

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * <input type="text" value="22"/>	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4	File No.* SR - <input type="text" value="2017"/> - * <input type="text" value="009"/>	Amendment No. (req. for Amendments *) <input type="text"/>
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Filing by National Securities 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 type="checkbox"/>	Section 19(b)(3)(A) * <input checked="" type="checkbox"/>	Section 19(b)(3)(B) * <input type="checkbox"/>
			Rule		
Pilot <input type="checkbox"/>	Extension of Time Period for Commission Action * <input type="checkbox"/>	Date Expires * <input type="text"/>	<input checked="" type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
			<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)	

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010	Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934
Section 806(e)(1) * <input type="checkbox"/>	Section 806(e)(2) * <input type="checkbox"/>
Section 3C(b)(2) * <input type="checkbox"/>	

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 action (limit 250 characters, required when Initial is checked \*).

To further describe and codify existing practices relating to the Bond Haircut.

**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 action.

First Name * <input type="text" value="Jacqueline"/>	Last Name * <input type="text" value="Chezar"/>
Title * <input type="text" value="Executive Director and Associate General Counsel"/>	
E-mail * <input type="text" value="jfarinella@dtcc.com"/>	
Telephone * <input type="text" value="(212) 855-3216"/>	Fax <input type="text"/>

**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.

(Title \*)

Date <input type="text" value="06/23/2017"/>	<input type="text" value="Managing Director and Deputy General Counsel"/>
By <input type="text" value="Nikki Poulos"/>	<input type="text" value="npoulos@dtcc.com"/>

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 EFFF 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 \***

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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 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

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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, security-based swap submission, or advance notice 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**

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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**

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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 of National Securities Clearing Corporation (“NSCC”) is attached hereto as Exhibit 5 and would (1) provide additional transparency in NSCC’s Rules & Procedures (“Rules”)<sup>1</sup> with respect to the existing methodology for calculating margin on Members’ Net Unsettled Positions and Net Balance Order Unsettled Positions (for purposes of this filing, referred to collectively herein as “Net Unsettled Positions”) in corporate and municipal bonds (“Bond Haircut”), which are excluded from the parametric volatility component of the margin calculation (“VaR Charge”); and (2) codify NSCC’s existing practice of applying the Bond Haircut to all corporate and municipal bonds without discretion, as described below.

(b) Not applicable.

(c) Not applicable.

## **2. Procedures of the Self-Regulatory Organization**

The proposed rule change was approved by the Risk Committee of NSCC’s Board of Directors on December 20, 2016.

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

(a) Purpose

### ***Proposal Overview***

The proposed rule change would provide additional transparency in the Rules with respect to the calculation and the application of the Bond Haircut. NSCC currently excludes Net Unsettled Positions in corporate and municipal bonds from its parametric VaR calculation and instead charges a Bond Haircut, which is calculated by multiplying the absolute value of the Net Unsettled Positions in each security by a percentage that is no less than two percent.

NSCC is proposing to enhance the description of the Bond Haircut in Procedure XV to provide more detail regarding the determination of the applied percentage, and to codify NSCC’s existing practice of applying the Bond Haircut to all corporate and municipal bonds without discretion.

### ***The Required Deposit and the Bond Haircut***

A primary objective of NSCC’s Clearing Fund is to have on deposit from each applicable Member assets sufficient to satisfy losses that may otherwise be incurred by NSCC as the result of the default of the Member and the resultant close out of that Member’s unsettled positions

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<sup>1</sup> Terms not defined herein are defined in the Rules, available at [www.dtcc.com/~media/Files/Downloads/legal/rules/nsccl\\_rules.pdf](http://www.dtcc.com/~media/Files/Downloads/legal/rules/nsccl_rules.pdf).

under NSCC's trade guaranty. Each Member's Clearing Fund required deposit is calculated daily pursuant to a formula set forth in Procedure XV of the Rules designed to provide sufficient funds to cover this risk of loss. The Clearing Fund formula accounts for a variety of risk factors through the application of a number of charges, each described in Procedure XV.

The VaR Charge is a core component of this formula and is designed to calculate the amount of money that may be lost on a portfolio over a given period of time assumed necessary to liquidate the portfolio, within a given level of confidence. Pursuant to Procedure XV, NSCC may currently exclude from this calculation Net Unsettled Positions in classes of securities whose volatility is amenable to generally accepted statistical analysis only in a complex manner, including corporate and municipal bonds.

