

Required fields are shown with yellow backgrounds and asterisks.

Filing 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"/>	Extension of Time Period for Commission Action * <input type="checkbox"/>	Date Expires * <input type="text"/>	Rule <input 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 \*).  
 Proposed rule change to expand the types of entities that are eligible to participate in FICC as Sponsored Members.

**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 \* Rosa      Last Name \* Chang  
 Title \* Executive Director and Associate General Counsel  
 E-mail \* rchang1@dtcc.com  
 Telephone \* (212) 855-4985      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.  
 (Title \*)  
 Date 03/01/2017      Managing Director and Deputy General Counsel  
 By Nikki Poulos        
 (Name \*)  
 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.  
 Persona Not Validated - 1459960765550,

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

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

**Form 19b-4 Information \***

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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 Proposed Rule Change

(a) The proposed rule change of Fixed Income Clearing Corporation (“FICC”) is annexed hereto as Exhibit 5 and consists of proposed modifications to the Government Securities Division (“GSD”) Rulebook (“Rules”)<sup>1</sup> that would (i) expand the types of entities that are eligible to participate in FICC as Sponsored Members under Rule 3A (Sponsoring Members and Sponsored Members) and (ii) make the following other amendments and clarifications to the Rules:

- Clarify that the “Sponsoring Member Omnibus Account” definition in Rule 1 (Definitions) refers to an “Account” as defined in Rule 1;
  - Amend Section 7 of Rule 3A to reference the application of fails charges to a Sponsoring Member Omnibus Account and to correct certain typographical errors;
  - Amend Section 9 of Rule 3A to correct an out-of-date cross-reference to Rule 13 (Funds-Only Settlement);
  - Amend Section 10 of Rule 3A to reflect the current Clearing Fund calculation procedures applicable to a Sponsoring Member Omnibus Account and to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation);
  - Amend Section 12 of Rule 3A to reflect the current loss allocation process applicable to Sponsored Member Trades in the event that the Sponsoring Member is insolvent or otherwise in default to FICC and to correct certain out-of-date cross-references to Rule 4 and certain typographical errors;
  - Amend Sections 13 and 14 of Rule 3A to correct certain out-of-date cross-references to Rule 21 (Restrictions on Access to Services); and
  - Amend Section 15 of Rule 3A to specify the standard with respect to which a Sponsoring Member is deemed by FICC to have knowledge that one of its Sponsored Members is insolvent or is otherwise unable to perform on any of its material contracts, obligations or agreements for purposes of the Sponsoring Member’s obligation to inform FICC of such matter.
- (b) Not applicable.
- (c) Not applicable.

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<sup>1</sup> Capitalized terms not defined herein are defined in the Rules, [available at http://www.dtcc.com/legal/rules-and-procedures](http://www.dtcc.com/legal/rules-and-procedures).

## 2. Procedures of the Self-Regulatory Organization

The proposed rule changes to expand the types of entities that may participate in FICC as Sponsored Members were approved by the Risk Committee of FICC's Board of Directors ("Board") and the Board's Business, Technology and Operations Committee on August 16, 2016. The remaining proposed rule changes were approved by FICC management on December 22, 2016 pursuant to delegated authority from the Board.

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

### (a) Purpose

The proposed rule change would expand the types of entities that are eligible to participate in FICC as Sponsored Members under Rule 3A (Sponsoring Members and Sponsored Members).

This filing also contains proposed rule changes that are not related to the proposed expansion of entity types eligible to be Sponsored Members but would provide specificity, clarity and additional transparency to the Rules.

### (i) *Background on the Proposed Expansion of Sponsored Member Eligibility*

In 2005, the Commission approved FICC rule filing SR-FICC-2004-22,<sup>2</sup> which established a Sponsoring Member-Sponsored Member relationship in the Rules. Under Rule 3A (Sponsoring Members and Sponsored Members), Bank Netting Members that are well-capitalized (as defined under applicable regulations) and have at least \$5 billion in equity capital are permitted to sponsor certain institutional firms (Sponsored Members) into GSD membership.

Under Rule 3A, a Sponsoring Member is permitted to submit to FICC for comparison, novation and netting certain types of eligible transactions between itself and its Sponsored Members (Sponsored Member Trades).<sup>3</sup> The Sponsoring Member is required to establish an omnibus account at FICC for all of its Sponsored Members' FICC-cleared activity (Sponsoring Member Omnibus Account),<sup>4</sup> which is separate from the Sponsoring Member's regular netting account. For operational and administrative purposes, FICC interacts solely with the Sponsoring

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<sup>2</sup> Securities Exchange Act Release No. 51896 (June 21, 2005), 70 FR 36981 (June 27, 2005) (SR-FICC-2004-22).

<sup>3</sup> See Rule 1, definition of "Sponsored Member Trades." Rules, supra note 1.

<sup>4</sup> See Rule 1, definition of "Sponsoring Member Omnibus Account." Id.

Member as agent for purposes of the day-to-day satisfaction of its Sponsored Members' obligations to FICC, including their securities and funds-only settlement obligations.<sup>5</sup>

Novation of eligible trading activity to FICC provides Sponsoring Members and their Sponsored Members the benefits of FICC's independent risk management and guaranty of completion of settlement of such trading activity. In addition, Sponsoring Members also may be able to offset on their balance sheets their obligations to FICC on Sponsored Member Trades against their obligations to FICC on other eligible FICC-cleared activity, as well as take lesser capital charges than would be required to the extent they engaged in the same trading activity with their Sponsored Members outside of a central counterparty.<sup>6</sup> By potentially alleviating balance sheet and capital constraints on their Sponsoring Members, participation in FICC as Sponsored Members may afford eligible institutional firms increased lending capacity and income.

