SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-97129; File No. SR-NSCC-2022-009)

March 13, 2023

Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change to Adopt Intraday Volatility Charge and Eliminate Intraday Backtesting Charge

I. INTRODUCTION

On July 7, 2022, National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-NSCC-2022-009 (the "Proposed Rule Change") 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 for comment in the Federal Register on July 20, 2022,[3] and the Commission has received comments on the Proposed Rule Change.[4]

On September 1, 2022, pursuant to Section 19(b)(2) of the Act,[5] the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the Proposed Rule Change.[6] On October

---

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

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 95286 (July 14, 2022), 87 FR 43355 (July 20, 2022) (File No. SR-NSCC-2022-009) ("Notice of Filing").

4 Comments are available at https://www.sec.gov/comments/sr-nscc-2022-009/srnscc2022009.htm.

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

6 Securities Exchange Act Release No. 95650 (Sept. 1, 2022), 87 FR 55054 (Sept. 8, 2022) (File No. SR-NSCC-2022-009).

14, 2022, the Commission instituted proceedings, pursuant to Section 19(b)(2)(B) of the Act,[7] to determine whether to approve or disapprove the Proposed Rule Change.[8] On January 10, 2023, the Commission designated a longer period for Commission action on the proceedings to determine whether to approve or disapprove the Proposed Rule Change.[9]

For the reasons discussed below, the Commission is approving the Proposed Rule Change.[10]

II. DESCRIPTION OF THE PROPOSED RULE CHANGE

NSCC provides clearing, settlement, risk management, central counterparty services, and a guarantee of completion for virtually all broker-to-broker trades involving equity securities, corporate and municipal debt securities, and unit investment trust transactions in the U.S. markets. A key tool that NSCC uses to manage its credit exposure to its members is collecting an appropriate Required Fund Deposit (i.e., margin) from each member.[11] A member's margin is designed to mitigate potential losses to NSCC associated with liquidation of the member's portfolio in the event of that

---

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

8 Securities Exchange Act Release No. 96088 (Oct. 14, 2022), 87 FR 63845 (Oct. 20, 2022) (File No. SR-NSCC-2022-009).

9 Securities Exchange Act Release No. 96621 (Jan. 10, 2023), 88 FR 2688 (Jan. 17, 2023) (File No. SR-NSCC-2022-009).

10 Capitalized terms not defined herein are defined in NSCC's Rules & Procedures ("Rules"), available at https://www.dtcc.com/~/media/Files/Downloads/legal/rules/nscc_rules.pdf.

11 See Rule 4 and Procedure XV of the Rules, supra note 10.

member's default.[12] The aggregate of all NSCC members' margin deposits (together with certain other deposits required under the Rules) constitutes NSCC's clearing fund, which NSCC would access should a member default and that member's margin, upon liquidation, be insufficient to satisfy NSCC's losses.[13]

A member's margin consists of a number of applicable components, each of which addresses specific risks faced by NSCC.[14] Each member's start of day required margin is calculated overnight, based on the member's prior end-of-day net unsettled positions, and notified to members early the following morning to be deposited by approximately 10:00 a.m.[15] In this Proposed Rule Change, NSCC would make two changes to its margin methodology.

First, NSCC would add an intraday volatility charge to its margin requirement, which would increase the margin it collects from members whose trading portfolios experience large and unexpected intraday volatility. NSCC performed an impact study with respect to this change that reviewed member positions at 4:00 p.m. between January 3, 2020 and May 28, 2021. The study showed that the proposal would have resulted in approximately eight intraday volatility charges collected on an average day during that

---

12 Under NSCC's Rules, a default would generally be referred to as a "cease to act" and could encompass a number of circumstances, such as a member's failure to make a margin deposit in a timely fashion. See Rule 46, supra note 10.