NSCC believes the Bond Haircut is a more appropriate measure of the risk presented to NSCC by its Members' positions in corporate and municipal bonds than the VaR Charge because the volatility of these securities is generally amenable to statistical analysis only in a complex manner. Because NSCC believes the Bond Haircut is more effective in capturing the risks presented by corporate and municipal bonds, in addition to adding more detail to Procedure XV regarding the calculation of the Bond Haircut, NSCC is also proposing to codify its existing practice by removing reference to discretion in application of the Bond Haircut to these securities.

*a. Corporate Bonds*

In order to calculate the Bond Haircut for positions in corporate bonds, NSCC first categorizes corporate bonds into security groups according to the bonds' remaining time to maturity and credit rating. NSCC then aligns each security group against a Merrill Lynch bond index.<sup>2</sup> Each bond index is chosen to provide a valuation proxy for computing the appropriate margin for securities categorized into that group. NSCC calculates a haircut rate applicable to each security group based on historical returns of the aligned Merrill Lynch bond index in the specified look-back period and a predetermined calibration percentile. NSCC is proposing to clarify in Procedure XV that the look-back period shall be no shorter than 10 years. Currently,

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<sup>2</sup> Bond indices are widely used to measure the risk of particular classes of corporate bonds. By aligning each security group to a Merrill Lynch bond index, NSCC is able to use widely accepted historical pricing information as a valuation proxy for each security group to correlate with the actual risk coverage for the particular attributes of the bonds. Using these reliable pricing proxies permits NSCC to conduct loss estimation associated with clearing these securities in a less complex statistical manner, while achieving the desired coverage target.

the look-back period is from 1995 to present day.<sup>3</sup> The haircut rate for each security group is recalculated periodically, based on a predetermined frequency. While NSCC is proposing to clarify in Procedure XV that such recalculation shall occur at least annually, currently the recalculation is performed on a daily basis.<sup>4</sup>

Further, NSCC determines the appropriate specified look-back period and predetermined calibration percentile, which shall not be less than 99 percent, in order to account for the particularized risk characteristics of corporate bonds, including market, liquidity and idiosyncratic risk (i.e., the volatility of a particular issue compared to the volatility of the index).

*b. Municipal Bonds*

The Bond Haircut for positions in municipal bonds is calculated at the CUSIP level. In order to account for price and valuation volatility, NSCC has set a tenor-based haircut schedule that applies according to the remaining time to maturity for separate categories of municipal bonds. Currently, NSCC applies this schedule to six separate categories of municipal bonds. For municipal bonds rated BBB+ or lower and for non-rated bonds, an additional factor is applied based on the applicable municipal sector. If a municipal bond is not mapped to any particular sector, the highest numerical municipal factor is applied to positions in that bond. NSCC reviews and re-assigns, as necessary, the risk factors assigned to each municipal sector no less frequently than annually.

This additional factor is added to lower rated municipal bonds because variable risk factors exist between municipal sectors. In addition to the risk associated with time-to-maturity, municipal bonds may also pose credit risk depending upon the bonds' assigned credit rating. The added sector-based factor, applicable to lower-rated municipal bonds, is designed to compensate for this additional credit risk. Therefore, NSCC believes the Bond Haircut as applied to municipal bonds is also an appropriate measure for the risk presented by these positions.

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<sup>3</sup> NSCC regularly reviews whether its margining methodology is achieving the desired risk mitigation objectives. In connection with such review, NSCC has determined to make technical enhancements to the calculation of the Bond Haircut as applied to positions in corporate bonds, including an adjustment to this look-back period. Such enhancements shall be proposed pursuant to a separate advance notice filing, to be filed pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010. 12 U.S.C. 5465(e)(1).