Currently, eligibility to become a Sponsored Member is limited to an entity that is a registered Investment Company under the Investment Company Act of 1940,<sup>7</sup> is a "qualified institutional buyer" as defined in Rule 144A<sup>8</sup> under the Securities Act of 1933,<sup>9</sup> and has at least one Sponsoring Member willing to sponsor the entity into GSD membership.<sup>10</sup>

The proposed rule change would eliminate the requirement that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940. Nevertheless, in order to ensure that Sponsored Members are financially sophisticated, FICC would retain the current requirement that a Sponsored Member be a "qualified institutional buyer" to the extent that its legal entity type falls under one of the enumerated categories of Rule 144A's definition of a "qualified institutional buyer." For institutional firms whose entity types do not clearly fall into one of the enumerated categories in Rule 144A's definition of "qualified institutional

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<sup>5</sup> See Rule 3A, Sections 5, 6, 7, 8 and 9. Id.

<sup>6</sup> Sponsoring Members interested in such relief should discuss this matter with their accounting and regulatory capital experts.

<sup>7</sup> 15 U.S.C. 80a-1 *et seq.*

The Sponsoring Member-Sponsored Member relationship has historically been based on a custodial banking arrangement in which the Sponsored Member Trades novated to FICC reflect investments by the Sponsoring Member of a registered Investment Company Sponsored Member's cash through Repo Transactions. However, a custodial banking relationship between a Sponsored Member and its Sponsoring Member(s) is not required under the Rules.

<sup>8</sup> See 17 CFR 230.144A.

<sup>9</sup> 15 U.S.C. 77a *et seq.*

<sup>10</sup> Currently, GSD has one Sponsoring Member and 1422 Sponsored Members.

buyer,” FICC would instead require such Sponsored Members to meet the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A (e.g., a corporation) must satisfy in order to be a “qualified institutional buyer” (other than requirements relating to entity type or organizational form). Under this alternative requirement, institutional firms whose entity types are not expressly included within the definition of “qualified institutional buyer” in Rule 144A (such as non-U.S. sovereign wealth funds) would be eligible to be Sponsored Members, provided they satisfy the financial thresholds that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A (e.g., a corporation) must meet in order to be a “qualified institutional buyer.” Because conceptions of financial sophistication may change with time, FICC believes it is appropriate to tie this requirement to the definition of “qualified institutional buyer” in Rule 144A, as such definition may be amended from time to time.

FICC believes that expanding eligibility to become a Sponsored Member beyond registered Investment Companies under the Investment Company Act of 1940 is appropriate because FICC’s risk management of the Sponsoring Member-Sponsored Member relationship occurs primarily at the Sponsoring Member level,<sup>11</sup> and the proposed expansion of the entity types eligible to participate in FICC as Sponsored Members (and the commensurate potential volume increase in novated activity) would not require any changes to FICC’s risk management practices applicable to Sponsoring Members or to FICC’s operational practices applicable to the comparison, novation, netting and settlement of Sponsored Member Trades.

FICC also believes that the proposed expansion of entity types eligible to participate in FICC as Sponsored Members would help to safeguard the U.S. financial market by lowering the risk of liquidity drain, protecting against fire sale risk,<sup>12</sup> and decreasing settlement and operational risk.

Expanding the types of institutional firms that are eligible to participate in FICC as Sponsored Members and thereby benefit from FICC’s guaranty of completion of settlement of their eligible transactions would mitigate the risk of a large scale exit by such firms from the

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<sup>11</sup> For example, a Sponsoring Member is responsible under Section 10 of Rule 3A for posting to FICC the Required Fund Deposit for its Sponsoring Member Omnibus Account, which includes the sum of the stand-alone VaR Charges for each of its Sponsored Members’ novated activity calculated separately. In addition, while Sponsored Members are principally liable to FICC for their settlement obligations, a Sponsoring Member is also required under Section 2 of Rule 3A to provide a guaranty to FICC for such obligations. This means that in the event one or more Sponsored Members does not satisfy its settlement obligations, FICC is able to invoke the guaranty provided by the Sponsoring Member.

<sup>12</sup> Fire sale risk is the risk of rapid asset sales of securities held by cash lenders when a dealer defaults. This rapid sale has the potential to create a market crisis because cash lenders are likely to sell large amounts of securities in a short period of time, which could dramatically reduce the price of such securities that such lenders are looking to sell.

U.S. financial market in a stress scenario and therefore lower the risk of a liquidity drain in such a scenario. Specifically, to the extent institutional firms would otherwise be engaging in the same type of eligible trading activity (e.g., repurchase agreement transactions) outside of a central counterparty, having such activity novated to FICC and subject to FICC's guaranty of completion of settlement would reduce the risk that such institutional firms discontinue such trading activity in a Netting Member default situation.

Similarly, broadening the pool of entities eligible for central clearing at FICC as Sponsored Members would also reduce the potential for market disruption from fire sales. Specifically, in a Netting Member default situation, the more institutional firms participate in FICC as Sponsored Members, the more trading activity with the defaulted Netting Member could be centrally liquidated in an orderly manner by FICC rather than by individual counterparties in potential fire sale conditions.