13 See id.

14 See Procedure XV of the Rules, supra note 10.

15 See Procedure XV, Sections II(B) of the Rules, supra note 10. The Rules provide that required deposits to the clearing fund are due within one hour of demand, unless otherwise determined by NSCC.

time period, at an average of $31.6 million, ranging in size from $251,000 to $1.35 billion.[16]

Second, NSCC would amend its margin requirement to eliminate the intraday backtesting charge because the charge relies upon an assumption that may lead to undercounting potential backtesting deficiencies.[17] NSCC will retain the backtesting charge it collects as margin at the start of each business day.[18] The proposed changes to its margin requirements are the result of NSCC's regular review of its margin methodology to evaluate whether margin levels are commensurate with the particular risk attributes of each relevant product, portfolio, and market.[19] NSCC performed an impact analysis looking at both the proposal's impact on end of day backtesting and intraday backtesting between February 2021 and February 2022, during which time period NSCC collected a daily average of $30 million from 15 members in intraday backtesting charges. Although NSCC would not have collected these amounts under the proposal, the study showed that the end of day backtesting would have remained above the 99% coverage target during that time period, and this aspect of the proposal would have had an immaterial impact on intraday backtesting results, causing backtesting to drop below the 99% coverage target slightly in only two instances.[20]

---

16 See Notice of Filing, supra note 3, at 43360-61.

17 See id. at 43357.

18 See Procedure XV, Section I.B(3) of the Rules, supra note 10.

19 See Notice of Filing, supra note 3, at 43357.

20 See id. at 43361.

A. Background Regarding Specific Aspects of NSCC's Margin Methodology

Volatility Component: Generally, the largest portion of an NSCC member's margin is the volatility component. The volatility component is designed to reflect the amount of money that could be lost on a portfolio over a given period within a 99th percentile level of confidence. This component represents the amount assumed necessary for NSCC to absorb losses while liquidating the member's portfolio.

NSCC's methodology for calculating the volatility component of a member's required margin depends on the type of security and whether the security has sufficient pricing or trading history for NSCC to robustly estimate the volatility component using statistical techniques. Generally, for most securities (that is, equity securities), NSCC calculates the volatility component using, among other things, a parametric Value at Risk ("VaR") model, which results in a "VaR Charge."[21] In addition, for securities that do not have sufficient pricing or trading history to perform the statistical analysis employed in the VaR model, NSCC applies a haircut to calculate the volatility component, in lieu of the VaR-based calculation.[22] The volatility component of a member's required margin is the sum of the VaR-based and the haircut-based calculations.

---

21 Specifically, NSCC calculates the VaR Charge as the greatest of (1) the larger of two separate calculations that utilize the VaR model, (2) a gap risk measure calculation based on the largest non-index position in a portfolio that exceeds a concentration threshold, which addresses concentration risk that can be present in a member's portfolio, or (3) a portfolio margin floor calculation based on the market values of the long and short positions in the portfolio, which addresses risks that might not be adequately addressed with the other volatility component calculations. See Procedure XV, Sections I(A)(1)(a)(i) and I(A)(2)(a)(i) of the Rules, supra note 10.

22 Securities that are subject to the haircut-based calculation include unit investment trusts, corporate and municipal bonds and Illiquid Securities. See Rule 1 and Procedure XV, Sections I(A)(1)(a)(iii) and (2)(a)(iii) of the Rules, supra note 10.

Margin requirement differential ("MRD") charge: NSCC may assess an MRD charge, which is designed to capture the unpredictability of a member's historical trading activity, as measured, in part, by the variability in a member's volatility charge over a 100-day lookback period.[23]

Backtesting charge: NSCC employs daily backtesting to determine the sufficiency of each member's margin, by simulating the liquidation gains or losses using the actual unsettled positions in the member's portfolio, and the actual historical returns for each security held in the portfolio.[24] A backtesting deficiency would result if the liquidation losses were greater than the member's margin. NSCC investigates the causes of any backtesting deficiencies, paying particular attention to members with backtesting deficiencies that bring the results for that member below the 99 percent confidence target (i.e., greater than two backtesting deficiency days in a rolling twelve-month period) to determine if there is an identifiable cause of repeat backtesting deficiencies.[25] NSCC also evaluates whether multiple members may experience backtesting deficiencies for the same underlying reason.[26]

---

[23] Specifically, MRD is calculated as the sum of an exponentially weighted moving average ("EWMA") of positive day over day changes over a 100-day look back period in member's (1) mark-to-market charge and (2) volatility charge, times a multiplier calibrated based on backtesting results. See Procedure XV, Sections I(A)(1)(e) and (2)(d) of the Rules, supra note 10.

[24] Backtesting is an ex-post comparison of actual outcomes with expected outcomes derived from the use of margin models. See 17 CFR 240.17Ad-22(a)(1).

[25] See Notice of Filing, supra note 3, at 43356.