<sup>4</sup> NSCC has also determined that the frequency of re-calibration of the haircut rates should be adjusted, and will propose to change this frequency pursuant to an advance notice filing. *Id.*

### ***Proposed Changes to Procedure XV***

In order to make the proposed changes, NSCC would exclude Net Unsettled Positions in corporate and municipal bonds from Procedure XV, Sections I.(A)(1)(a)(ii) and (2)(a)(ii). These Sections of Procedure XV would continue to provide NSCC with discretion to exclude certain securities, as described therein and other than corporate and municipal bonds, from its VaR margin calculation and instead apply a haircut-based margin charge. NSCC would add new Sections I.(A)(1)(a)(iii) and (2)(a)(iii) to Procedure XV to include more transparency around the determination of the Bond Haircut and to make clear that the Bond Haircut shall apply to all Net Unsettled Positions in corporate and municipal bonds, in lieu of a VaR Charge, and would not be subject to NSCC's discretion.

#### **(b) Statutory Basis**

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934 ("Act"), requires, in part, that the Rules promote the prompt and accurate clearance and settlement of securities transactions.<sup>5</sup> The proposed rule change with respect to the Bond Haircut would provide additional transparency in the Rules regarding the calculation and application of the Bond Haircut, and would codify NSCC's practice to apply the Bond Haircut to all positions in corporate and municipal bonds without discretion. The proposed changes would ensure that the Rules remain transparent, accurate and clear, which would enable all stakeholders to readily understand their rights and obligations in connection with NSCC's clearance and settlement of securities transactions. Therefore, NSCC believes that the proposed rule changes would promote the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.<sup>6</sup>

Rule 17Ad-22(e)(23)(i) under the Act requires, in part, that NSCC establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for publicly disclosing all relevant rules and material procedures.<sup>7</sup> Rule 17Ad-22(e)(23)(ii) under the Act requires, in part, that NSCC establish, implement, maintain and enforce written policies and procedures reasonably designed to provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in NSCC.<sup>8</sup> The proposed rule change enhances the transparency in the Rules regarding the calculation and application of the Bond Haircut and codifies NSCC's practice to apply the Bond Haircut to all positions in corporate and municipal bonds without discretion. In this way, the proposed rule change provides for the public disclosure, through the new Procedure XV, Sections I (A)(1)(a)(iii) and (2)(a)(iii) of the Rules, of the rules and procedures through which

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<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>6</sup> Id.

<sup>7</sup> 17 CFR 240.17Ad-22(e)(23)(i).

<sup>8</sup> 17 CFR 240.17Ad-22(e)(23)(ii).

NSCC calculates and applies the Bond Haircut. The proposed rule change would allow NSCC to further provide its participants with sufficient information regarding the Bond Haircut to enable those participants to identify and evaluate the risks and material costs associated with the calculation and application of the Bond Haircut, which are incurred through their participation in NSCC. As such, NSCC believes the proposed rule change is consistent with Rule 17Ad-22(e)(23)(i) and (ii) under the Act.<sup>9</sup>

#### **4. Self-Regulatory Organization's Statement on Burden on Competition**

NSCC does not believe that the proposed rule change would impact competition.<sup>10</sup> The proposed rule change would increase transparency of the Rules by codifying NSCC's current practice with respect to the assessment and imposition of the Bond Haircut. As such, NSCC believes that the proposed rule change would not impact Members or have any impact on competition.

#### **5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

NSCC has not received any written comments relating to this proposal. NSCC will notify the Commission of any written comments it receives.

#### **6. Extension of Time Period for Commission Action**

NSCC 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)**

(a) The proposed rule change is to take effect pursuant to paragraph A of Section 19(b)(3) of the Act.<sup>11</sup>

(b) The proposed rule change constitutes a stated policy, practice or interpretation with respect to the meaning of an existing rule.<sup>12</sup>

(c) Not applicable.

(d) Not applicable.

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<sup>9</sup> 17 CFR 240.17Ad-22(e)(23)(i), (ii).

<sup>10</sup> 15 U.S.C. 78q-1(b)(3)(I).

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>12</sup> 17 CFR 240.19b-4(f)(1).

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

Not applicable.

**9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act**

Not applicable.

**10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing, and Settlement Supervision Act**

Not applicable.

**11. Exhibits**

Exhibit 1 – Not applicable.

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

Exhibit 2 – Not applicable.

Exhibit 3 – Not applicable.

Exhibit 4 – Not applicable.

Exhibit 5 – Proposed changes to the Rules.



