

Proposed Rule Change by Fixed Income Clearing Corporation  
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial <input checked="" type="checkbox"/>	Amendment <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) <input checked="" type="checkbox"/>	Section 19(b)(3)(A) <input type="checkbox"/>	Section 19(b)(3)(B) <input type="checkbox"/>
Pilot <input type="checkbox"/>			Rule		
Extension of Time Period for Commission Action <input type="checkbox"/>			<input type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
Date Expires <input type="text"/>			<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(6)	

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>
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**Description**  
Provide a brief description of the proposed rule change (limit 250 characters).

Proposed Rule Change to amend the rules of the Mortgage-Backed Securities Division of FICC to replace the existing MBSD Participants Fund calculation methodology with a Value-at-Risk (VaR) model.

**Contact Information**  
Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name  Last Name   
 Title   
 E-mail   
 Telephone  Fax

**Signature**  
Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date   
 By  (Name)  
 Attorney-in-fact for Nikki Poulos, the FICC General Counsel  
 (Title)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

**Form 19b-4 Information**

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change**

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change.

(a) The proposed rule change is annexed hereto as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization.

a) The Credit and Market Risk Management Committee of the FICC Board of Directors approved the proposed rule filing on August 15, 2007.

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

(a) Clearing participants of the Mortgage-Backed Securities Division (“MBSD”) of FICC are required to maintain Participants Fund deposits. Each participant’s required deposit is calculated daily to ensure enough funds are available to cover the risks associated with that participant’s activities.

The purpose served by the Participants Fund is to have on deposit from each applicable participant assets sufficient to satisfy any losses that may otherwise be incurred by MBSD participants as the result of the default by the participant and the resultant close out of that participant’s settlement positions.

FICC proposes to replace the current Participants Fund methodology (which uses haircuts and offsets) with a Value-at-Risk (“VaR”) model which is expected to better reflect market volatility and more thoroughly distinguish levels of risk presented by individual securities.

Specifically, FICC is proposing to replace the existing MBSD margin calculation with a yield-driven VaR model. VaR is defined to be the maximum amount of money that may be lost on a portfolio over a given period of time, within a given level of confidence. With respect to the MBSD, FICC is proposing a 99 percent three-day VaR.

The changes to the components that comprise the current Participants Fund calculation versus the proposed VaR calculation in relation to the risks addressed by the components are summarized as follows<sup>1</sup>:

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<sup>1</sup> In addition to the following, the provision in the MBSD rules requiring participants to maintain a Basic Deposit and Minimum Market Margin Differential Deposit with the MBSD pursuant to Article IV, Rule 1, Section 1(a) and (b), will be eliminated.

<b>Existing Methodology</b>	<b>Risk Addressed</b>	<b>Proposed Methodology</b>
Market Margin Differential, which is the greater of:  (i) the P&L Requirement  or  (ii) the Market Volatility Requirement.	Adjusting contract price to market price,  and  Post mark-to-market fluctuations in security prices,	The sum of:  (i) Mark-to-market  and  (ii) Interest rate or index-driven model, as appropriate. <sup>2</sup>
Final margin requirement generated for second processing cycle. <sup>3</sup>	Additional exposure due to portfolio variation.	Margin Requirement Differential (“MRD”) includes intra-day portfolio variations and protection regarding late margin deficit satisfaction.
Prefunding of certain debit cash obligation items through the Participants Fund (no offset for credits)	Uncertainty of whether a member will satisfy its cash settlement obligation	Prefunding of certain debit cash obligation items through the Participants Fund (offset for credits) <sup>4</sup>
N/A	Potential loss in unlikely situations beyond the model’s effective range	Coverage Component (if necessary, applies additional charge to bring coverage to the applicable confidence level)
Minimum Market Margin Differential (currently, \$250,000)	Maintenance of a minimum amount of collateral to support potential counterparty liquidation losses.	A minimum charge of the greater of: (i) \$100,000, or (ii) a defined percentage of gross portfolio.

In addition, FICC may include in a participant’s Participants Fund requirement a “special charge” as determined by FICC in view of price fluctuations in or volatility or lack of liquidity of any security. FICC will make any such determination based on such factors as it determines to be appropriate from time to time.

<sup>2</sup> FICC shall have the discretion to not apply the interest rate model to classes of securities whose volatility is less amenable to statistical analysis (e.g., the security has a lack of pricing history). In lieu of such a calculation, the required charge with respect to such positions shall instead be determined based on an historic index volatility model.