Moreover, to the extent institutional firms would otherwise be engaging in eligible trading activity (e.g., repurchase agreement transactions) outside of a central counterparty, expanding the pool of entities eligible to participate in FICC as Sponsored Members would also decrease settlement and operational risk in the U.S. financial market in that such trading activity would now be eligible to be netted and subject to guaranteed settlement, novation and independent risk management through FICC.

(ii) **Detailed Description of the Proposed Rule Changes Related to the Expansion of Sponsored Member Eligibility**

**A. Proposed Changes to Rule 3A, Sections 2(d) and 3(a)**

Sections 2(d) and 3(a) of Rule 3A currently require that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940 and also be a "qualified institutional buyer" as defined in Rule 144A under the Securities Act of 1933.

FICC is proposing to amend Sections 2(d) and 3(a) of Rule 3A to eliminate the requirement that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940.

FICC is also proposing to amend Sections 2(d) and 3(a) of Rule 3A to permit institutional firms whose entity types are not expressly included within Rule 144A to be Sponsored Members, provided they meet the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of "qualified institutional buyer" in Rule 144A (e.g., a corporation) must satisfy in order to be a "qualified institutional buyer" (other than requirements relating to entity type or organizational form).

It should be noted that it is currently and, in connection with the proposed expansion of entity types eligible to participate in FICC as Sponsored Members, would continue to be the responsibility of each Sponsored Member and its Sponsoring Member(s) to evaluate whether entering into a given Sponsored Member Trade is consistent with a Sponsored Member's legal and regulatory requirements, and that FICC has no responsibility or liability in the event that a Sponsoring Member submits data to FICC for a Sponsored Member Trade that is inconsistent with those requirements.

***B. Proposed Changes to Rule 3A, Sections 3(c) and 4***

To account for the fact that, as proposed, non-U.S. entities that meet the proposed requirements would be permitted to be Sponsored Members, FICC is proposing to amend Section 3(c) of Rule 3A to provide that Sponsored Members that are FFI Members<sup>13</sup> would be required to be FATCA Compliant and to amend Section 4 of Rule 3A to provide that Sponsored Members and their Sponsoring Members would be required to comply with global sanctions laws.<sup>14</sup>

***(iii) Other Proposed Rule Changes***

This filing also contains proposed rule changes that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members. These proposed rule changes would provide specificity, clarity and additional transparency to the Rules as described below.

***A. Proposed Changes to Rule 1 (Definitions)***

FICC is proposing to clarify that the “Sponsoring Member Omnibus Account” definition in Rule 1 (Definitions) refers to an “Account” as defined in Rule 1.

***B. Proposed Changes to Rule 3A, Section 7***

FICC is proposing to amend Section 7 of Rule 3A to reference the application of fails charges<sup>15</sup> to a Sponsoring Member Omnibus Account in the same manner as such charges are applied to Netting Members pursuant to Rule 11 (Netting System) and to correct certain typographical errors.

With respect to the application of fails charges, in 2009, FICC received Commission approval of a rule filing to impose fails charges on Netting Members, which was an action that

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<sup>13</sup> Pursuant to Rule 1, the term “FFI Member” means “any Person that is treated as a non-U.S. entity for U.S. federal income tax purposes.” For the avoidance of doubt, the term FFI Member also includes “any Member that is a U.S. branch of an entity that is treated as a non-U.S. entity for U.S. federal income tax purposes.” Rules, supra note 1.

<sup>14</sup> Although GSD has Members, including certain Bank Netting Members, which are non-U.S. entities, currently, there are no Sponsoring Members that are non-U.S. entities.

Any future Sponsoring Member or Sponsored Member that is an FFI Member will be subject to the same FATCA Compliance screening and global sanctions screening as any other Member that is a non-U.S. entity.

<sup>15</sup> The term “fails charge” refers to the charge imposed by FICC on Netting Members for a delivery failure in Treasury Securities or debentures issued by Fannie Mae, Freddie Mac or the Federal Home Loan Banks, pursuant to Section 14 of Rule 11. Rules, supra note 1.



had been requested of GSD by the Treasury Markets Practices Group (“TMPG”)<sup>16</sup> in order to encourage market participants to resolve fails promptly.<sup>17</sup> The approved rule changes were included in Section 14 of Rule 11 (Netting System) and were stated to apply to Netting Members. As an account of a Netting Member (acting as a Sponsoring Member), FICC has imposed fails charges, if applicable, on Sponsoring Members for their Sponsoring Member Omnibus Accounts since the implementation of the charges in 2009. In reviewing the Rules in connection with this present filing, FICC believes that the application of the fails charges to a Sponsoring Member’s Sponsoring Member Omnibus Account should be made clear in Rule 3A for transparency.

***C. Proposed Changes to Rule 3A, Section 9***

FICC is proposing to amend Section 9 of Rule 3A to correct an out-of-date cross-reference to Rule 13 (Funds-Only Settlement).

