

**National Securities Clearing Corporation**

**Consolidated Financial Statements**

**For the years ended December 31, 2007 and 2006**

**National Securities Clearing Corporation**  
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**For the years ended December 31, 2007 and 2006**

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## Report of Independent Auditors

To the Board of Directors and Shareholder of  
National Securities Clearing Corporation:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and retained earnings and of cash flows present fairly, in all material respects, the financial position of National Securities Clearing Corporation and its subsidiary (the "Company") at December 31, 2007 and 2006, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 5 to the consolidated financial statements, the Parent changed the manner in which it accounts for its defined benefit pension and other postretirement plans in 2006.

*PricewaterhouseCoopers LLP*

February 15, 2008

# Consolidated Balance Sheet

(IN THOUSANDS, EXCEPT SHARE DATA)

December 31,	2007	2006
<b>Assets</b>		
Cash and cash equivalents	<b>\$4,882,087</b>	\$2,750,773
U.S. Treasury securities	<b>180,340</b>	119,517
Accounts receivable	<b>13,071</b>	5,358
Clearing fund	<b>306,951</b>	331,839
Fixed assets, less accumulated depreciation and amortization of \$74,856 and \$69,237 at December 31, 2007 and 2006, respectively	<b>39,694</b>	36,474
Deferred income taxes, net	<b>18,567</b>	21,963
Other assets	<b>2,265</b>	2,482
Total assets	<b>\$5,442,975</b>	\$3,268,406
<b>Liabilities and Shareholder's Equity</b>		
Liabilities:		
Accounts payable and other liabilities	<b>\$60,059</b>	\$84,831
Payable to participants	<b>448,313</b>	275,258
Long-term debt	<b>18,027</b>	21,687
Clearing fund:		
Cash deposits	<b>4,559,625</b>	2,504,791
Other deposits	<b>306,951</b>	331,839
Total liabilities	<b>5,392,975</b>	3,218,406
Commitments and contingent liabilities (Note 9)		
Shareholder's equity:		
Common stock, \$.50 par value: 30,000 shares authorized, 20,000 shares issued and outstanding	<b>10</b>	10
Paid in capital	<b>590</b>	590
Retained earnings	<b>49,400</b>	49,400
Total shareholder's equity	<b>50,000</b>	50,000
Total liabilities and shareholder's equity	<b>\$5,442,975</b>	\$3,268,406

The accompanying notes are an integral part of these financial statements.

# Consolidated Statements of Income and Retained Earnings

(IN THOUSANDS)

For the Year Ended December 31,

2007

2006

	2007	2006
<b>Revenues:</b>		
Clearing services	\$239,705	\$206,080
Distribution and other services	95,478	92,695
Interest income	244,016	168,473
Total revenues	579,199	467,248
Discounts and other refunds to participants	(441,202)	(298,501)
<b>Net revenues</b>	<b>137,997</b>	<b>168,747</b>
<b>Expenses:</b>		
Employee compensation and related benefits	82,704	118,378
Information technology	18,862	15,117
Professional and other services	20,489	16,796
Occupancy	11,418	13,422
Other general and administrative	5,160	4,922
<b>Total expenses</b>	<b>138,633</b>	<b>168,635</b>
(Loss) income before income taxes	(636)	112
(Benefit) provision for income taxes	(636)	112
<b>Net income</b>	<b>-</b>	<b>-</b>
Retained earnings, beginning of year	49,400	49,400
Retained earnings, end of year	\$49,400	\$49,400

The accompanying notes are an integral part of these financial statements.

# Consolidated Statements of Cash Flows

(IN THOUSANDS)