<sup>3</sup> The MBSD generates a preliminary margin report as part of a first processing cycle at the close the business day, and final margin requirement as part of a second processing cycle completed at approximately 11:30 a.m. each business day. Upon the implementation of the new VaR methodology, the MBSD will no longer generate a margin requirement as part of the second cycle, but rather a final margin requirement will be established after the running of the first cycle at approximately 9:00 p.m.

<sup>4</sup> Cash obligation item credits are retained by the MBSD and not passed through to the participant. As a result, the MBSD has correspondingly less risk vis-à-vis a firm with cash obligation credits, and therefore requires less collateral in this regard.

(b) The proposed rule change is consistent with the requirements of the Securities Exchange Act of 1934, as amended (the "Act"), and the rules and regulations thereunder, because it allows FICC to more effectively manage risk relating to member trading activity. As such, it supports the safeguarding of securities and funds which are in the custody or control of FICC or for which it is responsible.

4. 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.

5. 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.

6. Extension of Time Period for Commission Action.

FICC does not consent to an extension of the time period specified in Section 19(b)(2) of the Act for Commission action.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D).

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

(d) Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission.

The proposed rule change is not based on the rules of another self-regulatory organization or the Commission.

9. Exhibits

Exhibit 1 - Notice of proposed rule change for publication in the Federal Register.

Exhibit 2 - n/a

Exhibit 3 - n/a

Exhibit 4 - n/a

Exhibit 5 - Proposed Rule Text

**EXHIBIT 1**

**SECURITIES AND EXCHANGE COMMISSION**

**(Release No. 34-\_\_\_\_\_ ; File No. SR-FICC-2007-10)**

**SELF-REGULATORY ORGANIZATIONS**

Proposed Rule Change by FIXED INCOME CLEARING CORPORATION (“FICC”) relating to amending the rules of FICC’s Mortgage-Backed Securities Division (“MBSD”) to replace the existing MBSD Clearing Fund calculation methodology with a yield-driven Value-at-Risk (“VaR”) model.

Comments requested within \_\_\_\_ days after the date of this publication.

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Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”), 15 U.S.C. 78s(b)(1), notice is hereby given that on \_\_\_\_\_, FICC filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FICC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The text of the proposed rule change is attached hereto as Exhibit 5.

**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. 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 such statements.

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

(i) Clearing participants of the Mortgage-Backed Securities Division (“MBSD”) of FICC are required to maintain Participants Fund deposits. Each participant’s required deposit is calculated daily to ensure enough funds are available to cover the risks associated with that participant’s activities.

The purpose served by the Participants Fund is to have on deposit from each applicable participant assets sufficient to satisfy any losses that may otherwise be incurred by MBSD participants as the result of the default by the participant and the resultant close out of that participant’s settlement positions.

FICC proposes to replace the current Participants Fund methodology (which uses haircuts and offsets) with a Value-at-Risk (“VaR”) model which is expected to better reflect market volatility and more thoroughly distinguish levels of risk presented by individual securities.

Specifically, FICC is proposing to replace the existing MBSD margin calculation with a yield-driven VaR model. VaR is defined to be the maximum amount of money that may be lost on a portfolio over a given period of time, within a given level of confidence. With respect to the MBSD, FICC is proposing a 99 percent three-day VaR.

The changes to the components that comprise the current Participants Fund calculation versus the proposed VaR calculation in relation to the risks addressed by the components are summarized as follows<sup>1</sup>:

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<sup>1</sup> In addition to the following, the provision in the MBSD rules requiring participants to maintain a Basic Deposit and Minimum Market Margin Differential Deposit with the MBSD pursuant to Article IV, Rule 1, Section 1(a) and (b), will be eliminated.

<b><u>Existing Methodology</u></b>	<b><u>Risk Addressed</u></b>	<b><u>Proposed Methodology</u></b>
Market Margin Differential, which is the greater of:  (i) the P&L Requirement  or  (ii) the Market Volatility Requirement.	Adjusting contract price to market price,  and  Post mark-to-market fluctuations in security prices,	The sum of:  (i) Mark-to-market  and  (ii) Interest rate or index-driven model, as appropriate. <sup>2</sup>
Final margin requirement generated for second processing cycle. <sup>3</sup>	Additional exposure due to portfolio variation.	Margin Requirement Differential (“MRD”) includes intra-day portfolio variations and protection regarding late margin deficit satisfaction.
Prefunding of certain debit cash obligation items through the Participants Fund (no offset for credits)	Uncertainty of whether a member will satisfy its cash settlement obligation	Prefunding of certain debit cash obligation items through the Participants Fund (offset for credits) <sup>4</sup>
N/A	Potential loss in unlikely situations beyond the model’s effective range	Coverage Component (if necessary, applies additional charge to bring coverage to the applicable confidence level)
Minimum Market Margin Differential (currently, \$250,000)	Maintenance of a minimum amount of collateral to support potential counterparty liquidation losses.	A minimum charge of the greater of: (i) \$100,000, or (ii) a defined percentage of gross portfolio.