**EXHIBIT 1A**

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-[\_\_\_\_\_]; File No. SR-NSCC-2017-009)

[DATE]

Self-Regulatory Organizations; National Securities Clearing Corporation; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Further Describe and Codify Existing Practices Relating to the Bond Haircut

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) <sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June \_\_, 2017, National Securities Clearing Corporation (“NSCC”) 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 the clearing agency. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

The proposed rule change consists of amendments to NSCC’s Rules & Procedures (“Rules”)<sup>3</sup> in order to (1) provide additional transparency in the Rules with respect to the existing methodology for calculating margin on Members’ Net Unsettled Positions and Net Balance Order Unsettled Positions (for purposes of this filing, referred to collectively herein as “Net Unsettled Positions”) in corporate and municipal bonds (“Bond Haircut”), which are excluded from the parametric volatility component of the

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Terms not defined herein are defined in the Rules, available at [www.dtcc.com/~media/Files/Downloads/legal/rules/nsc\\_rules.pdf](http://www.dtcc.com/~media/Files/Downloads/legal/rules/nsc_rules.pdf).

margin calculation (“VaR Charge”); and (2) codify NSCC’s existing practice of applying the Bond Haircut to all corporate and municipal bonds without discretion, as described below.

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

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

(A) Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

***Proposal Overview***

The proposed rule change would provide additional transparency in the Rules with respect to the calculation and the application of the Bond Haircut. NSCC currently excludes Net Unsettled Positions in corporate and municipal bonds from its parametric VaR calculation and instead charges a Bond Haircut, which is calculated by multiplying the absolute value of the Net Unsettled Positions in each security by a percentage that is no less than two percent.

NSCC is proposing to enhance the description of the Bond Haircut in Procedure XV to provide more detail regarding the determination of the applied percentage, and to codify NSCC’s existing practice of applying the Bond Haircut to all corporate and municipal bonds without discretion.

***The Required Deposit and the Bond Haircut***

A primary objective of NSCC's Clearing Fund is to have on deposit from each applicable Member assets sufficient to satisfy losses that may otherwise be incurred by NSCC as the result of the default of the Member and the resultant close out of that Member's unsettled positions under NSCC's trade guaranty. Each Member's Clearing Fund required deposit is calculated daily pursuant to a formula set forth in Procedure XV of the Rules designed to provide sufficient funds to cover this risk of loss. The Clearing Fund formula accounts for a variety of risk factors through the application of a number of charges, each described in Procedure XV.

The VaR Charge is a core component of this formula and is designed to calculate the amount of money that may be lost on a portfolio over a given period of time assumed necessary to liquidate the portfolio, within a given level of confidence. Pursuant to Procedure XV, NSCC may currently exclude from this calculation Net Unsettled Positions in classes of securities whose volatility is amenable to generally accepted statistical analysis only in a complex manner, including corporate and municipal bonds.

NSCC believes the Bond Haircut is a more appropriate measure of the risk presented to NSCC by its Members' positions in corporate and municipal bonds than the VaR Charge because the volatility of these securities is generally amenable to statistical analysis only in a complex manner. Because NSCC believes the Bond Haircut is more effective in capturing the risks presented by corporate and municipal bonds, in addition to adding more detail to Procedure XV regarding the calculation of the Bond Haircut, NSCC is also proposing to codify its existing practice by removing reference to discretion in application of the Bond Haircut to these securities.

*a. Corporate Bonds*

In order to calculate the Bond Haircut for positions in corporate bonds, NSCC first categorizes corporate bonds into security groups according to the bonds' remaining time to maturity and credit rating. NSCC then aligns each security group against a Merrill Lynch bond index.<sup>4</sup> Each bond index is chosen to provide a valuation proxy for computing the appropriate margin for securities categorized into that group. NSCC calculates a haircut rate applicable to each security group based on historical returns of the aligned Merrill Lynch bond index in the specified look-back period and a predetermined calibration percentile. NSCC is proposing to clarify in Procedure XV that the look-back period shall be no shorter than 10 years. Currently, the look-back period is from 1995 to present day.<sup>5</sup> The haircut rate for each security group is recalculated periodically, based on a predetermined frequency. While NSCC is proposing to clarify in

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<sup>4</sup> Bond indices are widely used to measure the risk of particular classes of corporate bonds. By aligning each security group to a Merrill Lynch bond index, NSCC is able to use widely accepted historical pricing information as a valuation proxy for each security group to correlate with the actual risk coverage for the particular attributes of the bonds. Using these reliable pricing proxies permits NSCC to conduct loss estimation associated with clearing these securities in a less complex statistical manner, while achieving the desired coverage target.