[26] See id.

Based on that daily testing, NSCC may assess a backtesting charge, which is designed to collect additional margin generally from any member whose 12-month trailing backtesting coverage falls below or risks falling below the 99 percent confidence level.[27] Currently, this charge may be assessed on an intraday or regular basis.[28] If assessed, a member's start-of-day backtesting charge is generally equal to that member's third largest deficiency,[29] and a member's intraday backtesting charge is generally equal to that member's fifth largest deficiency, that occurred during the previous 12 months.[30] NSCC calculates the backtesting charge monthly and, based on those calculations, may either continue to impose an existing backtesting charge, impose a new or remove an existing backtesting charge, or it may either increase or decrease a member's existing backtesting charge as necessary to maintain its target backtesting coverage.[31]

B. Proposed Intraday Volatility Charge

NSCC proposes to implement an intraday volatility charge that would be part of its members' margin requirement to better address the volatility risks presented by members' intraday net unsettled positions between the collections of margin at the start of each business day.[32] NSCC states that through its regular monitoring, it has

---

27 See Procedure XV, Section I(B)(3) of the Rules, supra note 10. See also Securities Exchange Act Release No. 79167 (Oct. 26, 2016), 81 FR 75883 (Nov. 1, 2016) (File Nos. SR-FICC-2016-006; SR-NSCC-2016-004).

28 See Procedure XV, Section I(B)(3) of the Rules, supra note 10.

29 See id.

30 See id.

31 See id.

32 NSCC states that it did not believe that an intraday volatility charge was necessary in 2017, when it accelerated the time of its trade guarantee (from

occasionally observed significant intraday changes to market price volatility and significant changes to the size and composition of members' portfolios of net unsettled positions that could cause the amount collected as the volatility charge at the start of that business day ("start of day volatility charge") to no longer be sufficient to mitigate the volatility risks that such positions present to NSCC.[33] The proposed intraday volatility charge would be designed to address this risk.

Application of the intraday volatility charge: An intraday volatility charge generally would apply when the difference between a member's start of day volatility charge and a calculation of the volatility charge based on that member's intraday net unsettled positions exceeds 100 percent, and when the amount of the charge is greater than $250,000.

NSCC states that, on days when there is increased volatility in the market, it would provide notice to its members that an intraday volatility charge may be collected. If NSCC determines to collect an intraday volatility charge, NSCC would issue a notice by electronic mail to those members who are subject to that charge, who would be able to view the amount to be collected in NSCC's clearing fund management system.[34] This notification and collection process would be identical to the current process that is

---

midnight of one day after trade date to either the point of trade comparison and validation, for bilateral submissions, or the point of trade validation, for locked-in submissions), because it did not believe that such a charge was necessary to address the risks presented by the accelerated trade guarantee. See Notice of Filing, supra note 3, at 43357. See also Securities Exchange Act Release No. 79598 (Dec. 19, 2016), 81 FR 94462 (Dec. 23, 2016) (File No. SR-NSCC-2016-005); Addendum K of the Rules, supra note 10.

[33] See Notice of Filing, supra note 3, at 43357.

[34] See id. at 43359.

followed for the notification and collection of the intraday mark-to-market charges.[35] Members who receive that notice would be required to fund the amount of the intraday volatility charge within one hour of that notice, pursuant to Section II(B) of Procedure XV of the Rules.[36]

Calculation of the intraday volatility charge: The amount of intraday volatility charge would be equal to the difference between the start of day volatility charge and the intraday calculation of that volatility charge, reduced by the volatility portion of the MRD charge collected from that member at the start of the business day.[37] NSCC states that, although the MRD charge is intended to capture the same type of risk (i.e., variability in the volatility charge), it believes the proposed intraday volatility charge would provide it with a better measure of the significant intraday volatility swings in a member's positions, which may be inconsistent with a member's historical trading activity.[38] NSCC states, therefore, it would not be necessary for NSCC to collect as part of the intraday volatility charge any amounts that it has already collected as the volatility portion of the MRD charge for that business day.[39]

---

35 See id.

36 See Procedure XV, Section II(B) of the Rules, supra note 10.

37 To avoid doublecounting the risks captured by any intraday mark-to-market charges NSCC may assess (see Procedure XV, Section I(B)(5) of the Rules, supra note 10), NSCC would use the same end of day price returns as used in the start of day volatility charge.