For the Year Ended December 31,

2007

2006

Cash flows from operating activities:		
Net income	\$ -	\$ -
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of fixed assets	11,167	10,555
Loss on fixed asset disposals	-	27
Net discount accreted on U.S. Treasury securities owned	(711)	(1,745)
Deferred income taxes	3,396	(8,994)
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	(7,713)	6,107
Decrease in other assets	217	50
Decrease in accounts payable and other liabilities	(24,772)	(9,138)
Increase in payable to participants	173,055	16,725
Increase in clearing fund cash deposits	2,054,834	216,024
Net cash provided by operating activities	2,209,473	229,611
Cash flows from investing activities:		
Maturities of investments in U.S. Treasury securities	140,000	115,000
Purchases of investments in U.S. Treasury securities	(200,112)	(118,537)
Purchases of fixed assets	(14,387)	(8,890)
Transfer of fixed assets from Fixed Income Clearing Corporation	-	(415)
Net cash used in investing activities	(74,499)	(12,842)
Cash flows from financing activities:		
Capitalized leases	-	1,501
Principal payments on debt and capital lease obligations	(3,660)	(3,674)
Net cash used in financing activities	(3,660)	(2,173)
Net increase in cash and cash equivalents	2,131,314	214,596
Cash and cash equivalents, beginning of year	2,750,773	2,536,177
Cash and cash equivalents, end of year	\$4,882,087	\$2,750,773
Supplemental disclosure:		
Income taxes paid, net of refunds	\$3,456	\$14,700
Interest paid	\$927	\$1,161

## NOTE 1 BUSINESS AND OWNERSHIP

National Securities Clearing Corporation (NSCC), a clearing agency registered with the U.S. Securities and Exchange Commission (SEC), provides various services to members of the financial community (participants), consisting principally of securities trade comparison, netting, risk management, clearance and settlement.

NSCC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). The other principal operating subsidiaries of DTCC are The Depository Trust Company (DTC), Fixed Income Clearing Corporation (FICC), DTCC Deriv/SERV LLC, and DTCC Solutions LLC.

## NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Presentation:** The consolidated financial statements include the accounts of NSCC and its wholly-owned subsidiary. Intercompany accounts and transactions are eliminated in consolidation.

**Cash Equivalents:** NSCC invests funds in overnight reverse repurchase agreements, commercial paper and money market accounts which are considered cash equivalents. Reverse repurchase agreements provide for NSCC's delivery of cash in exchange for securities having a market value which is at least 102% of the amount of the agreement. Custodians designated by NSCC that are participants take possession of the securities. Overnight reverse repurchase agreements are recorded at the contract amounts and totaled \$4,677,299,000 and \$2,620,736,000 at December 31, 2007 and 2006, respectively. At December 31, 2007, the counterparties to these agreements were five major financial institutions that are also participants.

Overnight investments in commercial paper totaling \$20,325,000 and \$20,491,000 are included in cash equivalents at December 31, 2007 and 2006, respectively. At December 31, 2007, the issuer of the commercial paper was one major U.S. bank holding company that is also a participant.

Money market accounts with participants are used to sweep any remaining funds available. Overnight investments made in money market accounts totaling \$181,715,000 and \$108,793,000, representing deposits received from participants to facilitate their compliance with customer protection rules of the SEC, are also included in cash equivalents at December 31, 2007 and 2006, respectively. At December 31, 2007, the money market balance was with one participant.

**U.S. Treasury Securities:** U.S. Treasury securities are recorded at amortized cost and are considered to be held-to-maturity securities. The market values of these securities, which are due in less than one year, at December 31, 2007 and 2006, are \$181,085,000 and \$119,479,000, respectively. At December 31, 2007 and 2006, these securities were held with a participant in an account for the exclusive benefit of participants to facilitate their compliance with customer protection rules of the SEC.

# Notes to Consolidated Financial Statements

December 31, 2007 and 2006

**Fixed Assets:** Fixed assets consist of the following at December 31, 2007 and 2006:

(Dollars in thousands)	2007	2006
Land	\$1,540	\$1,540
Buildings and improvements	18,577	14,724
Leasehold improvements	10,336	10,336
Furniture and equipment	28,529	30,318
Software	50,012	43,238
Lease property under capital leases	5,556	5,555
Total cost	114,550	105,711
Less accumulated depreciation and amortization	74,856	69,237
Net book value	\$39,694	\$36,474

Buildings and improvements are primarily amortized over 39 years using the straight-line method. Leasehold improvements are amortized using the straight-line method over their useful lives or the remaining term of the related lease, whichever is shorter. Furniture and equipment are depreciated over estimated useful lives ranging from three to eight years, principally using accelerated methods. Software is amortized using the straight-line method over an estimated useful life of three years.

NSCC capitalized costs related to software that was developed for internal use or purchased totaling \$6,774,000 and \$4,153,000 in 2007 and 2006, respectively. The amortization of capitalized and purchased software costs was \$5,304,000 in 2007 and \$5,030,000 in 2006. The depreciation of other fixed assets was \$5,863,000 in 2007 and \$5,525,000 in 2006.

