

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- 82403; File No. SR-NSCC-2017-807)

December 26, 2017

Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing of Advance Notice to Increase the Authorized Amount Under the Prefunded Liquidity Program

Pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act entitled the Payment, Clearing, and Settlement Supervision Act of 2010 (“Clearing Supervision Act”)<sup>1</sup> and Rule 19b-4(n)(1)(i) under the Securities Exchange Act of 1934, as amended (“Act”),<sup>2</sup> notice is hereby given that on December 12, 2017, National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) the advance notice SR-NSCC-2017-807 (“Advance Notice”) as described in Items I, II and III below, which Items have been prepared by the clearing agency. 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

The advance notice of NSCC proposes to increase the aggregate amount of short-term promissory notes (“Commercial Paper”) and extendible-term promissory notes (“Extendible Notes” and, together with the Commercial Paper, “Notes”) that NSCC is authorized to issue and sell, as further described below.<sup>3</sup>

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

<sup>2</sup> 17 CFR 240.19b-4(n)(1)(i).

<sup>3</sup> Terms not defined herein are defined in the Rules and Procedures of NSCC (“Rules”), available at [http://www.dtcc.com/~media/Files/Downloads/legal/rules/nsc\\_rules.pdf](http://www.dtcc.com/~media/Files/Downloads/legal/rules/nsc_rules.pdf).

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

In its filing with the Commission, the clearing agency included statements concerning the purpose of and basis for the Advance Notice and discussed any comments it received on the Advance Notice. The text of these statements may be examined at the places specified in Item IV below. The clearing agency has prepared summaries, set forth in sections A and B below, of the most significant aspects of such statements.

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

NSCC has not solicited or received any written comments relating to this proposal. NSCC will notify the Commission of any written comments received by NSCC.

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

*Description of the Proposal*

NSCC maintains a program to issue and sell the Notes ("Prefunded Liquidity Program" or the "Program"), and is currently authorized to issue and sell the Notes in an aggregate amount up to \$5 billion.<sup>4</sup> NSCC is proposing to increase the aggregate amount of Notes it would be authorized to issue and sell under the Program to \$10 billion.

*Management of the Prefunded Liquidity Program.* Pursuant to the terms and conditions described in the 2015 Advance Notice, NSCC issues Notes to institutional investors, and invests the proceeds in accordance with the Clearing Agency Investment

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<sup>4</sup> The principal terms of the Prefunded Liquidity Program are described in an advance notice (SR-NSCC-2015-802) ("2015 Advance Notice") filed with the Commission pursuant to Section 806(e)(1) of the Clearing Supervision Act and Rule 19b-4(n)(1)(i) under the Act. See Securities Exchange Act Release No. 75730 (August 19, 2015), 80 FR 51638 (August 25, 2015) (SR-NSCC-2015-802).

Policy.<sup>5</sup> The Program is managed and monitored daily by the Treasury group (“Treasury”).<sup>6</sup> NSCC has structured the Prefunded Liquidity Program such that the maturities of the issued Notes are staggered to avoid concentrations of maturing liabilities. The majority of the Notes issued and sold under the Program to date have been Commercial Paper, however, NSCC maintains the flexibility to issue and sell any combination of Commercial Paper and Extendible Notes up to the authorized amount in order to allow it to adjust to the market for each of these types of Notes and to stagger the maturities of the outstanding Notes. Treasury also maintains and adheres to internal guidelines that limit the amount of Notes that can mature within any one-week period. The weighted average maturity of the aggregate Notes outstanding issued under the Prefunded Liquidity Program have generally ranged between one and two months, and, in order to maintain the staggered maturity structure, the weighted average maturity of the Notes would be expected to increase under the proposal to approximately three to six months.

