

# **IMPORTANT NOTICE**

**National Securities Clearing Corporation**



**A#:** 7061  
**P&S#** 6632  
**Date:** September 20, 2010  
**To:** ALL PARTICIPANTS  
**Attention:** MANAGING PARTNER/OFFICER, OPERATIONS  
PARTNER/OFFICER, COMPLIANCE OFFICER  
**From:** GENERAL COUNSEL'S OFFICE  
**Subject:** RULE CHANGE – SR-NSCC-2010-10 – CLARIFICATION OF RULE  
53 (“ALTERNATIVE PRODUCTS SERVICES AND MEMBERS”)

On September 20, 2010, the National Securities Clearing Corporation (“NSCC”) submitted a rule filing with the Securities and Exchange Commission pursuant to paragraph (A) of Section 19(b)(3) of the Securities Exchange Act of 1934. The rule filing, which is effective upon filing, clarifies Rule 53 (Alternative Investment Product Services and Members”) of its Rules & Procedures (the “Rules”) that an Alternative Investment Product (“AIP”) Service prospective member is not required to designate a settling bank in order to become an AIP member.

## **AIP Service**

In 2007, NSCC filed with the Securities and Exchange Commission (“Commission”), a rule change that established the AIP Service,<sup>1</sup> a processing platform for alternative investment products such as hedge funds, fund of hedge funds, commodities pools, managed futures and real estate investment trusts (“REITs”).

The AIP Service provides for settlement of related payments (“AIP Payments”) such as subscriptions and redemptions, activity, distributions, and commissions for AIPs. The AIP Service also supports communication of information and settlement of AIP Payments between the AIP Manufacturer and the AIP Distributor to facilitate processing of subscriptions and purchases, tenders and redemptions, dividends and distributions, commissions and fees, positions reporting, product information, account maintenance, automated transmission of imaged documents and such other services as NSCC may determine from time to time. AIP Members may provide for the transmission of data in connection with transactions for which the payments are made outside of NSCC, or for settlement through NSCC at their option.

## **AIP Settlement**

Currently, Rule 53, Section 7, paragraph (h) provides that unless “otherwise permitted by the Corporation, each AIP Member shall appoint an AIP Settling Bank for the purpose of settling with the Corporation on behalf of the

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<sup>1</sup> See Securities and Exchange Act Release No. 57813 (May 12, 2008), 73 FR 28539 (May 16, 2008) (SR-NSCC-2007-12).

AIP Member pursuant to an AIP Settling Bank Agreement.” This settlement bank provision was implemented in the initial AIP Service rule filing to accommodate the stringent settlement rules implemented for the AIP Service. AIP settlement is segregated from all other NSCC settlement obligations and is settled on a gross debit/gross credit basis. In other words, AIP Service participants must fully fund their debits before receipt of their credits. In the event of a failure, NSCC does not fund the credits but rather begins the AIP reversal process. The AIP Service’s pre-funded settlement mitigates DTCC’s risk. This settling bank provision was also included in the original AIP Service filing because participants were initially required to settle all NSCC invoices with their settlement obligation.

### **Clarification of Settling Bank Provision in Rule 53**

Since the development of the AIP Service, a significant number of prospective participants view its reporting functionality (Position, Activity and Distribution) as a key first step in adoption of the AIP Service. These AIP prospects have expressly indicated their interest in becoming AIP members in order to participate in the transmission of AIP Data and not the settling functions of the AIP Service.

In response to this feedback, NSCC has developed a functionality that can designate AIP Service members as “non-settling” members that use the AIP Service for messaging only. Position, Activity-Distribution and Commission, are typically “non-settling” and strictly reporting functions. Requiring these prospective participants to supply a settling bank simply for bill payment is a hindrance to product adoption and cost prohibitive. Additionally, the current list of NSCC settling banks accepting new clients is limited and those settling banks willing to accept new settlement business have requested large monthly fees from the AIP prospects.

The AIP Service has now been appropriately configured to allow for prospects to apply for membership without designating a settling bank. If a participant is established by Account Administration on the Entity Master File (EMF) without a settling bank’s ABA number, EMF notifies the AIP Service application that the participant is non-settling. The AIP Service retains a table of the non-settling participants and validates all settlement files created by the application against the table. If the participant has erroneously indicated settlement, no file will be created or sent to settlement. The erroneous transaction will continue through normal AIP processing as non-settling.

AIP Service participants that do not intend to use its settling function will no longer be required to settle their invoices in their settlement obligations. For those participants who are designated “non-settling” members, they will be permitted to use alternative means of payment as designated from time to time by NSCC. Current methods of payment include DTCC ePayment for NSCC Invoices to settle their bills (which allows participants without a settling bank designation to authorize payment of NSCC Invoices via debit to an ACH-accessible commercial account at a US bank) or via credit card.

The full text of this rule change (SR-NSCC-2010-10) may be obtained by visiting NSCC’s website at [www.nsc.com](http://www.nsc.com). Written comments on the proposed rule filing may be addressed to Lisa T. Siebold, Assistant Secretary, National Securities Clearing Corporation, 55 Water Street, New York, New York 10041, and your comments will be forwarded to the SEC. You may also address your written comments to the Secretary of the Commission, Securities and Exchange Commission, 100 F Street, NE, Washington DC 20549-1090. We request that you provide NSCC with a copy of your comments. Questions regarding the rule filing may be directed to Jennifer Kim, Associate Counsel, The Depository Trust & Clearing Corporation, at 212-855- 3283.