***D. Proposed Changes to Rule 3A, Section 10***

FICC is proposing to amend Section 10 of Rule 3A to reflect the current Clearing Fund calculation procedures applicable to a Sponsoring Member’s Sponsoring Member Omnibus Account. Specifically, FICC is proposing to amend Section 10 of Rule 3A to specify that a Sponsoring Member’s Sponsoring Member Omnibus Account Required Fund Deposit would be equal to the sum of the following: (I) the sum of the VaR Charges for all of the Sponsored Members whose activity is represented in the Sponsoring Member Omnibus Account as derived pursuant to Section 1b(a)(i) of Rule 4 (Clearing Fund and Loss Allocation), and (II) all amounts derived pursuant to the provisions of Rule 4 other than pursuant to Section 1b(a)(i) of Rule 4 computed at the level of the Sponsoring Member Omnibus Account. The proposed rule changes maintain the substance of the calculation of the Required Fund Deposit for a Sponsoring Member’s Sponsoring Member Omnibus Account (i.e., the main charges applicable to the individual Sponsored Members in the account are summed and then certain components are applied at the level of the Sponsoring Member Omnibus Account) but update the rules provisions to reflect the current Clearing Fund calculation terminology and delete references to terms that are no longer used in the Rules (such as “Clearing Fund components related to Fail Net Settlement Positions and Funds-Only Settlement amounts”).

FICC is also proposing to amend Section 10 of Rule 3A to specify that for purposes of calculating the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account, FICC would apply the higher of the Required Fund Deposit calculation as of the beginning of the current Business Day and intraday on the current Business Day.

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<sup>16</sup> The TMPG is a group of market participants that is active in the Treasury securities market and is sponsored by The Federal Reserve Bank of New York.

<sup>17</sup> Securities Exchange Act Release No. 59802 (April 20, 2009), 74 FR 19248 (April 28, 2009) (SR-FICC-2009-03).

In 2011, FICC received Commission approval to re-calculate each Business Day, at times established by FICC for this purpose, the amount of the VaR Charge applicable to each Margin Portfolio of a Member, based upon the open, intraday positions of such Margin Portfolio, for purposes of establishing whether a Member would be required to make payment of an additional amount (the Member's "Intraday Supplemental Fund Deposit") to its Required Fund Deposit.<sup>18</sup> The approved rule changes were included in Section 2a of Rule 4 (Clearing Fund and Loss Allocation). Prior to this approval, Clearing Fund requirements (including with respect to a Sponsoring Member's Sponsoring Member Omnibus Account) were calculated once each Business Day. Since the approval of these rule changes in 2011, FICC has calculated the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account based on the higher of the Required Fund Deposit calculation as of the beginning of the current Business Day and intraday on the current Business Day. In reviewing the Rules in connection with this present filing, FICC believes that this calculation procedure for the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account should be made clear in Rule 3A for transparency.

FICC is also proposing to amend Section 10 of Rule 3A to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation).

***E. Proposed Changes to Rule 3A, Section 12***

FICC is proposing to amend Section 12 of Rule 3A to reflect the current loss allocation process applicable to Sponsored Member Trades in the event that the Sponsoring Member is insolvent or otherwise in default to FICC. Specifically, FICC is proposing to amend Section 12 of Rule 3A to specify that any Remaining Loss incurred by FICC would be allocated to the Tier One Netting Members in accordance with the principles set forth in Section 7(d) of Rule 4 (Clearing Fund and Loss Allocation).

In 2011, FICC received Commission approval for its current loss allocation process set forth in Rule 4, which provides for loss mutualization of any Remaining Loss among all Tier One Netting Members.<sup>19</sup> FICC proposes to update references in Section 12 of Rule 3A to reference the current loss allocation process for Tier One Netting Members.

FICC also proposes to amend Section 12 of Rule 3A to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation) and to correct certain typographical errors.

***F. Proposed Changes to Rule 3A, Sections 13 and 14***

FICC is proposing to amend Sections 13 and 14 of Rule 3A to correct certain out-of-date cross-references to Rule 21 (Restrictions on Access to Services).

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<sup>18</sup> Securities Exchange Act Release No. 63986 (February 28, 2011), 76 FR 12144 (March 4, 2011) (SR-FICC-2010-09).

<sup>19</sup> Id.

**G. Proposed Changes to Rule 3A, Section 15**

FICC is proposing to amend Section 15 of Rule 3A to specify the standard with respect to which a Sponsoring Member is deemed by FICC to have knowledge that one of its Sponsored Members is insolvent or is otherwise unable to perform on any of its material contracts, obligations or agreements for purposes of the Sponsoring Member's obligation to inform FICC of such matter. Specifically, FICC is proposing to specify that if one or more duly authorized representatives of a Sponsoring Member, in its capacity as such, has knowledge that one of its Sponsored Members is insolvent or otherwise unable to perform on any of its material contracts, obligations or agreements, that such knowledge triggers the Sponsoring Member's obligation to inform FICC of such matter.

(b) Statutory Basis

Section 17A(b)(3)(F) of the Securities Exchange Act of 1934, as amended ("Act") requires, in part, that the Rules be designed to (i) "promote the prompt and accurate clearance and settlement of securities transactions,"<sup>20</sup> and (ii) "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest."<sup>21</sup>

By expanding the types of entities that may participate in FICC as Sponsored Members, FICC believes that the proposed rule change would help to safeguard the U.S. financial market by lowering the risk of liquidity drain (through FICC's guaranty of completion of settlement for a greater number of eligible transactions), protecting against fire sale risk (through FICC's ability to centralize and control the liquidation of a greater portion of a failed counterparty's portfolio) and decreasing settlement and operational risk (by making a greater number of transactions eligible to be netted and subject to guaranteed settlement, novation and independent risk management through FICC). By lowering the risk of liquidity drain in the U.S. financial market and protecting against fire sale risk, FICC believes the proposed rule change would "protect investors and the public interest" consistent with the requirements of the Act, cited above. By decreasing settlement and operational risk, FICC believes the proposed rule change would also "promote the prompt and accurate clearance and settlement of securities transactions" and "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions" consistent with the requirements of the Act, cited above.