In addition, FICC may include in a participant’s Participants Fund requirement a “special charge” as determined by FICC in view of price fluctuations in or volatility or

<sup>2</sup> FICC shall have the discretion to not apply the interest rate model to classes of securities whose volatility is less amenable to statistical analysis (e.g., the security has a lack of pricing history). In lieu of such a calculation, the required charge with respect to such positions shall instead be determined based on an historic index volatility model.

<sup>3</sup> The MBSD generates a preliminary margin report as part of a first processing cycle at the close the business day, and final margin requirement as part of a second processing cycle completed at approximately 11:30 a.m. each business day. Upon the implementation of the new VaR methodology, the MBSD will no longer generate a margin requirement as part of the second cycle, but rather a final margin requirement will be established after the running of the first cycle at approximately 9:00 p.m.

<sup>4</sup> Cash obligation item credits are retained by the MBSD and not passed through to the participant. As a result, the MBSD has correspondingly less risk vis-à-vis a firm with cash obligation credits, and therefore requires less collateral in this regard.

lack of liquidity of any security. FICC will make any such determination based on such factors as it determines to be appropriate from time to time.

(ii) The proposed rule change is consistent with the requirements of the Securities Exchange Act of 1934, as amended (the "Act"), and the rules and regulations thereunder, because it allows FICC to more effectively manage risk relating to member trading activity. As such, it supports the safeguarding of securities and funds which are in the custody or control of FICC or for which it is responsible.

**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 been solicited or received.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve such proposed rule change, or
- (B) institute proceedings to determine whether the proposed change should be disapproved.

**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 may be submitted by using the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>), or by sending an e-mail to [rule-comment@sec.gov](mailto:rule-comment@sec.gov). Please include File No. SR-FICC-2007-10 on the subject line.

- Paper comments should be sent in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington D.C. 20549-1090.

All submissions should refer to File Number SR-FICC-2007-10. 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 inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington D.C. 20549-9303. Copies of such filing also will be available for inspection and copying at FICC's principal office and on FICC's Web site at [www.ficc.com](http://www.ficc.com). 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 the file number above and should be submitted within \_\_\_\_\_ days after the date of publication.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.

Nancy M. Morris

EXHIBIT 5

**Underlined, boldface Text** indicates additional language

~~**Struck through, boldface text**~~ indicates deleted language

**Shaded text** indicates language that FICC has proposed to delete in a rule filing pending before the Securities and Exchange Commission.

Double underlined text indicates language that FICC has proposed to add in a rule filing pending before the Securities and Exchange Commission.

FIXED INCOME CLEARING CORPORATION  
MORTGAGE-BACKED SECURITIES DIVISION  
CLEARING RULEBOOK

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ARTICLE I DEFINITIONS AND GENERAL PROVISIONS

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Rule 1. Definitions

**End of Day Charge**

**The term “End of Day Charge” means with respect to each Participant, the calculation equaling: (i) the VaR Component; plus (ii) the Mark-to-Market Debit; minus (iii) the Mark-to-Market Credit; plus (iv) a cash obligation item debit; minus (v) a cash obligation item credit.**

Aggregated Accounts

The term "Aggregated Accounts" means a set of Accounts for the processing of transactions in the Comparison and Clearing System for which a Participant has elected pursuant to Section 2 of Rule 1 of Article II to have its Cash Settlement obligations and ~~Market Margin Differential~~ **Total Required Fund** Deposit requirements netted.

### Coverage Component

**The term “Coverage Component” means with respect to each Participant’s VaR Component, an additional charge to bring the Participant’s coverage to a targeted confidence level.**

### Long Position

The term "Long Position" means, for purposes of determining ~~Market Margin Differential~~ **Mark-to-Market**, a Participant's obligations with respect to the purchase of an Eligible Security or an Option Contract, as determined pursuant to Section 2 of Rule 2 of Article IV.

