by them outside the facilities of the NSCC.

Changes to Rule 9 affirmatively provide that NSCC does not guarantee the payment obligation in ESS and that payment credits and debits may be reversed. Technical and conforming changes clarify the concepts of delivering and receiving members and that settlement

processing is subject not only to the rights of NSCC in Section 2 of Rule 12 but also to the new reversal provision in Section 4 of Rule 9.

To conform to amended Rule 9, Addendum D is similarly being amended to state that ESS is not guaranteed and that payment credits and debits may be reversed as provided in Rule 9. Language making it clear that settlement processing is subject to the rights of NSCC under new Section 4 of Rule 9 and Section 2 of Rule 12, was also carried over to Addendum D. Because Addendum D also covers other services for which no change is made by this filing, certain of the revisions to Addendum D clarify that the revisions are limited to ESS. Historical statements in Addendum D are being eliminated.

The change to Addendum K is to delete the provision whereby NSCC provided a guarantee for ESS and thereby deemed ESS to be a “System” within the meaning of Rule 4. Without the guarantee, ESS is not considered to be a “System.” Consistent with the change, Procedure XV is modified so that when the clearing fund component titled “For Other Transactions” (that is, for other than CNS transactions and balance order transactions) is computed, ESS will not be included.

In considering the elimination of the guarantee, NSCC surveyed selected members and learned that they did not consider it vital that NSCC be responsible for their ESS payment obligations and that they do not rely on the NSCC to guarantee such payments. However, these members expressed a strong desire for NSCC to maintain the centralized delivery service. NSCC designed the proposed rule changes to meet the expressed need of certain members while reducing risk to NSCC and its members generally. NSCC believes that it is shifting the burden of risk to those that should bear it and to outside NSCC’s facilities.

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act⁴ and the rules and regulations thereunder applicable to NSCC. In particular, the Commission believes that by amending its rules, NSCC's exposure to potential losses from member defaults, insolvencies, mistakes, and fraud will be reduced and the risk of such potential losses will be appropriately shifted to the contracting members in an ESS transaction outside NSCC. The proposal is therefore consistent with the requirements of Section 17A(b)(3)(F),⁵ which requires, among other things, that the rules of a clearing agency are designed to promote the prompt and accurate clearance and settlement of securities transactions.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act⁶ and the rules and regulations thereunder.

⁴ 15 U.S.C. 78q-1.

⁵ 15 U.S.C. 78q-1(b)(3)(F).

⁶ 15 U.S.C. 78q-1.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁷ that the proposed rule change (File No. SR-NSCC-2010-01) be, and hereby is, approved.⁸

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.⁹

Florence E. Harmon
Deputy Secretary

⁷ 15 U.S.C. 78s(b)(2).

⁸ In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁹ 17 CFR 200.30-3(a)(12).