

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62743; File No. SR-FICC-2010-05)

August 19, 2010

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing and Order Granting Accelerated Approval on a Temporary Basis of Proposed Rule Change to Modify the Rules of the Government Securities Division Regarding the Calculation of Clearing Fund Deposits Relating to Inter-Dealer Broker Positions

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder² notice is hereby given that on August 18, 2010, the Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I and II below, which items have been prepared primarily by FICC.³ The Commission previously approved the proposal on a temporary basis.⁴ The Commission is publishing this notice and order to solicit comments on the proposed rule change from interested parties and to grant accelerated approval through February 18, 2011.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The proposed rule change seeks to modify the rules of FICC’s Government Securities Division (“GSD”) regarding the calculation of clearing fund requirements relating to inter-dealer broker (“IDB”) positions.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ FICC withdrew a substantively identical proposed rule change filed on August 4, 2010, that sought approval without requesting that the approval would be temporary.

⁴ Securities Exchange Act Release No. 60510 (August 17, 2009), 74 FR 42716 (August 24, 2009).

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FICC included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FICC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

The GSD maintains a clearing fund comprised of deposits of cash and eligible securities from its members to provide liquidity and to satisfy any losses that might otherwise be incurred as a result of a member's default and the subsequent close-out of its positions. The GSD uses a Value-at-Risk ("VaR") methodology to calculate clearing fund requirements.⁵ The clearing fund methodology used by GSD analyzes risk by reference to three factors: (1) end-of-day VaR charge assessing market volatility for observed open positions at end-of-day after giving effect to offsetting positions within the portfolio; (2) "margin requirement differential" ("MRD") to address intraday risk; and (3) "coverage component" ("CC") to adjust the calculation if necessary to reach a given confidence level.⁶ The margin calculation is predicated upon an assumption that the open positions of a defaulting member would be liquidated at the end of a three-day period.

⁵ VaR is defined as the maximum amount of money that may be lost on a given portfolio over a given period of time within a given confidence level.

⁶ Under the GSD clearing fund procedures, CC is not calculated with respect to IDB repo transactions. The GSD has recently adjusted the CC charge with respect to certain IDB cash transactions.

IDBs function as intermediaries trading with multiple counterparties, allowing anonymity between trading parties, and providing liquidity for the market. IDBs handle large transactions and operate on small spreads. They perform a critical function in the government securities market in the absence of a centralized trading exchange.

IDBs submit affirmed trades from their systems to the GSD with each trade matched to the counterparty that will ultimately deliver or receive the securities. Although IDBs do not generally hold positions, they may incur positions at the GSD when their counterparties are not GSD members. Because these trades are matched by the IDB to a counterparty prior to submission to the GSD, FICC represents that the risk to FICC in the case of an IDB's default is different from that presented when a dealer member submits a trade that may not have been already matched to a contraside.

The clearing fund requirement applicable to IDB transactions has increased significantly because of recent market volatility to the point where FICC believes it is disproportionate to the risk that IDB activity presents to the GSD. Given the importance of IDB transactions in the government securities marketplace, undue and unsustainable margin requirements on GSD IDB activity may be harmful and may introduce systemic risk in the event members are motivated to avoid imposition of disproportionate changes by netting outside of the GSD or by delaying trade submission until later in the day. Accordingly, the GSD adjusted the calculation of the CC charge for IDB transactions in November 2008 and conducted a review of the current margin methodology as applied to IDB activity.

As a result of this review, the GSD proposed and the Commission approved the use of a one-day liquidation assumption when calculating clearing fund requirements applicable to IDB

activity.⁷ Since IDB trades are matched prior to submission, the GSD believes that the one-day liquidation period as opposed to a three-day liquidation period is a more reasonable assumption in this context. The assumption of a three-day liquidation period will continue to apply to non-IDB activity.

The GSD will continue to monitor the IDB activity of its members and to periodically reassess whether the one-day liquidation period provides adequate coverage. In this regard, FICC will provide the Commission with data to allow the Commission to track the magnitudes and behaviors of the VaR calculations using a one-day liquidation horizon and using a three-day liquidation horizon and with such other information that the Commission may request. FICC further notes its ability under GSD Rule 4 to impose special charges in response to market circumstances or other risk factors with respect to a particular member.

FICC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act⁸ and the rules and regulations thereunder because the proposed change will modify the calculation of clearing fund requirements for IDB positions so that the clearing fund requirements is correlated more closely with the level of risk associated with IDB positions.

(B) Self-Regulatory Organization's Statement on Burden on Competition

FICC does not believe that the proposed rule change will have any impact or impose any burden on competition.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments relating to the proposed rule change have not yet been solicited or received. FICC will notify the Commission of any written comments received by FICC.

⁷ See note 4.

⁸ 15 U.S.C. 78q-1.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder and particularly with the requirements of Section 17A(b)(3)(F).⁹ Section 17A(b)(3)(F) requires that the rules of a clearing agency remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which it is responsible. The Commission finds that the approval of FICC's rule change on a temporary basis through February 18, 2011 is consistent with this section because by allowing FICC to temporarily modify its rules regarding the calculation of clearing fund requirements for IDB positions to what it believes correlates more closely with the level of risk associated with such positions, FICC will be taking steps toward potentially improving the national clearance and settlement system while still actively monitoring its ability to fulfill its safeguarding obligations.

FICC has requested that the Commission approve the proposed rule prior to the thirtieth day after publication of the notice of the filing. The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the publication of notice because such approval will allow FICC to continue to attempt to correlate IDBs' clearing fund requirements with the level of risk associated with their positions.

The Commission is approving the proposed rule filing on a temporary basis through February 18, 2011, so that FICC will have time to further evaluate the modified calculation of clearing fund requirements for IDB positions and to report its findings and conclusions to the Commission and so that the Commission will have time to evaluate FICC's findings and

⁹ 15 U.S.C. 78q-1(b)(3)(F).

conclusions before a final determination is made regarding adoption of any rule on a permanent basis.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the 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. Please include File Number SR-FICC-2010-05 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 Number SR-FICC-2010-05. 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 Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change 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 Web site viewing and printing in the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am

and 3:00 pm. Copies of such filings also will be available for inspection and copying at the principal office of FICC and on FICC's Web site at http://dtcc.com/downloads/legal/rule_filings/2010/ficc/2010-05.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 Number SR-FICC-2010-05 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁰ that the proposed rule change (File No. SR-FICC-2010-05) be and hereby is approved on an accelerated basis through February 18, 2011.¹¹

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.¹²

Florence E. Harmon
Deputy Secretary

¹⁰ 15 U.S.C. 78s(b)(2).

¹¹ 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).

¹² 17 CFR 200.30-3(a)(12).