

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-69699; File No. SR-NSCC-2013-805)

June 5, 2013

Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Advance Notice, as Modified by Amendment No. 1, to Require that All Locked-in Trade Data Submitted to It for Trade Recording be Submitted in Real-time

Pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010 (“Clearing Supervision Act”)<sup>1</sup> and Rule 19b-4(n)(1)(i)<sup>2</sup> thereunder, notice is hereby given that on April 30, 2013, the National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) an advance notice described in Items I, II and III below, which Items have been prepared primarily by NSCC. On May 14, 2013, NSCC filed Amendment No. 1 to the advance notice.<sup>3</sup> The Commission is publishing this notice to solicit comments on the advance notice from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Advance Notice

NSCC is proposing to modify its Rules to require that all locked-in trade data submitted to NSCC for trade recording be submitted in real-time, as defined below, and to prohibit pre-netting and other practices that prevent real-time trade submission.

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Advance Notice

In its filing with the Commission, NSCC included statements concerning the purpose of and basis for the advance notice and discussed any comments it received on the advance notice.

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<sup>1</sup> 12 U.S.C. 5465(e)(1).

<sup>2</sup> 17 CFR 240.19b-4(n)(i).

<sup>3</sup> In Amendment No. 1, NSCC modified Exhibit 5 to the original advance notice filing to correct a typographical error in the text of its Rules & Procedures (“Rules”) related to the advance notice.

The text of these statements may be examined at the places specified in Item IV below. NSCC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.<sup>4</sup>

(A) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Advance Notice

Proposal Overview

NSCC is proposing to modify its Rules to require that all locked-in trade data submitted to NSCC for trade recording be submitted in real-time,<sup>5</sup> and to prohibit pre-netting and other practices that prevent real time trade submission.

According to NSCC, the majority of all transactions processed at NSCC are submitted on a locked-in basis by self-regulatory organizations (“SROs”) (including national and regional exchanges and marketplaces), and Qualified Special Representatives (“QSRs”).<sup>6</sup> Currently NSCC data reveals that almost all exchanges<sup>7</sup> and some QSRs submit trades executed on their respective markets in real-time, representing approximately 91% of the locked-in trades submitted to NSCC today. The proposed rule change would require that all locked-in trades

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<sup>4</sup> The Commission has modified the text of the summaries prepared by NSCC.

<sup>5</sup> The term “real-time,” when used with respect to trade submission, will be defined in Procedure XIII (Definitions) of NSCC’s Rules as the submission of such data on a trade-by-trade basis promptly after trade execution, in any format and by any communication method acceptable to NSCC.

<sup>6</sup> QSRs are NSCC Members that either (i) operate an automated execution system where they are always the contra side of every trade, (ii) are the parent or affiliate of an entity operating such an automated system, where they are the contra side of every trade, or (iii) clear for a broker-dealer that operates such a system and the subscribers to the system acknowledge the clearing Member’s role in the clearance and settlement of these trades.

<sup>7</sup> One executing market with very low trade volume does not yet submit trades in real-time.

submitted for trade recording by SROs and QSRs be submitted to NSCC in real-time.<sup>8</sup>

NSCC is also proposing to prohibit practices that preclude real-time submission, such as “pre-netting.” NSCC states that typically, pre-netting is done on a bilateral basis between a QSR and its customer, both NSCC Members. According to NSCC, any pre-netting practices – whether in the form of “summarization” (i.e., technique in which the clearing broker nets all trades in a single CUSIP by the same correspondent broker into fewer submitted trades), “compression” (i.e., technique to combine submissions of data for multiple trades to the point where the identity of the party actually responsible for the trades is masked), netting, or any other practice that combines two or more trades prior to their submission to NSCC (collectively, “pre-netting”) – prevent the submission to NSCC of transactions on a trade-by-trade basis, and cause submitting firms to delay submission of their trades. According to NSCC, these practices disrupt NSCC’s ability to accurately monitor market and credit risks as they evolve during the trading day. Therefore, NSCC’s proposal will prohibit pre-netting activity on the part of entities submitting original trade data on a locked-in basis.<sup>9</sup> The rules of NSCC’s affiliate Fixed Income Clearing Corporation (“FICC”) currently prohibit such activity, and this proposed rule change

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<sup>8</sup> NSCC is not at this time modifying Procedure III (Trade Recording Service (Interface Clearing Procedures)) of its Rules, so files submitted to NSCC by The Options Clearing Corporation (“OCC”) relating to option exercises and assignments (Procedure III, Section D – Settlement of Option Exercises and Assignments) will not be required to be submitted in real-time. OCC’s process of assigning option assignments is and will continue to be an end-of-day process.