38 See Notice of Filing, supra note 3, at 43358.

39 See id.

When calculating the intraday volatility charge, NSCC proposes to adjust the net unsettled positions by excluding any position for which shares have either been delivered to the CNS System which is used by NSCC to account for and settle transactions or received by the member from the CNS System to satisfy all or any portion of that position. NSCC states it believes that, for purposes of this calculation, it would be appropriate to assume the positions for which the shares have been delivered and received would settle at the end of the day, so that the calculation would be more effectively driven by any significant intraday changes to the volatility risks presented by members' adjusted intraday net unsettled positions.[40]

Thresholds in Applying the Charge: As described above, NSCC proposes to only assess an intraday volatility charge if two thresholds are met (1) when the difference between the two calculations of the volatility charge exceeds 100 percent, and (2) the amount that would be calculated as an intraday volatility charge is greater than $250,000. NSCC states it believes the 100 percent threshold is appropriate because, in normal market conditions, intraday changes in volatility that are lower than this threshold are more likely due to normal market fluctuations, and NSCC believes that, based on past observations, only an increase that is larger than 100 percent of the start of day volatility charge and that is greater than $250,000 would require mitigation through the intraday volatility charge.[41]

---

40 See id.

41 NSCC states it believes amounts below this threshold, which is the minimum required deposit to the clearing fund, would be immaterial to address any increased risk. See id.

NSCC proposes to retain the discretion within its Rules to lower this threshold if it determines that a reduction would be appropriate to mitigate risks to NSCC, for example, during volatile market conditions or market events that cause increases in trading volume, or when NSCC believes a lower threshold is appropriate to mitigate risks presented by members whose portfolios may present relatively greater risks to NSCC on an overnight basis.[42] In circumstances when NSCC determines it is appropriate to reduce the threshold, the reduced threshold would apply to all members. NSCC states that this discretion would allow NSCC to collect an intraday volatility charge earlier in light of increased levels of volatility risks, and in these circumstances, a lower threshold would allow NSCC to more proactively preserve the coverage of its required fund deposit.[43]

Exceptions to Collecting an Intraday Volatility Charge: NSCC proposes two exceptions to collecting an intraday volatility charge from a particular member or members, which are instances where (a) trades submitted later in the day would offset trades submitted earlier in the day, such that the thresholds would not have been met if such activity had been submitted earlier in the day, or (b) the threshold was met due to the submission of an erroneous trade that can be corrected.

---

42 See id.

43 See id. As part of the Proposed Rule Change, NSCC filed Exhibit 3c – NSCC Market Risk Management Procedures (marked excerpt), which includes NSCC's internal criteria that would be applied to determine whether to adjust the threshold. Pursuant to 17 CFR 240.24b-2, NSCC requested confidential treatment of Exhibit 3c. Based on its review of those materials, the Commission understands that NSCC would provide notice to its members of any changes to the threshold.

NSCC monitors volatility in 15-minute increments throughout the business day.[44] When the threshold is exceeded during normal market conditions earlier in the trading day, NSCC states it would typically not collect an intraday volatility charge until later in the day when members have had an opportunity to submit trading activity that would be expected to offset trades submitted earlier in the day that caused the thresholds to be met,[45] or a system issue or other error could cause a delay in the submission of activity.[46] NSCC states that it believes an intraday volatility charge would not be necessary in these circumstances because the risk presented by the temporary increase in volatility would be expected to be mitigated by other clearing activity or corrected submissions later in the day.[47]

In determining whether to collect an intraday volatility charge, after the occurrence of a threshold trigger, NSCC would utilize the same escalation procedures that are currently in place when making similar determinations with respect to its current authority to impose intraday mark-to-market charges. Specifically, NSCC would utilize a predetermined escalation matrix that identifies the level of the required approver within the NSCC Market Risk group based on the amount of the calculated intraday volatility charge that would be collected.[48] A decision to collect the charge would be made based

---

44 See Notice of Filing, supra note 3, at 43357.

45 NSCC further states that off-setting trading activity may be submitted to NSCC later in the day in connection with a member's business model or trading practices. See id. at 43359.