Because the cash proceeds from the Prefunded Liquidity Program are one of NSCC’s existing default liquidity resources, as described below, Treasury, in consultation

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<sup>5</sup> See Securities Exchange Act Release No. 79528 (December 12, 2016), 81 FR 91232, (December 16, 2016) (SR-DTC-2016-007; SR-FICC-2016-005; SR-NSCC-2016-003). The 2015 Advance Notice stated that the proceeds from the issuance of the Notes would be held in a cash deposit account at the Federal Reserve Bank of New York (“FRBNY”). NSCC subsequently adopted the Clearing Agency Investment Policy, which permits NSCC to invest such proceeds in bank deposits either at the FRBNY or at an approved bank counterparty.

<sup>6</sup> Treasury is a part of the Chief Finance Office Organization of The Depository Trust & Clearing Corporation (“DTCC”), NSCC’s parent company. DTCC operates on a shared services model with respect to the NSCC and its affiliates. Most corporate functions are established and managed on an enterprise-wide basis pursuant to intercompany agreements under which it is generally DTCC that provides a relevant service to NSCC and its affiliates.

with the Liquidity Product Risk Unit,<sup>7</sup> makes decisions regarding the aggregate amount of Notes to be issued based on NSCC's projected liquidity needs.

*NSCC Liquidity Risk Management.* NSCC measures and manages its liquidity risks and needs on a daily basis. In compliance with its regulatory requirements, NSCC seeks to maintain liquid resources in a sufficient amount to meet its settlement obligations under a wide range of foreseeable stress scenarios that includes, but is not limited to, the default of the affiliated family of Members that would generate the largest aggregate payment obligation for NSCC in extreme but plausible market conditions.<sup>8</sup> NSCC developed the Prefunded Liquidity Program in order to strengthen its liquidity risk management by supplementing its other liquid resources with additional, prefunded, readily available liquid resources. NSCC's other liquid resources include (1) the cash in its Clearing Fund;<sup>9</sup> (2) the cash that would be obtained by drawing on NSCC's committed 364-day credit facility with a consortium of banks ("Credit Facility");<sup>10</sup> and (3) additional cash deposits, known as "Supplemental Liquidity Deposits."<sup>11</sup> By maintaining multiple

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<sup>7</sup> The Liquidity Product Risk Unit is a part of the Group Chief Risk Office of the DTCC and is responsible for NSCC's liquidity risk management program. *Id.*

<sup>8</sup> Rule 17Ad-22(e)(7)(i).

<sup>9</sup> Rule 4 (Clearing Fund) and Procedure XV (Clearing Fund Formula and Other Matters), *supra* note 3.

<sup>10</sup> Securities Exchange Act Release No. 80605 (May 5, 2017), 82 FR 21850 (May 10, 2017) (SR-DTC-2017-802, SR-NSCC-2017-802).

<sup>11</sup> Rule 4(A) (Supplemental Liquidity Deposits), *supra* note 3. The Supplemental Liquidity Deposits are designed to cover the heightened liquidity exposure arising around monthly option expiry periods and are required from those Members whose activity would pose the largest liquidity exposure to NSCC.

sources for liquidity, NSCC does not have to rely on any one source to meet its liquidity needs.

*Proposed Increase to the Program.* NSCC is proposing to increase the aggregate amount of Notes it would be authorized to issue and sell under the Prefunded Liquidity Program to \$10 billion dollars. The proposal would enable NSCC to continue to maintain a sufficient amount of liquid resources in compliance with its regulatory requirements through the issuance of additional Notes in the event its liquidity needs increase. The proposal also would enable NSCC to meet its regulatory requirements with additional, prefunded, readily available liquid resources, which are available for NSCC to draw as needed to complete end-of-day settlement in the event of a Member default.

Likewise, the proposal would provide NSCC with the flexibility to reduce its reliance on the Credit Facility as necessary. NSCC has observed varying levels of interest by the credit markets in recent years and cannot be certain that it will be able to continue to renew the Credit Facility at levels that would meet its projected liquidity needs in future years. Alternatively, the growth of the Prefunded Liquidity Program since its inception has been supported by a high, and growing, investor interest in high-rated Commercial Paper.<sup>12</sup> Further, while the Credit Facility continues to be an important liquidity resource, it does not provide NSCC with prefunded, readily available liquidity, and incurs a greater cost to maintain than the Prefunded Liquidity Program. The Program would still be a more cost-effective liquidity resources, as compared to the Credit

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<sup>12</sup> In March 31, 2016, NSCC had issued approximately \$1.4 billion in Commercial Paper to 81 investors and, as of July 31, 2017, this increased to approximately \$3 billion in Commercial Paper outstanding to 177 investors. Further, as NSCC's investor base has grown, it has also diversified to include corporations, asset managers, governments, and financial institutions.