### ~~Market Margin Differential~~ Mark-to-Market

The term “~~Market Margin Differential~~ **Mark-to-Market**” means, ~~with respect to Forward Transactions, Impending Transactions, Fails, and Aged Fails in an account in the Comparison and Clearing System,~~ the aggregate amount of a Participant’s Profits and Losses calculated by the Corporation pursuant to Sections 1, ~~2 and 3~~ of Rule 2 of Article IV.

### Mark-to-Market Credit

**The term “Mark-to-Market Credit” means the amount of a Participant’s Mark-to-Market if such amount represents a profit.**

### Mark-to-Market Debit

**The term “Mark-to-Market Debit” means the amount of a Participant’s Mark-to-Market if such amount represents a loss.**

### ~~Market Margin Differential~~ Deposit

**The term “Market Margin Differential Deposit” means the amount a Participant is required to deposit to the Participants Fund pursuant to Section 2 of Rule 2 of Article IV.**

### Minimum Charge

**The term "Minimum Charge" means the minimum amount of each Participant's Total Required Fund Deposit. The amount of the Minimum Charge shall equal the greater of: (i) \$100,000, or (ii) a percentage of the Participant's gross positions as such percentage is determined by the Corporation from time to time.**

### Participants Fund

The term "Participants Fund" means the fund for which provision is made in Article IV, to which Participants are required to make ~~Basic Deposits and to which Participants are also required to make Minimum Market Margin Differential Deposits, Market Margin Differential Deposits~~ **Total Required Fund Deposits** and Cross-Guaranty Repayment Deposits.

### Short Position

The term "Short Position" means, for purposes of determining ~~Market Margin Differential~~ **Mark-to-Market**, a Participant's obligations with respect to the sale of an Eligible Security or an Option Contract, as determined pursuant to Section 2 of Rule 2 of Article IV.

### Total Required Fund Deposit

**The term "Total Required Fund Deposit" means the amount a Participant is required to deposit to the Participants Fund pursuant to Section 3 of Rule 2 of Article IV.**

### VaR Component

**The term "VaR Component" means a calculation of the volatility with respect to the unsettled positions of a Member. Such volatility calculations shall be made in accordance with any generally accepted portfolio volatility model, including, but not limited to, any margining formula employed by any other clearing agency registered under Section 17A of the Securities Exchange Act of 1934. Such calculation shall be made utilizing such assumptions and based on such historical data as the Corporation deems reasonable and shall cover such range of historical volatility as the Corporation from time to time deems appropriate.**

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ARTICLE II TRANSACTIONS PROCESSED BY THE CORPORATION

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Rule 1. Accounts

Sec. 2. Aggregation of Accounts.

A Participant having more than one Account in the Comparison and Clearing System may elect, in the manner specified in the Procedures, to have the Corporation net Cash Settlement obligations and ~~Market Margin Differential~~ **Total Required Fund** Deposit requirements for some or all of such Accounts; provided, however, no netting of Cash Settlement obligations and ~~Market Margin Differential~~ **Total Required Fund** Deposit requirements for Dealer Accounts and Broker Accounts shall be permitted. A Participant or Limited Purpose Participant having more than one Account in the Comparison Only System may also elect, in the manner specified in the Procedures, to have the Corporation net Cash Settlement obligations for some or all of such Accounts.

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Rule 4. Processing by the Corporation and Reports

Sec. 1. RTTM Processing; Availability of Reports.

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The RTTM Compare Report shall constitute the sole confirmation of transactions between Original Contra-Side Participants or Limited Purpose Participants to be processed by the Corporation. As the sole confirmation, the RTTM Compare Report shall evidence a valid, binding and enforceable contract, and the Corporation shall be entitled to rely upon the RTTM Compare Report for all purposes under these Rules. In the case of a Fully Compared or Partially Compared transaction involving a Broker, each Dealer as to which the transaction has compared shall be bound by such contract. In the case of a Partially Compared transaction involving a Broker, unless the Dealer as to which the transaction has not compared submits a DK of the transaction in accordance with these Rules, such Dealer shall be responsible for ~~Market Margin Differential~~ **Total Required Fund** Deposits with respect to such transaction and may be responsible for such transaction in accordance with Section 5(b)(ii) of Rule 3 of Article III.

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Sec. 6. Unmatched Margin Report.