During 2007, there were no fixed asset disposals.

**Income Taxes:** Deferred tax assets and liabilities represent the expected future tax consequences of temporary differences between the carrying amount and tax basis of assets and liabilities. The net deferred tax asset is expected to be fully realized and, accordingly, no valuation allowance was established.

**Discounts and other refunds to participants:** NSCC provides discounts on its billing to participants based upon the amount of earnings to be retained in a given year with due regard to current and anticipated needs, as determined by its Board of Directors. Such discounts amounted to \$222,280,000 in 2007 and \$146,626,000 in 2006.

NSCC invests available clearing fund cash deposits principally in overnight reverse repurchase agreements. The earnings on these investments are passed through to participants and are included in interest income and discounts and other refunds to participants. Such earnings totaled \$218,922,000 and \$151,875,000 in 2007 and 2006, respectively.

**Payable to Participants:** Payable to participants includes settlement accounts payable of \$316,468,000 at December 31, 2007 and \$227,330,000 at December 31, 2006 which primarily represents deposits received from participants to facilitate their compliance with customer protection rules of the SEC.

**Revenue Recognition:** Revenue is recognized as services are rendered. Activities are captured daily and billed on a monthly basis.

**Expense Allocations:** Substantially all expenses are recorded at DTCC and are allocated to its subsidiaries based upon their use of such goods or services as determined by applicable allocation factors.

# Notes to Consolidated Financial Statements

December 31, 2007 and 2006

**Financial Instruments:** Management believes that the carrying value of all financial instruments which are short-term in nature approximates current market value. Due to the fixed term nature of long-term debt, if the company was to seek the same financing at December 31, 2007, the fixed rates assigned to these loans would be current borrowing rates available to companies with similar credit ratings.

**Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## NOTE 3 CLEARING FUND

NSCC's rules require certain participants to maintain clearing fund deposits based on calculated requirements, which were \$3,468,280,000 and \$1,814,897,000, at December 31, 2007 and 2006, respectively. The clearing fund is available to secure participants' obligations and certain liabilities of NSCC should they occur. All clearing fund cash and securities are recorded on the balance sheet. A summary of the total deposits held at December 31, 2007 and 2006, including \$1,398,296,000 and \$1,137,267,000, respectively, in excess of calculated requirements follows:

(Dollars in thousands)	2007	2006
Cash	\$4,559,625	\$2,504,791
Securities issued or guaranteed by the U.S. Government, at market value	306,951	331,839
Letters of credit issued by authorized banks	-	115,534
<b>Total</b>	<b>\$4,866,576</b>	<b>\$2,952,164</b>

## NOTE 4 TRANSACTIONS WITH RELATED PARTIES

**SIAC:** Under the terms of a prior agreement, the Securities Industry Automation Corporation (SIAC), an entity owned by the NYSE Group and the American Stock Exchange, had provided computer facilities, personnel and support services to NSCC. SIAC charged NSCC for these services based on its direct and overhead costs arising from providing such services. There were no charges under this agreement in 2007.

Beginning in 2004, NSCC and SIAC agreed to the migration of certain systems applications to DTCC. The insourcing of these applications was completed on October 29, 2004. In accordance with Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," NSCC accrued \$31,604,000 in 2004 to recognize its estimated obligations for real estate, severance pay, fixed asset abandonment, overhead and related expenses. During 2006, NSCC paid \$3,454,000 during the first quarter, and a final settlement of \$15,546,000 in July to satisfy all remaining obligations relating to the insourcing agreement.

**DTCC:** NSCC has an agreement with DTCC whereby DTCC disburses substantially all funds required to sustain the operations of NSCC. The principal exceptions are SIAC and DTC costs. The related expenses are allocated to NSCC based upon NSCC's use of such goods or services. Further, the agreement provides that DTCC performs credit and quantitative risk services, and certain other services for NSCC including administrative, internal audit, finance and legal services. In 2007, the billing for these services was determined as 102% of total allocated expenses excluding pass through charges and the impact of capitalized software. The billing for these services in 2006 was at 110% of the

# Notes to Consolidated Financial Statements

December 31, 2007 and 2006

cost of the services. The fee representing the amount over actual cost included in professional and other services expense was \$2,945,000 in 2007 and \$3,270,000 in 2006. At December 31, 2007 and 2006, the net payable to DTCC included in accounts payable and other liabilities totaled approximately \$53,887,000 and \$79,892,000, respectively.