Facility, after the proposed increase. Therefore, the proposal would give NSCC the flexibility to better diversify its reliance on the various liquidity resources, including the Prefunded Liquidity Program, as it deems necessary to continue to meet its liquidity needs and in order to manage the associated costs.

NSCC believes the proposal to add \$5 billion to the authorized amount under the Program would provide it with adequate capacity to mitigate an unexpected increase in its liquidity needs and any potential decrease in the aggregate amount under its Credit Facility. NSCC does not anticipate issuing Notes up to the maximum authorized amount in the near term, and believes the proposal would allow it to grow the Program as necessary. NSCC is not proposing any other change to the Prefunded Liquidity Program, which will continue under the same terms and conditions as described in the 2015 Advance Notice.<sup>13</sup>

*Expected Effect on and Management of Risks*

As described above, NSCC believes the proposal to increase the authorized aggregate amount of Notes it can issue under the Prefunded Liquidity Program would enable it to better manage its liquidity risks by providing it with flexibility to increase its reliance on the Program, as necessary and appropriate, in meeting its liquidity needs and associated regulatory requirements.

The Prefunded Liquidity Program, like other liquidity resources, involves certain risks that are standard in any commercial paper or extendible note program. Such risks were addressed in the 2015 Advance Notice and include the risk that NSCC does not have sufficient funds to repay issued Notes when they mature. By increasing the authorized

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<sup>13</sup> Supra note 4.

aggregate amount of the Prefunded Liquidity Program, and thus potentially the aggregate amount of outstanding Notes that it will have to repay upon maturity, NSCC may be further exposed to this risk. However, as discussed in the 2015 Advance Notice, NSCC continues to believe this risk is remote, as the proceeds of the Program would be used only in the event of a Member default, and NSCC would replenish that cash, as it would replenish any of its liquidity resources that are used to facilitate settlement in the event of a Member default, with the proceeds of the close out of that defaulted Member's portfolio. This notwithstanding, in the event that proceeds from the close out are insufficient to fully repay a liquidity borrowing, then NSCC would look to its loss waterfall to repay any outstanding liquidity borrowings. NSCC has also further mitigated this risk by structuring the Prefunded Liquidity Program so that the maturity dates of the issued Notes are sufficiently staggered, which would provide NSCC with time to complete the close out of a defaulted Member's portfolio. As described above, NSCC would continue to follow its internal guidelines in the management of the Program to stagger the maturity dates of the issued Notes, and to extend the weighted average maturity of the issued Notes to maintain this staggered structure.

A second risk is that NSCC may be unable to issue new Notes as issued Notes mature, or that there is a decrease in investor interest in commercial paper. As discussed in the 2015 Advance Notice, this risk is mitigated by the fact that NSCC maintains a number of different liquidity resources, described above, and would not depend on the Prefunded Liquidity Program as its sole source of liquidity.

NSCC believes that the significant systemic risk mitigation benefits of providing NSCC with additional, prefunded liquid resources outweigh these risks.

Consistency with the Clearing Supervision Act

Although the Clearing Supervision Act does not specify a standard of review for an advance notice, its stated purpose is instructive: to mitigate systemic risk in the financial system and promote financial stability by, among other things, promoting uniform risk management standards for systemically important financial market utilities and strengthening the liquidity of systemically important financial market utilities.<sup>14</sup>

Section 805(a)(2) of the Clearing Supervision Act<sup>15</sup> authorizes the Commission to prescribe risk management standards for the payment, clearing and settlement activities of designated clearing entities, like NSCC, and financial institutions engaged in designated activities for which the Commission is the supervisory agency or the appropriate financial regulator. Section 805(b) of the Clearing Supervision Act<sup>16</sup> states that the objectives and principles for the risk management standards prescribed under Section 805(a) shall be to, among other things, promote robust risk management, promote safety and soundness, reduce systemic risks, and support the stability of the broader financial system.