<sup>5</sup> NSCC regularly reviews whether its margining methodology is achieving the desired risk mitigation objectives. In connection with such review, NSCC has determined to make technical enhancements to the calculation of the Bond Haircut as applied to positions in corporate bonds, including an adjustment to this look-back period. Such enhancements shall be proposed pursuant to a separate advance notice filing, to be filed pursuant to Section 806(e)(1) of the Payment, Clearing, and Settlement Supervision Act of 2010. 12 U.S.C. 5465(e)(1).

Procedure XV that such recalculation shall occur at least annually, currently the recalculation is performed on a daily basis.<sup>6</sup>

Further, NSCC determines the appropriate specified look-back period and predetermined calibration percentile, which shall not be less than 99 percent, in order to account for the particularized risk characteristics of corporate bonds, including market, liquidity and idiosyncratic risk (i.e., the volatility of a particular issue compared to the volatility of the index).

*b. Municipal Bonds*

The Bond Haircut for positions in municipal bonds is calculated at the CUSIP level. In order to account for price and valuation volatility, NSCC has set a tenor-based haircut schedule that applies according to the remaining time to maturity for separate categories of municipal bonds. Currently, NSCC applies this schedule to six separate categories of municipal bonds. For municipal bonds rated BBB+ or lower and for non-rated bonds, an additional factor is applied based on the applicable municipal sector. If a municipal bond is not mapped to any particular sector, the highest numerical municipal factor is applied to positions in that bond. NSCC reviews and re-assigns, as necessary, the risk factors assigned to each municipal sector no less frequently than annually.

This additional factor is added to lower rated municipal bonds because variable risk factors exist between municipal sectors. In addition to the risk associated with time-to-maturity, municipal bonds may also pose credit risk depending upon the bonds' assigned credit rating. The added sector-based factor, applicable to lower-rated

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<sup>6</sup> NSCC has also determined that the frequency of re-calibration of the haircut rates should be adjusted, and will propose to change this frequency pursuant to an advance notice filing. *Id.*

municipal bonds, is designed to compensate for this additional credit risk. Therefore, NSCC believes the Bond Haircut as applied to municipal bonds is also an appropriate measure for the risk presented by these positions.

### ***Proposed Changes to Procedure XV***

In order to make the proposed changes, NSCC would exclude Net Unsettled Positions in corporate and municipal bonds from Procedure XV, Sections I.(A)(1)(a)(ii) and (2)(a)(ii). These Sections of Procedure XV would continue to provide NSCC with discretion to exclude certain securities, as described therein and other than corporate and municipal bonds, from its VaR margin calculation and instead apply a haircut-based margin charge. NSCC would add new Sections I.(A)(1)(a)(iii) and (2)(a)(iii) to Procedure XV to include more transparency around the determination of the Bond Haircut and to make clear that the Bond Haircut shall apply to all Net Unsettled Positions in corporate and municipal bonds, in lieu of a VaR Charge, and would not be subject to NSCC's discretion.

#### **2. Statutory Basis**

Section 17A(b)(3)(F) of the Act, requires, in part, that the Rules promote the prompt and accurate clearance and settlement of securities transactions.<sup>7</sup> The proposed rule change with respect to the Bond Haircut would provide additional transparency in the Rules regarding the calculation and application of the Bond Haircut, and would codify NSCC's practice to apply the Bond Haircut to all positions in corporate and municipal bonds without discretion. The proposed changes would ensure that the Rules remain transparent, accurate and clear, which would enable all stakeholders to readily

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<sup>7</sup> 15 U.S.C. 78q-1(b)(3)(F).

understand their rights and obligations in connection with NSCC's clearance and settlement of securities transactions. Therefore, NSCC believes that the proposed rule changes would promote the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.<sup>8</sup>

