

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-69890; File No. SR-NSCC-2013-05)

June 28, 2013

Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change to Require that All Locked-in Trade Data Submitted to It for Trade Recording be Submitted in Real-time

I. Introduction

On April 30, 2013, the National Securities Clearing Corporation (“NSCC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change SR-NSCC-2013-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder.² On May 14, 2013, NSCC filed with the Commission Amendment No. 1 to the proposed rule change.³ The proposed rule change was published for comment in the Federal Register on May 20, 2013.⁴ The Commission received one comment letter to the proposed rule change.⁵ For the reasons discussed below, the Commission is granting approval of the proposed rule change.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, NSCC corrected a typographical error in the text of its Rules & Procedures (“Rules”) related to the proposed rule change.

⁴ Release No. 34-69571 (May 14, 2013), 78 FR 29408 (May 20, 2013).

⁵ Comment letter from Kermit Kubitz dated June 10, 2013, <http://www.sec.gov/comments/sr-nsc-2013-05/nsc201305.shtml>. The commenter supports the proposed rule change’s requirement “to submit trades without any pre-processing . . .” and believes that, “any cost associated with submitting higher volumes of data from limiting pre-netting is small compared to the risks and costs of inaccurate data which might result from submission of other than accurate trade data.”

II. Description

NSCC filed the proposed rule change to require that all locked-in trade data submitted to NSCC for trade recording be submitted in real-time,⁶ and to prohibit pre-netting⁷ and other practices that prevent real-time trade submission, as discussed below.

Proposal Overview

According to NSCC, the majority of all transactions processed at NSCC are submitted on a locked-in basis by self-regulatory organizations (“SRO”) (including national and regional exchanges and marketplaces), and Qualified Special Representatives (“QSR”).⁸ Currently, NSCC data reveals that almost all exchanges⁹ 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 rule change will require that all locked-in trades submitted for

⁶ 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.

⁷ According to NSCC, any pre-netting practices include: (i) “summarization” (i.e., a technique in which the clearing broker nets all trades in a single CUSIP by the same correspondent broker into fewer submitted trades); (ii) “compression” (i.e., a 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); (iii) netting; and (iv) any other practice that combines two or more trades prior to their submission to NSCC (collectively, “Pre-netting”).

⁸ QSRs are NSCC members (“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.

⁹ One executing market with very low trade volume does not yet submit trades in real-time.

trade recording by SROs and QSRs be submitted to NSCC in real-time.¹⁰

NSCC will also prohibit Pre-netting practices that preclude real-time trade submission. NSCC states that typically, Pre-netting is done on a bilateral basis between a QSR and its customer, both NSCC Members. According to NSCC, Pre-netting practices disrupt NSCC's ability to accurately monitor market and credit risks as they evolve during the trading day. Therefore, NSCC will prohibit Pre-netting activity on the part of entities submitting original trade data on a locked-in basis.¹¹ The rules of NSCC's affiliate Fixed Income Clearing Corporation ("FICC") currently prohibit such activity, and this rule change will align NSCC's trade submission rules with those of FICC.¹²

Further, NSCC does not expect the rule changes to impact trade volumes significantly. According to NSCC, the majority of trades are currently being submitted to NSCC in real-time

¹⁰ 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.

¹¹ 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.

¹² 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. 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).

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.

In the wake of recent industry disruptions, industry participants have been focused on developing controls to address the risks that arise from technology issues. 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 rule 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.¹³

Implementation Timeframe

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

III. Discussion

Section 19(b)(2)(C) of the Act¹⁴ 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. Section 17A(b)(3)(F) of the Act¹⁵ requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of

¹³ See Market Technology Roundtable Comment Letter dated Sept. 28, 2012, available at <http://www.sec.gov/comments/4-652/4652-17.pdf>.

¹⁴ 15 U.S.C. 78s(b)(2)(C).

¹⁵ 15 U.S.C. 78q-1(b)(3)(F).

securities transactions. The Commission finds that the rule change is consistent with these requirements because the receipt of locked-in trade data on a real-time basis should 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 on a closer to real-time basis, thereby potentially minimizing a source of operational risk and facilitating the prompt and accurate clearance and settlement of securities transactions.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act¹⁶ and the rules and regulations thereunder.

¹⁶ 15 U.S.C. 78q-1.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁷ that the proposed rule change (File No. SR-NSCC-2013-05) be, and hereby is, approved.¹⁸

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.¹⁹

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Deputy Secretary

¹⁷ 15 U.S.C. 78s(b)(2).

¹⁸ In approving the proposed rule change, the Commission considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁹ 17 CFR 200.30-3(a)(12).