If trade input with respect to a transaction in Eligible Securities involving a Broker has not compared or has Partially Compared, the Dealer(s) for which trade input has not compared will be furnished an Unmatched Margin Report. The Dealer may then either affirm the transaction or submit a DK of the transaction as described in Sections 1 and 4 of this Rule 4. Unless and until each Dealer receiving the Unmatched Margin Report submits a DK of such transaction in accordance with the Procedures, ~~Market Margin Differential~~ **Mark-to-Market** shall be payable by the Dealer with respect to such transaction pursuant to

Section 4 of Rule 2 of Article IV, the same as if such transaction had been listed in such Dealer's Open Commitment Report.

Rule 7. Reporting of Clearance; Expiration or Exercise of Option Contracts

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Sec. 2. Comparison of Cleared SBO Trades.

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- (b) If the Corporation receives a Notification of Settlement from both the delivering and the receiving Participants but the information submitted by the Participants does not compare within dollar tolerances determined by the Corporation pursuant to the Procedures or compares only in part, or if only one Participant submits a Notification of Settlement, the Corporation shall so indicate in each Participant's Transaction Summary Report. Until such time as the Participant submitting incorrect information submits a correction, or, if only one Participant submitted a Notification of Settlement, the information is deleted by that Participant or the other Participant submits a Notification of Settlement with information that compares, the SBO Trade (or portion thereof with respect to which information does not compare) will continue to be reflected on each Participant's Open Commitment Report and will remain subject to ~~Market Margin Differential~~ **Total Required Fund** Deposit requirements as computed pursuant to Sections 1, 2 and 3 of Rule 2 of Article IV.

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Sec. 3. Settlement of Trade-for-Trade Transactions.

- (b) If the Corporation receives a Notification of Settlement and/or a cancellation from both parties to a Trade-for-Trade transaction but the information submitted by the Participants does not compare or compares only in part, or if only one Participant submits a Notification of Settlement and/or a cancellation, the Corporation shall so indicate in each Participant's Transaction Summary Report. Until such time as Notifications of Settlement and/or cancellations compare as to the entire principal amount of the Trade-for-Trade transaction, the outstanding portion of such transaction will continue to be reflected on each Participant's Open Commitment Report and will remain subject to ~~Market Margin Differential~~ **Total Required Fund** Deposit requirements as computed pursuant to Sections 1, 2 and 3 of Rule 2 of Article IV.

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Sec. 5. Expiration or Exercise of Option Contracts.

On the expiration or exercise date of any Option Contract as reported to the Corporation pursuant to Section 2 of Rule 3 of this Article II, both the selling and the purchasing

Participants shall submit a cancellation of the Option Contract to the Corporation and, in the case of exercise, unless both parties to the Option Contract otherwise agree, submit trade input with respect to the purchase or sale of the Eligible Securities subject to such Option Contract in accordance with the provisions of Section 2 of Rule 3 of this Article II. Until both Participants submit a cancellation, the Corporation shall continue to show the Option Contract on the Participants' Open Commitment Reports and shall continue to require ~~Market Margin Differential~~ Total Required Fund Deposits with respect thereto as provided in Section 4 of Rule 2 of Article IV.

#### ARTICLE IV PARTICIPANTS FUND

##### ~~Rule 1. Minimum Deposits to Participants Fund~~

##### ~~Sec. 1. Establishment.~~

~~Each Participant shall be required to make a minimum deposit to the Participants Fund for each Account maintained for it by the Corporation. The minimum deposit shall consist of the following:~~

~~————— (a) for all Participants, except investment companies registered with the Securities and Exchange Commission pursuant to the Investment Company Act of 1940, a Basic Deposit in a fixed amount set forth in the Procedures; and~~

~~————— (b) for each Participant participating in the Comparison and Clearing System, a Minimum Market Margin Differential Deposit for each Account or set of Aggregated Accounts in that System in such amount as the Corporation from time to time may determine.~~

~~The Minimum Market Differential Deposit shall not be used to offset or otherwise reduce a Participant's required Market Margin Differential Deposit, as determined and payable pursuant to Sections 2 and 3 of Rule 2 of this Article IV.~~

##### ~~Sec. 2. Increases.~~

~~The Board of Directors may increase the amount of either the Basic Deposit or the Minimum Market Margin Differential Deposit and exempt any Broker Account from the Minimum Market Margin Differential Deposit requirement.~~