Rule 17Ad-22(e)(23)(i) under the Act requires, in part, that NSCC establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for publicly disclosing all relevant rules and material procedures.<sup>9</sup> Rule 17Ad-22(e)(23)(ii) under the Act requires, in part, that NSCC establish, implement, maintain and enforce written policies and procedures reasonably designed to provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in NSCC.<sup>10</sup> The proposed rule change enhances the transparency in the Rules regarding the calculation and application of the Bond Haircut and codifies NSCC's practice to apply the Bond Haircut to all positions in corporate and municipal bonds without discretion. In this way, the proposed rule change provides for the public disclosure, through the new Procedure XV, Sections I.(A)(1)(a)(iii) and (2)(a)(iii) of the Rules, of the rules and procedures through which NSCC calculates and applies the Bond Haircut. The proposed rule change would allow NSCC to further provide its participants with sufficient information regarding the Bond Haircut to enable those participants to identify and evaluate the risks and material costs associated with the calculation and application of the Bond Haircut, which are incurred

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<sup>8</sup> Id.

<sup>9</sup> 17 CFR 240.17Ad-22(e)(23)(i).

<sup>10</sup> 17 CFR 240.17Ad-22(e)(23)(ii).

through their participation in NSCC. As such, NSCC believes the proposed rule change is consistent with Rule 17Ad-22(e)(23)(i) and (ii) under the Act.<sup>11</sup>

(B) Clearing Agency's Statement on Burden on Competition

NSCC does not believe that the proposed rule change would impact competition.<sup>12</sup> The proposed rule change would increase transparency of the Rules by codifying NSCC's current practice with respect to the assessment and imposition of the Bond Haircut. As such, NSCC believes that the proposed rule change would not impact Members or have any impact on competition.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

NSCC has not received any written comments relating to this proposal. NSCC will notify the Commission of any written comments it receives .

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act and paragraph (f) of Rule 19b-4 thereunder. At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

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<sup>11</sup> 17 CFR 240.17Ad-22(e)(23)(i), (ii).

<sup>12</sup> 15 U.S.C. 78q-1(b)(3)(I).



IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NSCC-2017-009 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number SR-NSCC-2017-009. 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 website (<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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m.

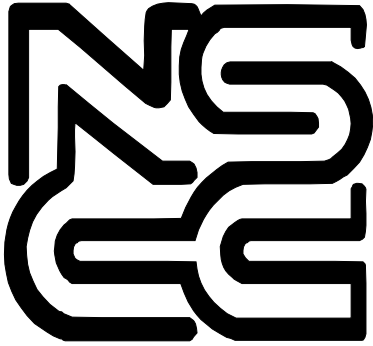
and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of NSCC and on DTCC's website (<http://dtcc.com/legal/sec-rule-filings.aspx>). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NSCC-2017-009 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).



NATIONAL  
SECURITIES  
CLEARING  
CORPORATION

RULES & PROCEDURES

TEXT OF PROPOSED RULE CHANGE

**Bold and underlined text** indicates proposed added language

**~~Bold and strikethrough text~~** indicates proposed deleted language

## PROCEDURE XV. CLEARING FUND FORMULA AND OTHER MATTERS<sup>1</sup>

### I.(A) Clearing Fund Formula for Members

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#### (1) For CNS Transactions

(a)(i) The volatility of such Member's net of unsettled Regular Way, When-Issued and When-Distributed pending positions (i.e., net positions that have not yet passed Settlement Date) and fail positions (i.e., net positions that did not settle on Settlement Date), hereinafter collectively referred to as Net Unsettled Positions. Such calculation 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, provided, however, that not less than two standard deviations' volatility shall be calculated under any model chosen. 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.

(ii) The Corporation shall have the discretion to exclude from the **above** calculations **in subsection (i) above** Net Unsettled Positions in classes of securities whose volatility is (x) less amenable to statistical analysis, such as OTC Bulletin Board or Pink Sheet issues or issues trading below a designated dollar threshold (e.g., five dollars), or (y) amenable to generally accepted statistical analysis only in a complex manner, **such as other than municipal ~~or~~ and corporate bonds.** The amount of Clearing Fund with respect to such Net Unsettled Positions shall be determined by multiplying the absolute value of such positions by a percentage designated by the Corporation, which percentage shall be not less than 10% in respect of the positions covered by subsection x of this paragraph and shall be not less than 2% in respect of the positions covered by subsection y of this paragraph; **The Corporation shall exclude from the calculations in subsection (i) above municipal and corporate bonds, which are addressed in subsection (iii) below.**

**(iii) The Corporation shall exclude from the calculations in subsection (i) above Net Unsettled Positions in corporate and municipal bonds. The amount of Clearing Fund required with respect to Net Unsettled Positions in corporate and municipal bonds shall be determined by multiplying the absolute value of such positions by a percentage designated by the Corporation, which shall be not less than 2%, calculated as follows:**

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<sup>1</sup> All calculations shall be performed daily or, if the Corporation deems it appropriate, on a more frequent basis.