**DTC:** DTC fees in 2007 and 2006 included \$50,000 and \$53,000, respectively, relating to charges for NSCC participants which NSCC sponsors at DTC. Such amounts are rebilled to the related participants and are included in revenues from services. Further, NSCC provided various computer services to DTC through SIAC under NSCC's agreement with SIAC. As a result of the insourcing of certain systems applications to DTCC, NSCC has discontinued providing these services to DTC. The net amounts payable to DTC included in accounts payable and other liabilities at December 31, 2007 and 2006 were \$19,000 and \$3,000, respectively.

**FICC:** NSCC had an agreement with FICC whereby NSCC provided credit and quantitative risk services to FICC. Effective October 1, 2006, this agreement was terminated and DTCC began providing these services under its service agreement with FICC. NSCC also provided various computer services to FICC through SIAC under NSCC's agreement with SIAC. Beginning in 2005, FICC and SIAC agreed to migrate the systems applications to DTCC. The insourcing of these applications as specified in the agreement was completed on October 15, 2005. As a result, NSCC has discontinued providing these services to FICC. Further, NSCC has an agreement with FICC whereby FICC provides real-time trade matching services to NSCC. At December 31, 2007 and 2006, no amounts were due from FICC.

**Omgeo LLC:** DTCC has an agreement with Omgeo LLC (Omgeo), a joint venture with Thomson Financial whereby, if Omgeo reduces or terminates certain services it receives from DTCC or its affiliates, Omgeo will pay certain extraction costs as specified in the agreement. Such charges relating to NSCC included in reimbursement from affiliates were \$5,000 in 2007 and \$107,000 in 2006.

## NOTE 5 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

All eligible employees of NSCC participate in DTCC's trustee, noncontributory defined benefit pension plan. In addition, NSCC participates in DTCC's noncontributory supplemental executive retirement and benefit restoration plans which provide for certain benefits to eligible executives of NSCC upon retirement. Further, NSCC participates in DTCC's life insurance program, which provides payment of death benefits to beneficiaries of eligible retired employees, and DTCC's healthcare program which provides benefits to eligible retired employees. DTCC's costs for these plans aggregated \$52,397,000 in 2007 and \$54,418,000 in 2006.

In accordance with Financial Accounting Standards Board Statement No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans," DTCC recorded a credit of \$45,613,000 on a pre-tax basis offset by a deferred tax reversal of \$18,547,000 resulting in a net credit of \$27,066,000 to the accumulated other comprehensive loss account to report the funded status of the defined benefit pension and other postretirement benefit plans, thereby increasing shareholders' equity in 2007. The reduction in the obligation was primarily the result of an increase in the interest rate used to discount the projected benefit obligation to its present settlement amount. The remaining net charge in shareholders' equity represents an amount not yet recognized as pension expense.

The impact of DTCC adopting this standard in 2006 was a charge of \$121,718,000 on a pre-tax basis offset by a deferred tax asset of \$45,411,000 resulting in a net charge of \$76,307,000 to the accumulated other comprehensive loss account, thereby reducing shareholders' equity. In addition, a credit of \$24,400,000 was recorded on a pre-tax basis offset by a deferred tax liability of \$10,084,000 resulting in a net credit of \$14,316,000 to the accumulated other comprehensive loss account to reflect a net reduction in the additional minimum pension liability, thereby increasing shareholders' equity, due to an increase in the interest rate used to discount the projected benefit obligation to its present settlement amount and an increase in the fair value of plan assets reflecting the actual rate of return exceeding the expected return in 2006.

# Notes to Consolidated Financial Statements

December 31, 2007 and 2006

NSCC's share of the periodic charges and accumulated other comprehensive credit was a credit of \$1,494,000 in 2007. Such amount is included in employee compensation and related benefits. The equivalent amount for 2006 was a charge of \$29,738,000. Charges are based primarily upon the proportion of NSCC's salary costs to aggregate salary costs for DTCC and its subsidiaries and credits are determined on a first-in-first-out basis.

Disclosures of pension and other post-retirement benefit obligations, expense components and actuarial assumptions for the DTCC plans are included in DTCC's consolidated financial statements.