By providing specificity, clarity, and additional transparency to the Rules, the proposed rule changes to Rule 1 (Definitions) and Rule 3A (Sponsoring Members and Sponsored Members) that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members would provide Members with a better understanding of the Rules, making errors in the performance of their responsibilities to FICC less likely to occur and thereby ensuring that

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<sup>20</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>21</sup> Id.

FICC's clearing and settlement system works efficiently. Therefore, FICC believes the proposed rule change would "promote the prompt and accurate clearance and settlement of securities transactions" by FICC and also "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions" consistent with the requirements of the Act, cited above.

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

FICC believes that the proposed rule changes associated with the expansion of entity types eligible to be Sponsored Members would promote competition by increasing the types of entities that may participate in FICC as Sponsored Members and therefore permit more market participants to utilize FICC's services.

At the same time, participation in FICC as a Sponsored Member would continue to be limited to legal entities that are either "qualified institutional buyers" as defined in Rule 144A under the Securities Act of 1933, or that otherwise satisfy the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of "qualified institutional buyer" in Rule 144A (e.g., a corporation) must satisfy in order to be a "qualified institutional buyer" (other than requirements relating to entity type or organizational form), and that have at least one Sponsoring Member willing to sponsor them into GSD membership. These limitations may impact institutional firms that are unable to satisfy such eligibility requirements by excluding them from being able to novate their eligible activity to FICC (and avail themselves of the commensurate benefits described in *Section 3(a)(i) – Background on the Proposed Expansion of Sponsored Member Eligibility* above). Nevertheless, FICC believes that any resulting burden on competition would be necessary and appropriate in furtherance of the Act, as permitted by Section 17A(b)(3)(I) of the Act,<sup>22</sup> in light of the fact that such eligibility requirements are designed to allow FICC to ensure the financial sophistication of Sponsored Members and to prudently manage the risk associated with Sponsored Members' participation in FICC. Moreover, FICC would not restrict the ability of institutional firms to enter into eligible transactions with Netting Members (including Sponsoring Members) outside of GSD.

FICC believes that the proposed changes to Rule 1 (Definitions) and Rule 3A (Sponsoring Members and Sponsored Members) that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members would not have an impact, nor impose any burden, on competition because each of such proposed changes would simply provide specificity, clarity and additional transparency within the Rules.

#### **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 been solicited or received. FICC will notify the Commission of any written comments received by FICC.

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<sup>22</sup> 15 U.S.C. 78q-1(b)(3)(I).

**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)**

- (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. 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-FICC-2017-003)

[DATE]

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change to Expand the Types of Entities That Are Eligible to Participate in Fixed Income Clearing Corporation as Sponsored Members and Make Other Changes

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 March 1, 2017, Fixed Income Clearing Corporation (“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 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 the Government Securities Division (“GSD”) Rulebook (“Rules”)<sup>3</sup> that would (i) expand the types of entities that are eligible to participate in FICC as Sponsored Members under Rule 3A (Sponsoring Members and Sponsored Members) and (ii) make the following other amendments and clarifications to the Rules:

- Clarify that the “Sponsoring Member Omnibus Account” definition in Rule 1 (Definitions) refers to an “Account” as defined in Rule 1;

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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> Capitalized terms not defined herein are defined in the Rules, available at <http://www.dtcc.com/legal/rules-and-procedures>.

- Amend Section 7 of Rule 3A to reference the application of fails charges to a Sponsoring Member Omnibus Account and to correct certain typographical errors;
- Amend Section 9 of Rule 3A to correct an out-of-date cross-reference to Rule 13 (Funds-Only Settlement);
- Amend Section 10 of Rule 3A to reflect the current Clearing Fund calculation procedures applicable to a Sponsoring Member Omnibus Account and to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation);
- Amend Section 12 of Rule 3A to reflect the current loss allocation process applicable to Sponsored Member Trades in the event that the Sponsoring Member is insolvent or otherwise in default to FICC and to correct certain out-of-date cross-references to Rule 4 and certain typographical errors;
- Amend Sections 13 and 14 of Rule 3A to correct certain out-of-date cross-references to Rule 21 (Restrictions on Access to Services); and
- Amend Section 15 of Rule 3A to specify the standard with respect to which a Sponsoring Member is deemed by FICC to have knowledge that one of its Sponsored Members is insolvent or is otherwise unable to perform on any of its material contracts, obligations or agreements for purposes of the Sponsoring Member's obligation to inform FICC of such matter.

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

The proposed rule change would expand the types of entities that are eligible to participate in FICC as Sponsored Members under Rule 3A (Sponsoring Members and Sponsored Members).

This filing also contains proposed rule changes that are not related to the proposed expansion of entity types eligible to be Sponsored Members but would provide specificity, clarity and additional transparency to the Rules.

(i) *Background on the Proposed Expansion of Sponsored Member Eligibility*

In 2005, the Commission approved FICC rule filing SR-FICC-2004-22,<sup>4</sup> which established a Sponsoring Member-Sponsored Member relationship in the Rules. Under Rule 3A (Sponsoring Members and Sponsored Members), Bank Netting Members that are well-capitalized (as defined under applicable regulations) and have at least \$5 billion in equity capital are permitted to sponsor certain institutional firms (Sponsored Members) into GSD membership.

