

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50386; File No. SR-FICC-2003-05)

September 15, 2004

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Order Granting Approval of a Proposed Rule Change Relating to Additional Account Structures

I. Introduction

On July 9, 2003, Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR-FICC-2003-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹. Notice of the proposal was published in the Federal Register on February 13, 2004.² No comment letters were received. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

II. Description

The proposed rule change amends the rules of both the Government Securities Division (“GSD”) and the Mortgage-Backed Securities Division (“MBSD”) of FICC with respect to their additional account structures. GSD and MBSD both permit members to open and maintain accounts in addition to their primary accounts. These additional accounts developed as an administrative convenience for members that wanted to keep certain activities segregated from their primary accounts. The proposed rule change addresses certain legal risks associated with these accounts.

Government Securities Division

For each additional account opened for a member, GSD assigns a unique participant ID

¹ 15 U.S.C. 78s(b)(1).

² Securities Exchange Act Release No. 49212 (February 9, 2004), 69 FR 7273.

number and separately calculates daily clearing fund requirements, funds-only settlement requirements, and net settlement positions based solely upon the activity in the additional account.³ Currently, the opening and maintenance of additional accounts requested by a GSD member is governed by an agreement between the member and GSD.⁴ Pursuant to the additional account agreement, the member agrees to be responsible for all of the obligations and liabilities associated with the additional account; however, GSD's rules do not address the opening and maintenance of these additional accounts.⁵

The proposed rule change reflects the principles set forth in the additional account agreement and those that FICC management has defined to govern these accounts. Specifically, additional accounts that are opened for someone other than a member itself or for the member's wholly-owned subsidiary shall require the approval of FICC's Membership and Risk Management Committee. The proposed rule change makes clear that GSD members will be responsible for all of the obligations arising under GSD's rules that are associated with additional accounts. The additional account entity will not have any proprietary interest with

³ The maintenance of such accounts has billing implications as set forth in GSD's fee structure.

⁴ The additional account structure permitted by GSD should be contrasted with GSD's executing firm feature, which permits a member to submit trades of a non-GSD member with which the member has a correspondent relationship. Executing firm trades are commingled with the member's own trades in the member's GSD account and are not separated from the member's other activity (including other executing firm activity) for any purpose. Therefore, the member's clearing fund requirement, funds-only settlement requirement, and net settlement position reflects all executing firm activity in its GSD account.

⁵ The only exceptions to this are with respect to repo brokers that are expressly required to open second accounts for their brokered repo activity and GSD's fee structure which includes charges associated with the maintenance of additional accounts.

respect to the additional account and will not have any rights or privileges of GSD members. GSD will have the right to deny the opening of an additional account if it believes that the additional account entity presents risk to FICC, such as legal risk from an insolvency regime that is adverse to GSD's rights.

Mortgage-Backed Securities Division

Currently, MBS rules expressly permit participants to open additional accounts upon request for themselves or for any other entity. FICC has reviewed MBS's current rules and is enhancing them by making clear that (i) additional account holders do not have membership or property rights with respect to additional accounts and (ii) MBS may apply collateral associated with one account of a participant to satisfy obligations among any or all of that participant's accounts. These provisions will serve to protect MBS in the event an additional account holder makes a claim with respect to the property, proceeds, or collateral associated with the activity of the account.

III. Discussion

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible.⁶ The proposed rule change, by clarifying the rights and obligations of FICC and of its members with respect to additional accounts established by FICC's members for their own use or for the use of non-members, is designed to protect FICC and its members from any unnecessary financial risks. Accordingly, the proposed rule change should help to assure the safeguarding of securities and funds which are in FICC's custody or

⁶ 15 U.S.C. 78q-1(b)(3)(F).

control or for which it is responsible.

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 and the rules and regulations thereunder applicable.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-FICC-2003-05) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.⁷

Margaret H. McFarland
Deputy Secretary

⁷ 17 CFR 200.30-3(a)(12).