46 See id.

47 See id.

48 As part of the Proposed Rule Change, NSCC filed Exhibit 3c – NSCC Market Risk Management Procedures (marked excerpt), which includes NSCC's internal

on documentation provided to the required approver regarding the circumstances of the calculated charge.[49]

Application to Positions in Securities Financing Transactions: NSCC has established a clearing service for securities financing transactions to make central clearing available at NSCC for equity securities financing transactions ("SFTs").[50] NSCC proposes to include the intraday volatility charge among the margin charges that are applicable to SFT positions cleared through NSCC.

C. Proposed Elimination of the Intraday Backtesting Charge

NSCC is also proposing to eliminate the intraday backtesting charge. NSCC states that, in connection with recent regulatory feedback, it has determined that the current methodology for calculating the intraday backtesting charge relies upon an assumption that NSCC would cease to act for a member that has paid all of its intraday margin requirements, when it is possible that would not be the case.[51] That is, NSCC could cease to act for a member that has not paid all of its intraday margin requirements, meaning that the member would have provided less margin to NSCC and may therefore present additional losses. As a result, this methodology may underestimate a member's backtesting losses and undercount potential backtesting deficiencies, whereas a

---

escalation procedures that will be applicable to a determination to waive a member's intraday volatility charge or to alter the applicable threshold. Pursuant to 17 CFR 240.24b-2, NSCC requested confidential treatment of Exhibit 3c.

49 See Notice of Filing, supra note 3, at 43359.

50 See Rule 56, supra note 10.

51 See Notice of Filing, supra note 3, at 43360.

calculation that disregards intraday margin collections would penalize members for making intraday margin deposits and be considered double margining.[52]

More specifically, if NSCC collects margin from a member intraday, but does not include that amount as part of the member's margin when backtesting, resulting in a backtesting deficiency and a subsequent intraday backtesting charge, that member would have covered its risk to NSCC twice – first as intraday margin collected from that member and second as an intraday backtesting charge.[53] Therefore, given these deficiencies and in light of the proposed intraday volatility charge, NSCC proposes to eliminate the intraday backtesting charge.

III. DISCUSSION AND COMMISSION FINDINGS

Section 19(b)(2)(C) of the Act[54] directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and rules and regulations thereunder applicable to such organization. After carefully considering the Proposed Rule Change, the Commission finds that the Proposed Rule Change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to NSCC. In particular, the Commission finds that the Proposed Rule Change is consistent with Section

---

52 See id.

53 See id.

54 15 U.S.C. 78s(b)(2)(C).

17A(b)(3)(F)[55] of the Act and Rules 17Ad-22(e)(4)(i), (e)(6)(i), and (e)(23)(ii) thereunder.[56]

A. Consistency with Section 17A(b)(3)(F) of the Act

Section 17A(b)(3)(F) of the Act[57] requires that the rules of a clearing agency, such as NSCC, be designed to, among other things, promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible.[58] The Commission believes that the proposal is consistent with Section 17A(b)(3)(F) of the Act for the reasons stated below.

As described above in Section II.B, NSCC proposes to add an intraday volatility charge to its margin requirements that NSCC may collect when certain thresholds are met. As discussed in more detail in Section III.C infra, the Commission believes that this proposed change to NSCC's margin methodology would help NSCC ensure that it collects sufficient margin to cover its credit exposure to its members in times of intraday market volatility.

Moreover, as described above in Section II.C, NSCC proposes to eliminate the intraday backtesting charge because it is based on an unreasonable assumption and is not necessary, in light of the proposed intraday volatility charge, for NSCC to address its intraday market risk exposures and backtesting coverage metrics. NSCC provided

---

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

56 17 CFR 240.17Ad-22(e)(4)(i), (e)(6)(i), and (e)(23)(ii).

57 15 U.S.C. 78q-1(b)(3)(F).

58 Id.

information regarding the impact of the proposed intraday backtesting charge elimination on its backtesting coverage.[59] The results of the analysis showed that, despite not collecting intraday backtesting charges, NSCC's end of day backtesting would have remained above the 99 percent coverage target during that time period, and that this aspect of the proposal would have had an immaterial impact on intraday backtesting results, causing backtesting to drop below the 99 percent coverage target slightly in only two instances.[60] The Commission has reviewed NSCC's analysis and agrees that its results indicate that NSCC's proposal to eliminate the intraday backtesting charge would not materially impact NSCC's margin coverage, and because the proposed intraday volatility charge would, when applicable, allow NSCC to collect additional amounts which would more accurately reflect the intraday changes to market volatility or the size of a member's portfolio.