Under Rule 3A, a Sponsoring Member is permitted to submit to FICC for comparison, novation and netting certain types of eligible transactions between itself and

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<sup>4</sup> Securities Exchange Act Release No. 51896 (June 21, 2005), 70 FR 36981 (June 27, 2005) (SR-FICC-2004-22).



its Sponsored Members (Sponsored Member Trades).<sup>5</sup> The Sponsoring Member is required to establish an omnibus account at FICC for all of its Sponsored Members' FICC-cleared activity (Sponsoring Member Omnibus Account),<sup>6</sup> which is separate from the Sponsoring Member's regular netting account. For operational and administrative purposes, FICC interacts solely with the Sponsoring Member as agent for purposes of the day-to-day satisfaction of its Sponsored Members' obligations to FICC, including their securities and funds-only settlement obligations.<sup>7</sup>

Novation of eligible trading activity to FICC provides Sponsoring Members and their Sponsored Members the benefits of FICC's independent risk management and guaranty of completion of settlement of such trading activity. In addition, Sponsoring Members also may be able to offset on their balance sheets their obligations to FICC on Sponsored Member Trades against their obligations to FICC on other eligible FICC-cleared activity, as well as take lesser capital charges than would be required to the extent they engaged in the same trading activity with their Sponsored Members outside of a central counterparty.<sup>8</sup> By potentially alleviating balance sheet and capital constraints on their Sponsoring Members, participation in FICC as Sponsored Members may afford eligible institutional firms increased lending capacity and income.

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<sup>5</sup> See Rule 1, definition of "Sponsored Member Trades." Rules, supra note 3.

<sup>6</sup> See Rule 1, definition of "Sponsoring Member Omnibus Account." Id.

<sup>7</sup> See Rule 3A, Sections 5, 6, 7, 8 and 9. Id.

<sup>8</sup> Sponsoring Members interested in such relief should discuss this matter with their accounting and regulatory capital experts.

Currently, eligibility to become a Sponsored Member is limited to an entity that is a registered Investment Company under the Investment Company Act of 1940,<sup>9</sup> is a “qualified institutional buyer” as defined in Rule 144A<sup>10</sup> under the Securities Act of 1933,<sup>11</sup> and has at least one Sponsoring Member willing to sponsor the entity into GSD membership.<sup>12</sup>

The proposed rule change would eliminate the requirement that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940. Nevertheless, in order to ensure that Sponsored Members are financially sophisticated, FICC would retain the current requirement that a Sponsored Member be a “qualified institutional buyer” to the extent that its legal entity type falls under one of the enumerated categories of Rule 144A’s definition of a “qualified institutional buyer.” For institutional firms whose entity types do not clearly fall into one of the enumerated categories in Rule 144A’s definition of “qualified institutional buyer,” FICC would instead require such Sponsored Members to meet the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A (e.g., a corporation) must satisfy in order to be a “qualified institutional

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<sup>9</sup> 15 U.S.C. 80a-1 *et seq.*

The Sponsoring Member-Sponsored Member relationship has historically been based on a custodial banking arrangement in which the Sponsored Member Trades novated to FICC reflect investments by the Sponsoring Member of a registered Investment Company Sponsored Member’s cash through Repo Transactions. However, a custodial banking relationship between a Sponsored Member and its Sponsoring Member(s) is not required under the Rules.

<sup>10</sup> See 17 CFR 230.144A.

<sup>11</sup> 15 U.S.C. 77a *et seq.*

<sup>12</sup> Currently, GSD has one Sponsoring Member and 1422 Sponsored Members.

buyer” (other than requirements relating to entity type or organizational form). Under this alternative requirement, institutional firms whose entity types are not expressly included within the definition of “qualified institutional buyer” in Rule 144A (such as non-U.S. sovereign wealth funds) would be eligible to be Sponsored Members, provided they satisfy the financial thresholds that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A (e.g., a corporation) must meet in order to be a “qualified institutional buyer.” Because conceptions of financial sophistication may change with time, FICC believes it is appropriate to tie this requirement to the definition of “qualified institutional buyer” in Rule 144A, as such definition may be amended from time to time.

FICC believes that expanding eligibility to become a Sponsored Member beyond registered Investment Companies under the Investment Company Act of 1940 is appropriate because FICC’s risk management of the Sponsoring Member-Sponsored Member relationship occurs primarily at the Sponsoring Member level,<sup>13</sup> and the proposed expansion of the entity types eligible to participate in FICC as Sponsored Members (and the commensurate potential volume increase in novated activity) would not require any changes to FICC’s risk management practices applicable to Sponsoring

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<sup>13</sup> For example, a Sponsoring Member is responsible under Section 10 of Rule 3A for posting to FICC the Required Fund Deposit for its Sponsoring Member Omnibus Account, which includes the sum of the stand-alone VaR Charges for each of its Sponsored Members’ novated activity calculated separately. In addition, while Sponsored Members are principally liable to FICC for their settlement obligations, a Sponsoring Member is also required under Section 2 of Rule 3A to provide a guaranty to FICC for such obligations. This means that in the event one or more Sponsored Members does not satisfy its settlement obligations, FICC is able to invoke the guaranty provided by the Sponsoring Member.

Members or to FICC's operational practices applicable to the comparison, novation, netting and settlement of Sponsored Member Trades.