## NOTE 6 INCOME TAXES

NSCC is included in DTCC's consolidated Federal, combined New York State and New York City, and unitary California and Illinois income tax returns. A separate company Florida return is filed. The provision for income taxes calculated on a separate company basis for the years ended December 31, 2007 and 2006 consists of the following:

(Dollars in thousands)	2007	2006
Current income taxes:		
Federal	(\$3,147)	\$8,183
State and local	(885)	923
Deferred income tax (benefit):		
Federal	3,354	(8,903)
State and local	42	(91)
(Benefit) provision for income taxes	(\$636)	\$112

The 2007 benefit is primarily due to the pre-tax book loss increased by the reversal of deferred tax assets, such as book capitalized costs currently deductible on the tax return and changes to other comprehensive income.

The major temporary differences that gave rise to the deferred tax assets (liabilities) at December 31, 2007 and 2006 are as follows:

(Dollars in thousands)	2007	2006
Employee benefit related	\$19,792	\$21,297
Depreciation and amortization	1,048	1,297
Lease abandonment costs	66	(2,854)
Capitalization of software developed for internal use	(3,794)	462
Other	1,455	1,761
Net deferred income tax asset	\$18,567	\$21,963

# Notes to Consolidated Financial Statements December 31, 2007 and 2006

On November 7, 2007, the Financial Accounting Standards Board voted to defer the effective date of Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," for all non-public companies for the periods beginning after December 15, 2007. This decision was confirmed with the issuance of FASB Staff Position No. Fin 48-2 on February 1, 2008. FIN 48 establishes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The impact of applying this interpretation beginning in 2008 is not expected to have a material effect on the financial position of the company.

## NOTE 7 LONG-TERM DEBT AND LINES OF CREDIT

Long-term debt at December 31, 2007 and 2006 consists of the following:

(Dollars in thousands)	2007	2006
Notes payable	\$14,816	\$16,911
Sale-leaseback obligation	1,262	1,454
Capital lease obligations	1,949	3,322
<b>Total</b>	<b>\$18,027</b>	<b>\$21,687</b>

Notes payable at December 31, 2007 include secured borrowings totaling \$8,500,000 from two insurance companies at a fixed rate of 4.62%. The notes are secured by property, plant and equipment. Principal and interest payments are due semi-annually on March 15 and September 15 of each year through 2012. Interest expense related to these notes totaled \$429,000 in 2007 and \$509,000 in 2006. Notes payable also include unsecured borrowings totaling \$6,316,000 from an insurance company to finance the acquisition of real estate, at a fixed rate of 5.03%. Principal payments are due annually on December 15 of each year through 2023. Interest payments are due semi-annually on June 15 and December 15 of each year, through the same period. Interest expense related to these notes totaled \$338,000 in 2007 and \$357,000 in 2006.

In March 2003, the company entered into a sale-leaseback transaction covering certain assets aggregating \$1,800,000. The company treated this transaction as a financing arrangement and depreciates the assets using its normal depreciation policy. Payments under this arrangement are due in installments from 2004 to 2009. The implicit interest rate on the obligation is 4.7%.

Leased property meeting certain criteria is capitalized and the present value of the related lease payments is recorded as a liability. At December 31, 2007, future minimum payments including interest, which are due through 2010, totaled \$2,233,000. Payments over the next three years are \$1,239,000, \$820,000, and \$174,000, respectively.

At December 31, 2007, NSCC maintained a committed line of credit of \$4,100,000,000 with 24 major banks that are primarily participants to provide for potential liquidity needs. In addition, a \$50,000,000 shared credit line with DTC and DTCC is maintained with a participant to support potential short-term operating cash requirements. During 2007, there were no borrowings under these credit facilities.