With respect to both aspects of this proposal, the Commission believes that, by allowing NSCC to collect sufficient margin, the proposal should help ensure that, in the event of a member default, NSCC's operation of its critical clearance and settlement services would not be disrupted because of insufficient financial resources. Accordingly, the Commission finds that NSCC's proposal should help NSCC to continue providing prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.

59 As part of the Proposed Rule Change, NSCC filed Exhibit 3b – NSCC Intraday Backtesting Charge Impact Study Data, comparing the current and proposed margin collections. Pursuant to 17 CFR 240.24b-2, NSCC requested confidential treatment of Exhibit 3b. The confidential information provided more granular support for this analysis.

60 See id.

Moreover, as described in Section II above, NSCC would access the mutualized clearing fund should a defaulted member's own margin be insufficient to satisfy losses to NSCC caused by the liquidation of that member's portfolio. Because NSCC's proposal to adopt an intraday volatility charge should help ensure that NSCC has collected sufficient margin from members, the proposed changes would also help minimize the likelihood that NSCC would have to access the clearing fund, thereby limiting non-defaulting members' exposure to mutualized losses. The Commission believes that by helping to limit the exposure of NSCC's non-defaulting members to mutualized losses, the proposed changes should help NSCC assure the safeguarding of securities and funds which are in its custody or control, consistent with Section 17A(b)(3)(F) of the Act.[61]

B. Consistency with Rule 17Ad-22(e)(4)(i) under the Act

Rule 17Ad-22(e)(4)(i) under the Act requires that each covered clearing agency, such as NSCC, establish, implement, maintain and enforce written policies and procedures reasonably designed to effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by maintaining sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence.[62] The Commission believes that the proposal is consistent with Rule 17Ad-22(e)(4)(i) under the Act for the reasons stated below.[63]

---

61 15 U.S.C. 78q-1(b)(3)(F).

62 17 CFR 240.17Ad-22(e)(4)(i).

63 Id.

The proposed change to adopt an intraday volatility charge would allow NSCC to better manage its credit exposures to members by maintaining sufficient resources to cover those credit exposures fully with a high degree of confidence. Specifically, and as discussed further in Section III.C infra, the proposed intraday volatility charge would allow NSCC to collect additional margin on an intraday basis to help NSCC effectively mitigate the risks related to intraday increases in volatility and would address the increased risks NSCC may face related to liquidating a member's portfolio following that member's default.

Moreover, the proposed change to eliminate the intraday backtesting charge set forth in Section II.C would eliminate a charge that is currently calculated based on an unreasonable assumption and is not necessary for NSCC to address its intraday market risk exposures and backtesting coverage metrics. As discussed above,[64] the Commission has reviewed and analyzed the results of NSCC's backtesting analysis and believes that this proposal would allow NSCC to continue to collect margin to meet its coverage requirements.

Therefore, for the reasons discussed above, the Commission finds that the Proposed Rule Change is reasonably designed to enable NSCC to effectively identify, measure, monitor, and manage its credit exposure to members, and those arising from its payment, clearing, and settlement processes, including by maintaining sufficient financial resources to cover its credit exposure to each member fully with a high degree of confidence consistent with Rule 17Ad-22(e)(4)(i).[65]

---

64 See notes 59-60 supra and accompanying text.

65 17 CFR 240.17Ad-22(e)(4)(i).

C. Consistency with Rule 17Ad-22(e)(6)(i) under the Act

Rule 17Ad-22(e)(6)(i) under the Act requires that each covered clearing agency that provides central counterparty services, like NSCC, establish, implement, maintain and enforce written policies and procedures reasonably designed to cover its credit exposures to its participants by establishing a risk-based margin system that, at a minimum, considers, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market.[66]

As described above in Section II, each member's margin consists of a number of applicable components, each of which is calculated to address specific risks faced by NSCC. The Commission agrees that the proposal to adopt an intraday volatility charge set forth in Section II.B should enable NSCC to more effectively address the risks presented by significant intraday changes to market volatility or a member's portfolio of net unsettled positions. NSCC provided information regarding the impact of the proposed intraday volatility charge on its margin collection.[67] Specifically, a recent impact study shows that the proposal would have resulted in approximately eight intraday volatility charges collected on an average day during that time period, and such charges would have been an average of $31.6 million, ranging in size from $251,000 to $1.35 billion.[68] The Commission has reviewed NSCC's analysis and agrees that its results

---

66 17 CFR 240.17Ad-22(e)(6)(i).