~~————— If either the Basic Deposit or the Minimum Market Margin Differential Deposit is increased by the Corporation, such increase shall not become effective until each affected Participant is notified of such increase and afforded an opportunity to give written notice to the Corporation of its election to withdraw as a Participant as provided in Rule 2 of Article III. If a Participant does not give such written notice before the time specified in the notice to it of the increase in the Basic~~

~~Deposit or the Minimum Market Margin Differential Deposit at the time when the same becomes effective, it shall deposit to the Participants Fund the amount of the increase.~~

~~Sec. 3. ———— Decreases.~~

~~If either the Basic Deposit or the Minimum Market Margin Differential Deposit to the Participants Fund after having been fixed by the Corporation and paid in by a Participant is thereafter decreased by the Corporation, the difference will be paid by the Corporation to the Participant upon its request as soon as all of its Cash Settlement obligations have been discharged and, in the case of a Participant, all transactions in the Comparison and Clearing System open at the time of such decrease from which losses and payments chargeable to the Participants Fund might result have been closed.~~

~~Rule 2. 1.      **Daily Market Margin Differential Deposits to Participants Fund Total Required Fund Deposit**~~

~~Sec. 1.            **Mark-to-Market --** Computation of Profit or Loss.~~

~~Each Business Day, the Corporation shall separately compute Profit or Loss for each transaction in each Account maintained by a Participant in the Comparison and Clearing System **as follows: and (a) in the case of Forward Transactions and Fails, the net Profit or net Loss for all transactions in each Class or CUSIP number in the Account or, (b) in the case of Aged Fails, aggregate Losses in each Class or CUSIP number in the Account.**~~

(a) A transaction shall be deemed to have produced a Profit if:

(i) the Participant has a Long Position in a transaction involving the purchase of an Eligible Security in which the Current Market Value exceeds the original contract value;

(ii) the Participant has a Short Position in any transaction involving the sale of an Eligible Security in which the original contract value exceeds the Current Market Value;

(iii) the Participant has a Long Position in an unexpired Call Option Contract for an Eligible Security in which the Current Market Value of the Eligible Security exceeds the Strike Price; and

(iv) the Participant has a Long Position in any unexpired Put Option Contract for an Eligible Security in which the Strike Price exceeds the Current Market Value of the Eligible Security.

(b) A transaction shall be deemed to have produced a Loss if:

(i) the Participant has a Long Position in a transaction involving the purchase of an Eligible Security in which the original contract value exceeds Current Market Value;

(ii) the Participant has a Short Position in any transaction involving the sale of an Eligible Security in which the Current Market Value exceeds the original contract value;

(iii) the Participant has a Short Position in any unexpired Call Option Contract for an Eligible Security in which the Current Market Value of the Eligible Security exceeds the Strike Price; and

(iv) the Participant has a Short Position in an Option Contract for an Eligible Security subject to an unexpired Put Option Contract in which the Strike Price exceeds the Current Market Value of the Eligible Security.

The amount of Profit or Loss computed for each transaction pursuant to this Section 1 shall be reported in the Participant's daily Open Commitment Report.

Sec. 2. Long Positions and Short Positions.

For purposes of Section 1 of this Rule 2, Participants' Long Positions and Short Positions shall be determined as follows:

(a) In the case of a transaction between Dealers not involving a Broker:

(i) The Dealer listed on an Open Commitment Report as the purchaser of an Eligible Security or the purchaser of an Option Contract shall be deemed to have a Long Position; and

(ii) The Dealer listed on an Open Commitment Report as the seller of an Eligible Security or the seller (writer) of an Option Contract shall be deemed to have a Short Position.

(b) In the case of a transaction involving a Broker:

(i) If the transaction is Fully Compared:

(A) the Dealer listed on its Open Commitment Report as the purchaser of an Eligible Security or the purchaser of an Option Contract shall be deemed to have a Long Position;

(B) the Dealer listed on its Open Commitment Report as the seller of a Eligible Security or the seller (writer) of an Option Contract shall be deemed to have a Short Position; and

(C) the Broker shall be deemed to have neither a Long Position nor a Short Position.

(ii) If the transaction has not compared:

(A) If both Dealers have submitted a DK of the transaction as reflected on their respective Unmatched Margin Reports, neither of the Dealers nor the Broker shall be deemed to have a Long Position or a Short Position and the transaction shall cease to be reflected on the records of the Corporation.