<sup>9</sup> Trades executed in the normal course of business between a Member that clears for other broker-dealers, and its correspondent, or between correspondents of the Member, which correspondent(s) is not itself a Member and settles such obligations through such clearing Member (i.e., “internalized trades”) are not required to be submitted to NSCC and shall not be considered to violate the “pre-netting” prohibition.

would align NSCC's trade submission rules with those of FICC.<sup>10</sup>

NSCC does not expect the proposed rule changes to impact trade volumes significantly. According to NSCC, the majority of trades are currently being submitted to NSCC in real-time on a trade-by-trade basis, and NSCC is operationally capable of managing trade volumes that are multiple times larger than the historical peak volumes. NSCC's trade capture application, Universal Trade Capture, provides contract information to Members in real-time. Receipt of trade data in real-time will enable NSCC to record, and report to Members, trade data as it is received by the marketplaces, thereby promoting intra-day reconciliation of transactions at the Member level.

In the wake of recent industry disruptions, industry participants have been focused on developing controls to address the risks that arise from technology issues. NSCC believes that technology issues that could potentially cause significant disruptions and losses have become more likely in the securities markets that have leveraged technology advances to move to higher frequency trading environment. A comment letter submitted to the Commission in advance of its Technology and Trading Roundtable, held in October 2012, and signed by a number of industry participants including SROs, broker-dealers, and buy-side firms, supported this proposed rule

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<sup>10</sup> See, e.g., GSD Rule 11 (Netting System), Section 3 ("All trade data required to be submitted to the Corporation under this Section must be submitted on a trade-by-trade basis with the original terms of the trades unaltered. A Member or any of its Affiliates may not engage in the Pre-Netting of Trades prior to their submission to the Corporation in contravention of this section. In addition, a Member or any of its Affiliates may not engage in any practice designed to contravene the prohibition against the Pre-Netting of Trades."), [http://dtcc.com/legal/rules\\_proc/FICC-Government\\_Security\\_Division\\_Rulebook.pdf](http://dtcc.com/legal/rules_proc/FICC-Government_Security_Division_Rulebook.pdf). See also Order Granting Approval of a Proposed Rule Change Relating to Trade Submission Requirements and Pre-Netting, Release No. 34-51908 (June 22, 2005), 70 FR 37450 (June 29, 2005).

change as a crucial component of the industry controls that could increase market transparency and ultimately mitigate risks associated with high-frequency trading and related technology.<sup>11</sup>

As a central counterparty, NSCC contributes to market stability by interposing itself between counterparties to financial transactions and thereby reducing the risk faced by market participants. NSCC believes the proposed rule change will align NSCC's Rules with the trend in risk mitigation to move towards real-time trade submission and processing. NSCC believes the proposal will also support NSCC's critical role in maintaining financial stability by reducing the operational risk that results from locked-in trade data not being submitted to NSCC in real-time, particularly from firms that delay trade submission so as to pre-net their data. For example, receipt of locked-in trade data on a real-time basis will permit NSCC's risk management processes to monitor trades closer to trade execution on an intra-day basis, and identify and manage any issues relating to excessive risk exposure earlier in the day. According to NSCC, it will also be able to provide safe storage for real-time trade data, mitigating the risk that an event that occurs after trade execution and disrupts trade input will significantly delay completion of those trades or may even cause trade data to be lost.

While the proposed rule change will require some QSRs to enhance their trade submission systems, and could cause increased fees for those NSCC Members that pre-net their trade data so as to reduce clearance fees, NSCC believes the significant risk mitigation benefits of this proposal outweigh any temporary burdens or increased costs that may result. As a user-owned industry utility and a registered clearing agency, NSCC believes it must appropriately allocate the costs of its services in order to maintain a fee schedule that is fair and equitable

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<sup>11</sup> Comment Letter dated Sept. 28, 2012 (<http://www.sec.gov/comments/4-652/4652-17.pdf>).

among its participants. According to NSCC, enabling Members to persist in pre-netting practices permits those participants to evade paying their fair share of NSCC's costs, rendering NSCC's fee schedule, as currently applied, inequitable to the firms for whom trades are submitted in real-time without any pre-netting. Further, over the past few years, NSCC has adjusted its fee schedule to give more weight to "value transacted" and less weight to "units processed," which NSCC believes will reduce the impact of this rule change on Members' fees.

#### Implementation Timeframe

If the Commission approves this proposed rule change, Members will be advised of the implementation date through issuance of an NSCC Important Notice. The proposed rule change will not be implemented earlier than seven (7) months from the date of Commission approval.