67 As part of the Proposed Rule Change, NSCC filed Exhibit 3a – NSCC Intraday Volatility Charge Impact Study Data, comparing the current and proposed margin collections. Pursuant to 17 CFR 240.24b-2, NSCC requested confidential treatment of Exhibit 3a. The confidential information provided more granular support for this analysis.

68 See id. and Notice of Filing, supra note 3, at 43361.

indicate that NSCC's proposal results in margin levels commensurate with the credit exposures to better reflect the intraday changes to market volatility or the size of a member's portfolio.

One commenter raised concerns with respect to the analysis cited by NSCC in the Proposed Rule Change, stating that NSCC did not provide any data to support its assertion that it occasionally observed significant intraday changes to market price volatility.[69] Consistent with NSCC's statement regarding observing volatility, the Commission notes that this time period includes periods of significant intraday market volatility, including, for example, the initial Covid-19 volatility in March 2020 and the meme stock trading in January 2021. Moreover, the Commission believes that the information submitted by NSCC confidentially provides an overview of how the proposed charge would have helped NSCC address any intraday exposures related to such market volatility. For each trading date during the January 2020 through March 2021 time period, the data provided to the Commission indicates the start of day VaR collected by NSCC across all members, what the intraday VaR need is for all of NSCC as of 4 p.m., the MRD offset, what the intraday volatility charge would have been, and the number of members affected by a call. Based on its review of this data, which indicates what NSCC's intraday exposures would have been during this timeframe by comparing the start of day VaR amounts to the intraday VaR charge based on the day's trading activity, the Commission believes that the proposed intraday volatility charge would help

---

69 Letter from John S. Markle, VP and Deputy General Counsel, Robinhood Securities LLC, at 2 (Aug. 23, 2022), available at https://www.sec.gov/comments/sr-nscc-2022-009/srnscc2022009-20137444-307937.pdf ("Robinhood Letter").

NSCC address significant intraday exposures. Moreover, the commenter indicates that its own analysis showed that it would have incurred an intraday volatility charge approximately once per week.[70] The Commission does not disagree that such a frequency could be possible depending on the commenter's portfolio and any intraday market volatility, and the Commission does not believe that this information renders the proposed intraday volatility charge unreasonable.

As set forth in the proposed rule text filed with this Proposed Rule Change,[71] the proposed intraday volatility charge would provide NSCC the authority to reduce the applicable threshold of 100 percent "if [NSCC] determines that a reduction of the threshold is appropriate to mitigate risks to [NSCC] by accelerating the collection of anticipated additional margin from those Members whose portfolios may present relatively larger risks to [NSCC] on an overnight basis," including, for example, during volatile market conditions or market events that cause increases in trading volumes. The Commission believes that this ability is reasonable and consistent with NSCC's need to manage the risks arising from intraday volatility because it would allow NSCC to respond to market stress in a manner appropriate to the circumstances.

One commenter stated that the proposal did not specify how far NSCC could reduce the intraday volatility charge threshold.[72] The Commission does not believe that the lack of a floor for the threshold is unreasonable. NSCC could only lower the

---

70 Robinhood Letter at 2, supra note 69.

71 See proposed Section I(B)(6) of Procedure XV, available at https://www.sec.gov/rules/sro/nscc/2022/34-95286-ex5.pdf.

72 Robinhood Letter at 2, supra note 69.

threshold, if NSCC determines that a reduction of the threshold is appropriate to mitigate risks to NSCC by accelerating the collection of anticipated additional margin from members whose portfolios may present relatively larger risks to NSCC on an overnight basis, for example, during volatile market conditions or market events that cause increases in trading volumes, and as approved consistent with its internal procedures, which the Commission has reviewed as part of the materials submitted confidentially.[73] and the Commission does not believe that a floor is necessary to ensure transparency. In addition, the Commission understands that members would be informed of any changes to the threshold, based on its review of the confidential materials submitted in connection with this Proposed Rule Change.[74] The Commission also notes that NSCC has similar authority with respect to its intraday mark-to-market charge in its existing Rules.[75] Moreover, as discussed in Section III.D infra, the Commission believes that the increased transparency arising from the Proposed Rule Change with respect to intraday volatility should overall improve a member's ability to understand the potential charges to which it may be subject.