FICC also believes that the proposed expansion of entity types eligible to participate in FICC as Sponsored Members would help to safeguard the U.S. financial market by lowering the risk of liquidity drain, protecting against fire sale risk,<sup>14</sup> and decreasing settlement and operational risk.

Expanding the types of institutional firms that are eligible to participate in FICC as Sponsored Members and thereby benefit from FICC's guaranty of completion of settlement of their eligible transactions would mitigate the risk of a large scale exit by such firms from the U.S. financial market in a stress scenario and therefore lower the risk of a liquidity drain in such a scenario. Specifically, to the extent institutional firms would otherwise be engaging in the same type of eligible trading activity (e.g., repurchase agreement transactions) outside of a central counterparty, having such activity novated to FICC and subject to FICC's guaranty of completion of settlement would reduce the risk that such institutional firms discontinue such trading activity in a Netting Member default situation.

Similarly, broadening the pool of entities eligible for central clearing at FICC as Sponsored Members would also reduce the potential for market disruption from fire sales. Specifically, in a Netting Member default situation, the more institutional firms participate in FICC as Sponsored Members, the more trading activity with the defaulted

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<sup>14</sup> Fire sale risk is the risk of rapid asset sales of securities held by cash lenders when a dealer defaults. This rapid sale has the potential to create a market crisis because cash lenders are likely to sell large amounts of securities in a short period of time, which could dramatically reduce the price of such securities that such lenders are looking to sell.

Netting Member could be centrally liquidated in an orderly manner by FICC rather than by individual counterparties in potential fire sale conditions.

Moreover, to the extent institutional firms would otherwise be engaging in eligible trading activity (e.g., repurchase agreement transactions) outside of a central counterparty, expanding the pool of entities eligible to participate in FICC as Sponsored Members would also decrease settlement and operational risk in the U.S. financial market in that such trading activity would now be eligible to be netted and subject to guaranteed settlement, novation and independent risk management through FICC.

(ii) *Detailed Description of the Proposed Rule Changes  
Related to the Expansion of Sponsored Member Eligibility*

A. *Proposed Changes to Rule 3A, Sections 2(d) and  
3(a)*

Sections 2(d) and 3(a) of Rule 3A currently require that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940 and also be a “qualified institutional buyer” as defined in Rule 144A under the Securities Act of 1933.

FICC is proposing to amend Sections 2(d) and 3(a) of Rule 3A to eliminate the requirement that a Sponsored Member be a registered Investment Company under the Investment Company Act of 1940.

FICC is also proposing to amend Sections 2(d) and 3(a) of Rule 3A to permit institutional firms whose entity types are not expressly included within Rule 144A to be Sponsored Members, provided they meet the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A

(e.g., a corporation) must satisfy in order to be a “qualified institutional buyer” (other than requirements relating to entity type or organizational form).

It should be noted that it is currently and, in connection with the proposed expansion of entity types eligible to participate in FICC as Sponsored Members, would continue to be the responsibility of each Sponsored Member and its Sponsoring Member(s) to evaluate whether entering into a given Sponsored Member Trade is consistent with a Sponsored Member’s legal and regulatory requirements, and that FICC has no responsibility or liability in the event that a Sponsoring Member submits data to FICC for a Sponsored Member Trade that is inconsistent with those requirements.

*B. Proposed Changes to Rule 3A, Sections 3(c) and 4*

To account for the fact that, as proposed, non-U.S. entities that meet the proposed requirements would be permitted to be Sponsored Members, FICC is proposing to amend Section 3(c) of Rule 3A to provide that Sponsored Members that are FFI Members<sup>15</sup> would be required to be FATCA Compliant and to amend Section 4 of Rule 3A to provide that Sponsored Members and their Sponsoring Members would be required to comply with global sanctions laws.<sup>16</sup>

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<sup>15</sup> Pursuant to Rule 1, the term “FFI Member” means “any Person that is treated as a non-U.S. entity for U.S. federal income tax purposes.” For the avoidance of doubt, the term FFI Member also includes “any Member that is a U.S. branch of an entity that is treated as a non-U.S. entity for U.S. federal income tax purposes.” Rules, supra note 3.

<sup>16</sup> Although GSD has Members, including certain Bank Netting Members, which are non-U.S. entities, currently, there are no Sponsoring Members that are non-U.S. entities.

Any future Sponsoring Member or Sponsored Member that is an FFI Member will be subject to the same FATCA Compliance screening and global sanctions screening as any other Member that is a non-U.S. entity.

(iii) Other Proposed Rule Changes

This filing also contains proposed rule changes that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members. These proposed rule changes would provide specificity, clarity and additional transparency to the Rules as described below.

A. *Proposed Changes to Rule 1 (Definitions)*

FICC is proposing to clarify that the “Sponsoring Member Omnibus Account” definition in Rule 1 (Definitions) refers to an “Account” as defined in Rule 1.

B. *Proposed Changes to Rule 3A, Section 7*

FICC is proposing to amend Section 7 of Rule 3A to reference the application of fails charges<sup>17</sup> to a Sponsoring Member Omnibus Account in the same manner as such charges are applied to Netting Members pursuant to Rule 11 (Netting System) and to correct certain typographical errors.

With respect to the application of fails charges, in 2009, FICC received Commission approval of a rule filing to impose fails charges on Netting Members, which was an action that had been requested of GSD by the Treasury Markets Practices Group (“TMPG”)<sup>18</sup> in order to encourage market participants to resolve fails promptly.<sup>19</sup> The approved rule changes were included in Section 14 of Rule 11 (Netting System) and were

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<sup>17</sup> The term “fails charge” refers to the charge imposed by FICC on Netting Members for a delivery failure in Treasury Securities or debentures issued by Fannie Mae, Freddie Mac or the Federal Home Loan Banks, pursuant to Section 14 of Rule 11. Rules, supra note 3.