#### Proposed Rule Changes

NSCC proposes to amend Rule 7 (Comparison and Trade Recording Operation), Procedures II (Trade Comparison and Recording Service), IV (Special Representative Service) and XIII (Definitions) of its Rules in order to require that all locked-in trades submitted for trade recording by SROs and QSRs be submitted on a real-time basis, and to make clear that locked-in trade data from SROs and QSRs must be submitted on a trade-by-trade basis, in the original form in which they are executed, and that pre-netting and similar practices are prohibited.

In light of these proposed changes, Addendum N (Interpretation of the Board of Directors: Locked-In Data From Qualified Special Representatives) of NSCC's Rules will be deleted, as it will be no longer relevant.

#### (B) Clearing Agency's Statement on Comments on the Advance Notice Received from Members, Participants, or Others

While written comments relating to the proposed rule change have not yet been solicited with respect to this filing, the proposed rule changes described herein were the subject of a prior

rule filing that was filed with the Commission in 2006 as File No. SR-NSCC-2006-04 (“2006 Filing”).<sup>12</sup> NSCC received a number of public comments to the 2006 Filing. NSCC submitted a public response to each of the comments in 2006.<sup>13</sup> The 2006 Filing was officially withdrawn on December 29, 2011.

(C) Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

*Description of Change*

NSCC is proposing to amend its Rules in order to require that all locked-in trade data submitted to NSCC for trade recording be submitted promptly after trade execution (or in real-time), and to prohibit pre-netting and other practices that prevent real-time trade submission.

The proposed rule change is described in detail above.

*Anticipated Effect on and Management of Risk*

As described above, the proposed rule change is designed to reduce the operational, market, and credit risk to both NSCC and its Members that results from locked-in trade data not being submitted to NSCC in real-time. The risk-mitigating effects of this proposal are described in detail above.

III. Date of Effectiveness of the Advance Notice and Timing for Commission Action

The clearing agency may implement the proposed change pursuant to Section 806(e)(1)(G) of the Clearing Supervision Act<sup>14</sup> if it has not received an objection to the

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<sup>12</sup> Release No. 34-53742 (Apr. 28, 2006), 71 FR 26804 (May 8, 2006).

<sup>13</sup> Response Letter from NSCC dated Aug. 18, 2006 (<http://www.sec.gov/comments/sr-nsc-2006-04/nsc200604-9.pdf>).

<sup>14</sup> 12 U.S.C. 5465(e)(1)(G).

proposed change within 60 days of the later of (i) the date that the Commission received the advance notice or (ii) the date the Commission receives any further information it requested for consideration of the notice. The clearing agency shall not implement the proposed change if the Commission has any objection to the proposed change.

The Commission may extend the period for review by an additional 60 days if the proposed change raises novel or complex issues, subject to the Commission providing the clearing agency with prompt written notice of the extension. A proposed change may be implemented in less than 60 days from the date of receipt of the advance notice, or the date the Commission receives any further information it requested, if the Commission notifies the clearing agency in writing that it does not object to the proposed change and authorizes the clearing agency to implement the proposed change on an earlier date, subject to any conditions imposed by the Commission. The clearing agency shall post notice on its website of proposed changes that are implemented.

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.<sup>15</sup>

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<sup>15</sup> NSCC also filed the proposals contained in this advance notice as a proposed rule change under Section 19(b)(1) of the Exchange Act and Rule 19b-4 thereunder. 15 U.S.C. 78s(b)(1); 17 CFR 240.19b-4. Pursuant to Section 19(b)(2) of the Exchange Act, generally not later than 45 days after the date of publication of the proposed rule change in the Federal Register or such longer period up to 90 days if the Commission determines that a longer period is appropriate and publishes the reasons for such determination or the self-regulatory organization consents the Commission will either: (i) by order approve or disapprove the proposed rule change or (ii) institute proceedings to determine whether the proposed rule change should be disapproved. 17 U.S.C. 78s(b)(2)(A). See Release No. 34-69571 (May 14, 2013), 78 FR 29408 (May 20, 2013).



#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the advance notice is consistent with the Clearing Supervision

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](mailto:rule-comments@sec.gov). Please include File No. SR-NSCC-2013-805 on the subject line.

##### Paper Comments:

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

All submissions should refer to File No. SR-NSCC-2013-805. 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 advance notice that are filed with the Commission, and all written communications relating to the advance notice 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 such filings also will be available for inspection and copying at the principal office of NSCC and on NSCC's website at

[http://www.dtcc.com/downloads/legal/rule\\_filings/2013/nsc/SR-NSCC-2013-805.pdf](http://www.dtcc.com/downloads/legal/rule_filings/2013/nsc/SR-NSCC-2013-805.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 submissions should refer to File No. SR-NSCC-2013-805 and should be submitted on or before [insert date 15 days from publication in the Federal Register].

By the Commission.

Kevin M. O'Neill  
Deputy Secretary