**(A) Corporate bonds shall be categorized into groups according to the bonds' "remaining time to maturity" and credit rating. From time to time, but not less frequently than annually, the Corporation shall establish for each category of corporate bonds a percentage calculated using historical market price volatility of a benchmark index. Such percentage shall be based on (1) the historical returns of the applicable benchmark index; (2) a pre-determined look-back period, which shall not be shorter than 10 years; and (3) a pre-determined calibration percentile, which shall not be less than 99%.**

**(B) Municipal bonds shall be grouped by "remaining time to maturity" and separately categorized by municipal sector. The Corporation shall establish a percentage applicable to each "remaining time to maturity" grouping. From time to time, but not less frequently than annually, the Corporation shall assign each municipal sector a risk factor. If a municipal bond is rated lower than a pre-determined threshold, which shall be no lower than BBB+, or is non-rated, then the Corporation shall apply a risk factor to the applicable percentage. Such risk factor shall be based on the sector index's spread to a benchmark index. The highest sector-based risk factor shall apply to municipal bonds that are not mapped to a municipal sector.**

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**(2) For Balance Order Transactions**

(a)(i) The volatility of such Member's net of unsettled Regular Way, When-Issued and When-Distributed positions that have not yet passed Settlement Date, hereinafter collectively referred to as Net Balance Order Unsettled Positions. Such calculation 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, provided, however, that not less than two standard deviations' volatility shall be calculated under any model chosen. 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.

(ii) The Corporation shall have the discretion to exclude from the **above** calculations **in subsection (i) above** Net Balance Order Unsettled Positions in classes of securities whose volatility is (x) less amenable to statistical analysis, such as OTC Bulletin Board or Pink Sheet issues or issues trading below a designated dollar threshold (e.g., five dollars), or (y) amenable to generally accepted statistical analysis only in a complex manner, **such as other than** municipal **or and** corporate bonds. The amount of Clearing Fund required with respect to such Net Balance Order Unsettled Positions shall be determined

by multiplying the absolute value of such positions by a percentage designated by the Corporation, which percentage shall be not less than 10% in respect of the positions covered by subsection x of this paragraph and shall be not less than 2% in respect of the positions covered by subsection y of this paragraph; The Corporation shall exclude from the calculations in subsection (i) above municipal and corporate bonds, which are addressed in subsection (iii) below.

(iii) The Corporation shall exclude from the calculations in subsection (i) above Net Balance Order Unsettled Positions in corporate and municipal bonds. The amount of Clearing Fund required with respect to Net Balance Order Unsettled Positions in corporate and municipal bonds shall be determined by multiplying the absolute value of such positions by a percentage designated by the Corporation, which shall be not less than 2%, calculated as follows:

(A) Corporate bonds shall be categorized into groups according to the bonds' "remaining time to maturity" and credit rating. From time to time, but not less frequently than annually, the Corporation shall establish for each category of corporate bonds a percentage calculated using historical market price volatility of a benchmark index. Such percentage shall be based on (1) the historical returns of the applicable benchmark index; (2) a pre-determined look-back period, which shall not be shorter than 10 years; and (3) a pre-determined calibration percentile, which shall not be less than 99%.

(B) Municipal bonds shall be grouped by "remaining time to maturity" and separately categorized by municipal sector. The Corporation shall establish a percentage applicable to each "remaining time to maturity" grouping. From time to time, but not less frequently than annually, the Corporation shall assign each municipal sector a risk factor. If a municipal bond is rated lower than a pre-determined threshold, which shall be no lower than BBB+, or is non-rated, then the Corporation shall apply a risk factor to the applicable percentage. Such risk factor shall be based on the sector index's spread to a benchmark index. The highest sector-based risk factor shall apply to municipal bonds that are not mapped to a municipal sector.

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