(B) If both Dealers have not submitted a DK of the transaction as reflected on their respective Unmatched Margin Reports:

(1) the Dealer reported on its Unmatched Margin Report to have been named by the Broker as the purchaser of an Eligible Security or the purchaser of an Option Contract shall be deemed, until such time as the Dealer submits a DK of the transaction, to have a Long Position for purposes of computing Loss, but not Profit, pursuant to Section 1 of this Rule 2;

(2) the Dealer reported on its Unmatched Margin Report to have been named by the Broker as the seller of an Eligible Security or the seller (writer) of an Option Contract shall be deemed, until such time as the Dealer submits a DK of the transaction, to have a Short position for purposes of computing Loss, but not Profit, pursuant to Section 1 of this Rule 2; and

(3) the Broker shall be deemed to have neither a Long Position nor a Short Position.

(iii) If the transaction is Partially Compared:

(A) The Dealer with respect to which the transaction has compared shall be deemed:

(1) to have a Long Position in any Eligible Security or Option Contract of which it is listed in its Open Commitment Report to be the purchaser; and

(2) to have a Short Position in any Eligible Security or Option Contract of which it is listed in its Open Commitment report to be the Seller;

(B) If the Dealer with respect to which the transaction has not compared has not submitted a DK of the transaction as reflected on its Unmatched Margin Report:

(1) the Dealer shall be deemed to have a Long Position or a Short Position determined in the manner described in subparagraph (b)(ii)(B) above with respect to uncomparing transactions; and

(2) the Broker shall be deemed to have neither a Long Position nor a Short Position.

(C) If the Dealer with respect to which the transaction has not compared has submitted a DK of the transaction as reflected on its Unmatched Margin Report:

(1) such Dealer shall be deemed to have neither a Long Position nor a Short Position; and

(2) the Broker shall be deemed to have a Short Position or Long Position corresponding to the Long Position or Short Position of the Dealer with respect to which the transaction has compared.

~~Sec. 3. Determination of Market Margin Differential.~~

~~Market Margin Differential shall be determined as follows:~~

~~(a) Market Margin Differential for Forward Transactions in an Account shall be the sum of net Profits and net Losses computed pursuant to Section 1 of this Rule 2 for such Forward Transactions in all Classes or CUSIP numbers in the Account (i.e., net Profits for Forward Transactions in any Class or CUSIP number in the Account shall offset net Losses for Forward Transactions in any other Class or CUSIP number in the Account).~~

~~(b) Market Margin Differential for Impending Transactions in an Account shall be the sum of net Profits and net Losses computed pursuant to Section 1 of this Rule 2 for such Impending Transactions in Classes or CUSIP numbers in the Account (i.e., net Profits for Impending Transactions in any Class or CUSIP number in the Account shall offset net Losses computed for Impending Transactions in any other Class or CUSIP number in the Account).~~

~~(c) The Market Margin Differential for Fails in the Account shall be the sum of net Losses (but not net Profits) computed pursuant to Section 1 of this Rule 2 for all Classes or CUSIP numbers in the Account (i.e., net Profits computed for Fails in any Class or CUSIP number in the Account shall not be used to offset net Losses computed for Fails in any other Class or CUSIP number in the Account).~~

~~(d) Market Margin Differential for Aged Fails in all Classes or CUSIP numbers in the Account shall equal aggregate Losses computed pursuant to Section 1 of this Rule 2 (i.e., no Profits shall be taken into account either for a particular Class or CUSIP number or for all Classes or CUSIP numbers in the Account).~~

Sec. 4 3. Market Margin Differential Deposits Total Required Fund Deposit.

Each Business Day, each Participant shall be required to make a **Market Margin Differential Total Required Fund** Deposit to the Participants Fund for each of its Accounts or sets of Aggregated Accounts in the Comparison and Clearing System equal to **the greater of: (i) the Minimum Charge, or (ii) the End of Day Charge<sup>\*</sup>; plus the difference sum** of the following:

~~(a) 130% (or such other percentage as the Corporation from time to time may determine) of the greater of: (i) Market Margin Differential, if any, for Forward Transactions, Impending Transactions, Fails and Aged Fails in the Account or set of Aggregated Accounts or (ii) 25 basis points (or such other number of basis points as the Corporation from time to time may determine) of Net Position and 25 basis points (or such other number of basis points as the Corporation from time to time may determine) of largest outstanding Net-Out Position minus Excess Profits from Forward Transactions;~~

(a) the Coverage Component;

plus

(b) An additional payment (“special charge”) from such Participant as determined by the Corporation from time to time in view of market conditions and other financial and operational capabilities of the Participant. The Corporation shall make any such determination based on such factors as the Corporation determines to be appropriate from time to time.