The overall impact of the proposal is to reduce the liquidity risks associated with NSCC's operation as a central counterparty by providing it with additional, prefunded liquidity to complete end-of-day settlement in the event of a Member default. By reducing NSCC's liquidity risks, the proposal would promote its robust risk management. Given its important role in mitigating risks faced by its Members and the financial

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<sup>14</sup> See 12 U.S.C. 5461(b).

<sup>15</sup> 12 U.S.C. 5464(a)(2).

<sup>16</sup> 12 U.S.C. 5464(b).

markets, a reduction in NSCC’s liquidity risk would also reduce systemic risk, and would promote the safety, soundness and stability in the broader financial system. Therefore, NSCC believes the proposal is consistent with Section 805(b) of the Clearing Supervision Act.<sup>17</sup>

NSCC also believes that the proposal is consistent with the requirements of the Act, and the rules and regulations thereunder applicable to a registered clearing agency. In particular, NSCC believes the proposal is consistent with Rule 17Ad-22(e)(7)(ii) under the Act.<sup>18</sup>

Rule 17Ad-22(e)(7)(ii) under the Act requires that a covered clearing agency hold qualifying liquid resources sufficient to meet the minimum liquidity resource requirement under Rule 17Ad-22(e)(7)(i) in each relevant currency for which the covered clearing agency has payment obligations owed to clearing members.<sup>19</sup> Rule 17Ad-22(a)(14) under the Act defines “qualifying liquidity resources,” in part, as cash held either at the central bank of issue or at creditworthy commercial banks.<sup>20</sup>

The proceeds of the Program are cash held at either the FRBNY or a bank counterparty that has been approved pursuant to the Clearing Agency Investment Policy, and, as such, are considered “qualifying liquid resources” under Rule 17Ad-22(a)(14).<sup>21</sup>

These proceeds are available for NSCC to draw as needed to complete end-of-day

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<sup>17</sup> Id.

<sup>18</sup> 17 CFR 240.17Ad-22(e)(7)(ii).

<sup>19</sup> Id.

<sup>20</sup> 17 CFR 240.17Ad-22(a)(14).

<sup>21</sup> Id.

settlement in the event of the default of a Member, and, as such, are one of NSCC's liquidity resources that it maintains in order to meet its settlement obligations under a wide range of foreseeable stress scenarios that includes, but is not limited to, the default of the affiliated family of Members that would generate the largest aggregate payment obligation for NSCC in extreme but plausible market conditions, in compliance with NSCC's requirement under Rule 17Ad-22(e)(7)(i). The proposal to increase the authorized amount of Notes NSCC may issue under the Program would enable NSCC to increase the amount of qualifying liquid resources it holds for these purposes. Therefore, the proposal would enable NSCC to continue to meet its requirements under Rule 17Ad-22(e)(7)(ii) in the event its liquidity needs increase.<sup>22</sup>

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

The proposed change may be implemented if the Commission does not object to the proposed change within 60 days of the later of (i) the date that the proposed change was filed with the Commission or (ii) the date that any additional information requested by the Commission is received. 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 the advance notice is filed, or the date further information requested by the Commission is received, if the Commission notifies the clearing agency in writing that it does not object to the proposed change and

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Id.

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.

#### 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 Number SR-NSCC-2017-807 on the subject line.

##### Paper Comments:

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

All submissions should refer to File Number SR-NSCC-2017-807. 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 the filing also will be available for inspection and copying at the principal office of NSCC and on DTCC's website (<http://dtcc.com/legal/sec-rule-filings.aspx>). All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NSCC-2017-807 and should be submitted on or before [insert date 15 days from publication in the Federal Register].

By the Commission.

Brent J. Fields,  
Secretary