Moreover, given the deficiencies in the current calculation of the intraday backtesting charge, the Commission believes NSCC's proposal to eliminate the intraday backtesting charge would continue to allow NSCC to maintain a risk-based margin system that considers, and produces margin levels commensurate with the risks of its members' portfolios.

---

[73] See notes 48 and 71 supra.

[74] See note 43 supra.

[75] See Procedure XV, Section I(B)(5) of the Rules, supra note 10.

Accordingly, the Commission finds the proposal is consistent with Rule 17Ad-22(e)(6)(i) under the Act because it is designed to assist NSCC in maintaining a risk-based margin system that considers, and produces margin levels commensurate with, the risks of portfolios that experience significant volatility on an intraday basis.[76]

D. Consistency with Rule 17Ad-22(e)(23)(ii) under the Act

Rule 17Ad-22(e)(23)(ii) under the Act requires that each covered clearing agency, like NSCC, establish, implement, maintain and enforce written policies and procedures reasonably designed to provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in NSCC.[77] The Commission believes that the proposal is consistent with Rule 17Ad-22(e)(23)(ii) under the Act for the reason stated below.

As described above in Section II.B, NSCC is proposing to amend its Rules to include a description of the intraday volatility charge, including the thresholds that would trigger the collection of the charge, the exceptions to the collection of the charge when the thresholds are met, the method by which NSCC would calculate that charge, and NSCC's discretion to reduce the percent threshold that triggers the collection of the charge, including the circumstances when NSCC may exercise this discretion. Additionally, NSCC represents that members would be able to continue to use existing tools, including the ability to view the calculated volatility charge in 15-minute increments throughout the business day and the VaR margin calculator available on NSCC's Risk Client Portal, to monitor their positions and anticipate any potential

---

76 17 CFR 240.17Ad-22(e)(6)(i).

77 17 CFR 240.17Ad-22(e)(23)(ii).

intraday charges. For these reasons, the Commission believes the Proposed Rule Change would provide members with sufficient information regarding when and how NSCC may collect additional amounts to address the risks of portfolios that experience significant volatility on an intraday basis. The Commission also believes that the specificity regarding how and when NSCC would calculate the intraday volatility charge provides additional transparency over the "special charge" in NSCC's Rules that allows NSCC to collect a special charge in times of market volatility or price fluctuations. As NSCC states, "[w]hen the intraday volatility charge is triggered, a special charge would not also be required from a Member to address the same volatility risks."[78]

Finally, one commenter asserted that the proposal failed to provide any information regarding what would happen if a member fails to meet an intraday volatility charge.[79] However, NSCC's Rules address a member's requirement to meet its obligations with respect to required margin, as determined by NSCC, and set forth NSCC's authority if a member does not meet its obligations.[80] Therefore, the Commission disagrees that this proposal should have provided more information on what happens if a member does not meet this type of margin call.

Accordingly, the Commission finds that the Proposed Rule Change would enable NSCC to establish, implement, maintain, and enforce written policies and procedures

---

78 See Notice of Filing, supra note 3, at 43359-60.

79 Robinhood Letter at 2-3, supra note 69.

80 See Rule 4, Section 1 and Procedure XV, Section II(B) of the Rules, supra note 10. See also Letter from Timothy Hulse, Managing Director, DTCC, at 1-2 (Sept. 27, 2022), available at https://www.sec.gov/comments/sr-nscc-2022-009/srnscc2022009-20144273-309218.pdf.

reasonably designed to provide sufficient information to enable members to identify and evaluate the risks, fees, and other material costs they incur as NSCC members, consistent with Rule 17Ad-22(e)(23)(ii).

IV. CONCLUSION

On the basis of the foregoing, the Commission finds that the Proposed Rule Change is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act[81] and the rules and regulations promulgated thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act[82] that proposed rule change SR-NSCC-2022-009, be, and hereby is, APPROVED.[83]

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[84]

Sherry R. Haywood
Assistant Secretary

---

81 15 U.S.C. 78q-1.

82 15 U.S.C. 78s(b)(2).

83 In approving the Proposed Rule Change, the Commission considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

84 17 CFR 200.30-3(a)(12).