\* The Corporation shall have the discretion to exclude from the Participant’s VaR Component unsettled positions in classes of securities whose volatility is less amenable to statistical analysis. In lieu of the VaR Component, the margin required with respect to such classes of securities shall instead be determined based on an historic index volatility model.

**plus**

**(c) a margin requirement differential which considers intra-day portfolio variations and potential for a late margin deficit satisfaction;**

~~(b) 100% (or such other percentage as the Corporation from time to time may determine) of the amount of any projected negative Cash Adjustments or SBO Market Differential to be included in the Participant's Cash Settlement obligation with respect to the Account or set of Aggregated Accounts; minus~~

~~(e) the amount of any other Market Margin Differential Deposits which the Participant has previously made to, and which remain in, the Participants Fund with respect to such Account or set of Aggregated Accounts.~~

The ~~Market Margin Differential~~ **Total Required Fund** Deposit required for each of a Participant's Accounts or sets of Aggregated Accounts shall be reported daily, and payment shall be due that day by the time specified in the Procedures; however, such payment shall not be due on a given day if: (a) the difference between the amount of a Participant's required ~~Market Margin Differential~~ **Total Required Fund** Deposit as reported on that day and the amount then on deposit towards satisfaction of that Participant's ~~Market Margin Differential~~ **Total Required Fund** Deposit is equal to or less than the lesser of: (i) \$250,000, or (ii) 25 percent of the amount currently on deposit towards satisfaction of that Participant's required ~~Market Margin Differential~~ **Total Required Fund** Deposit; and (b) the Participant is not on the Watch List .

**The Corporation shall have the right to adjust any components of the calculation of a Participant's Total Required Fund Deposit as set forth in this Section 3.**

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Sec. ~~5.~~ **4**      Excess Deposits.

In the event that a Participant's open commitments in any Account or set of Aggregated Accounts in the Comparison and Clearing System require a ~~Market Margin Differential~~ **Total Required Fund** Deposit to the Participants Fund for such Account or set of Aggregated Accounts in an amount less than ~~Market Margin Differential~~ **Total Required Fund** Deposits previously made by the Participant to, and remaining in, the Participants Fund with respect to such Account or set of Aggregated Accounts, the Participant shall be entitled, upon request to the Corporation made in the manner

specified in the Procedures, to the release of such excess or the unused portion of such excess, as the case may be, or to application of such excess to any other Account or set of Aggregated Accounts maintained for the Participant. Nothing herein shall be construed as permitting a Participant to reduce the amount of its Minimum ~~Market Margin Differential Deposit to the Participants Fund~~ Charge with respect to any of its Accounts or sets of Aggregated Accounts ~~below the amount required to be maintained pursuant to Rule 1 of this Article IV~~ or reduce the amount of its Cross-Guaranty Repayment Deposit to the Participants Fund below the amount required to be maintained pursuant to Section 4 of Rule 4 of Article III.

Sec. ~~6.~~ 5. Form of Deposits.

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Sec. ~~7.~~ 6. Special Provisions Relating to Deposits of Cash.

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Sec. ~~8.~~ 7. Special Provisions Relating to Deposits of Eligible Participants Fund Securities.

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Rule ~~3~~ 2. Failure to Discharge Liability

If any Participant fails to discharge any liability to the Corporation, the amount of its deposits to the Participants Fund, and any cash received in respect of such deposits and not yet distributed to the Participant, for the Account or set of Aggregated Accounts to which the liability relates or any other Account or set of Aggregated Accounts, or so much thereof as is necessary, shall forthwith be applied toward the discharge of such liability. To the extent necessary, the Corporation may draw against any letters of credit and liquidate any securities deposited by a Participant in the Participants Fund for the Account or set of Aggregated Accounts to which the liability relates or any other Account or set of Aggregated Accounts. Each Participant shall immediately make good the deficiency in the amount of its minimum required deposits and, in the case of a Participant, ~~Market Margin Differential~~ Total Required Fund Deposits to the Participants Fund resulting from application of its deposits as provided in this Rule 3.

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Rule ~~4~~ 3. Restoration of Participant Fund Deficits; Recoveries

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Rule 5 4. Ceasing to Be a Participant or to Maintain an Account or Set of Aggregated Accounts

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Rule **6.5.**

Watch List

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