**NOTE 8 SHAREHOLDER'S EQUITY**

(Dollars in thousands)	Common stock	Paid in Capital	Retained Earnings
Balance at December 31, 2005	\$10	\$590	\$49,400
Net income 2006	-	-	-
Balance at December 31, 2006	10	590	49,400
Net income 2007	-	-	-
Balance at December 31, 2007	\$10	\$590	\$49,400

**NOTE 9 COMMITMENTS AND CONTINGENT LIABILITIES**

The CNS system interposes NSCC between participants in securities clearance and settlement. CNS transactions are generally guaranteed as of the later of midnight of T+1, or midnight of the day they are reported to the membership as compared/recorded. Since all trades submitted to NSCC are matched, the failure of participants to deliver securities to NSCC on settlement date, and the corresponding failure of NSCC to redeliver the securities, results in open positions. Open positions are marked-to-market daily. Such marks are debited or credited to the involved participants through the settlement process. At the close of business on December 31, 2007, open positions due to NSCC aggregated \$7,454,648,000 (\$3,749,160,000 at December 31, 2006). When a participant does not deliver securities due to NSCC on the settlement date, NSCC, in accordance with its SEC-approved rules, utilizes the Stock Borrow Program (SBP) to complete its delivery obligations to the extent that participants have made available for loan to the system shares of that issue. As of December 31, 2007, NSCC completed delivery of \$1,693,456,000 in securities through the SBP (\$1,105,727,000 at December 31, 2006), leaving \$5,761,192,000 in open delivery obligations due to participants (\$2,643,433,000 at December 31, 2006). NSCC's borrowing from the SBP does not relieve a participant's obligation to deliver the securities to NSCC. In addition, the settlement of trades is generally scheduled to occur 3 days after the trade date. As of December 31, 2007, trades totaling \$78.9 billion were scheduled to settle over the next three settlement days.

Net rental expense amounted to \$8,773,000 and \$9,759,000, in 2007 and 2006, respectively. At December 31, 2007, future minimum rental payments under all noncancelable leases are as follows:

(Dollars in thousands)	
2008	\$3,846
2009	3,441
2010	3,028
2011	2,854
2012	2,854
Total minimum rental payments	\$16,023

NSCC is involved in legal proceedings and litigation arising in the ordinary course of business. In the opinion of management, the outcome of such proceedings and litigation is not expected to have a material effect on NSCC's consolidated financial position.

## **NOTE 10 OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK**

In the normal course of business, NSCC guarantees certain obligations of its participants under specified circumstances (see Note 9). If a participant fails to fulfill its obligations, NSCC could be exposed to risk in amounts in excess of those recorded in NSCC's settlement accounts receivable and payable.

NSCC mitigates its exposure to risk by requiring participants to meet established NSCC financial standards for membership, monitoring their compliance with other financial standards established by NSCC and by requiring participants to provide clearing fund deposits in the form of cash, marketable securities, or letters of credit (see Note 3).

If a participant fails to fulfill its settlement obligations to NSCC and NSCC ceases to act on behalf of the participant, NSCC will liquidate that participant's guaranteed security receive and deliver obligations and apply that defaulting participant's clearing fund deposit to satisfy any net outstanding obligation and/or loss.

NSCC has entered into a netting contract and limited cross-guaranty agreement with DTC which includes certain arrangements and financial guarantees to ensure that securities delivered by DTC to NSCC to cover CNS allocations are fully collateralized. NSCC has also entered into a multilateral netting contract and limited cross-guaranty agreement with DTC, FICC and The Options Clearing Corporation (OCC) under which these clearing agencies have agreed to make payment to each other for any remaining unsatisfied obligations of a common defaulting participant to the extent that they have excess resources of the defaulting participant. NSCC and OCC have also entered into an agreement providing for payments to each other relating to the settlement of certain option exercises and assignments in the event of a mutual participant's failure.

In the event that a deficiency still exists after the application of the guaranty payments from the other clearing agencies, before NSCC may assess its membership, NSCC is required to apply against the deficiency at least 25% of its retained earnings or such greater amount to be determined by the Board of Directors. NSCC may then assess the balance of the deficiency in accordance with NSCC's Rules.

As discussed in Note 1, NSCC provides various services to members of the financial community who participate in securities trade comparison, clearance and settlement. As such, NSCC has a significant group concentration of credit risk since its participants may be impacted by economic conditions affecting the securities industry. As described above, such risk is mitigated in a number of ways.

## **NOTE 11 OTHER MATTERS**

In 2006, the company entered into an agreement to surrender leased office space at one of its facilities prior to the expiration of the remaining lease term. A provision of \$439,000 was recorded to reflect the net cost of surrendering the space, including the impairment in the carrying value of leasehold improvements. In 2007, there was no similar provision. Further, NSCC incurred related relocation and severance expenses totaling \$284,000 that are included in employee compensation and related benefits. In 2006, there was a similar provision of \$1,678,000.