<sup>18</sup> The TMPG is a group of market participants that is active in the Treasury securities market and is sponsored by The Federal Reserve Bank of New York.

<sup>19</sup> Securities Exchange Act Release No. 59802 (April 20, 2009), 74 FR 19248 (April 28, 2009) (SR-FICC-2009-03).

stated to apply to Netting Members. As an account of a Netting Member (acting as a Sponsoring Member), FICC has imposed fails charges, if applicable, on Sponsoring Members for their Sponsoring Member Omnibus Accounts since the implementation of the charges in 2009. In reviewing the Rules in connection with this present filing, FICC believes that the application of the fails charges to a Sponsoring Member's Sponsoring Member Omnibus Account should be made clear in Rule 3A for transparency.

*C. Proposed Changes to Rule 3A, Section 9*

FICC is proposing to amend Section 9 of Rule 3A to correct an out-of-date cross-reference to Rule 13 (Funds-Only Settlement).

*D. Proposed Changes to Rule 3A, Section 10*

FICC is proposing to amend Section 10 of Rule 3A to reflect the current Clearing Fund calculation procedures applicable to a Sponsoring Member's Sponsoring Member Omnibus Account. Specifically, FICC is proposing to amend Section 10 of Rule 3A to specify that a Sponsoring Member's Sponsoring Member Omnibus Account Required Fund Deposit would be equal to the sum of the following: (I) the sum of the VaR Charges for all of the Sponsored Members whose activity is represented in the Sponsoring Member Omnibus Account as derived pursuant to Section 1b(a)(i) of Rule 4 (Clearing Fund and Loss Allocation), and (II) all amounts derived pursuant to the provisions of Rule 4 other than pursuant to Section 1b(a)(i) of Rule 4 computed at the level of the Sponsoring Member Omnibus Account. The proposed rule changes maintain the substance of the calculation of the Required Fund Deposit for a Sponsoring Member's Sponsoring Member Omnibus Account (i.e., the main charges applicable to the individual Sponsored Members in the account are summed and then certain components are applied



at the level of the Sponsoring Member Omnibus Account) but update the rules provisions to reflect the current Clearing Fund calculation terminology and delete references to terms that are no longer used in the Rules (such as “Clearing Fund components related to Fail Net Settlement Positions and Funds-Only Settlement amounts”).

FICC is also proposing to amend Section 10 of Rule 3A to specify that for purposes of calculating the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account, FICC would apply the higher of the Required Fund Deposit calculation as of the beginning of the current Business Day and intraday on the current Business Day.

In 2011, FICC received Commission approval to re-calculate each Business Day, at times established by FICC for this purpose, the amount of the VaR Charge applicable to each Margin Portfolio of a Member, based upon the open, intraday positions of such Margin Portfolio, for purposes of establishing whether a Member would be required to make payment of an additional amount (the Member’s “Intraday Supplemental Fund Deposit”) to its Required Fund Deposit.<sup>20</sup> The approved rule changes were included in Section 2a of Rule 4 (Clearing Fund and Loss Allocation). Prior to this approval, Clearing Fund requirements (including with respect to a Sponsoring Member’s Sponsoring Member Omnibus Account) were calculated once each Business Day. Since the approval of these rule changes in 2011, FICC has calculated the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account based on the higher of the Required Fund Deposit calculation as of the beginning of the current Business Day and intraday on the current Business Day. In reviewing the Rules in

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<sup>20</sup> Securities Exchange Act Release No. 63986 (February 28, 2011), 76 FR 12144 (March 4, 2011) (SR-FICC-2010-09).

connection with this present filing, FICC believes that this calculation procedure for the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account should be made clear in Rule 3A for transparency.

FICC is also proposing to amend Section 10 of Rule 3A to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation).

*E. Proposed Changes to Rule 3A, Section 12*

FICC is proposing to amend Section 12 of Rule 3A to reflect the current loss allocation process applicable to Sponsored Member Trades in the event that the Sponsoring Member is insolvent or otherwise in default to FICC. Specifically, FICC is proposing to amend Section 12 of Rule 3A to specify that any Remaining Loss incurred by FICC would be allocated to the Tier One Netting Members in accordance with the principles set forth in Section 7(d) of Rule 4 (Clearing Fund and Loss Allocation).

In 2011, FICC received Commission approval for its current loss allocation process set forth in Rule 4, which provides for loss mutualization of any Remaining Loss among all Tier One Netting Members.<sup>21</sup> FICC proposes to update references in Section 12 of Rule 3A to reference the current loss allocation process for Tier One Netting Members.

FICC also proposes to amend Section 12 of Rule 3A to correct certain out-of-date cross-references to Rule 4 (Clearing Fund and Loss Allocation) and to correct certain typographical errors.

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<sup>21</sup> Id.

*F. Proposed Changes to Rule 3A, Sections 13 and 14*

FICC is proposing to amend Sections 13 and 14 of Rule 3A to correct certain out-of-date cross-references to Rule 21 (Restrictions on Access to Services).

*G. Proposed Changes to Rule 3A, Section 15*

FICC is proposing to amend Section 15 of Rule 3A to specify the standard with respect to which a Sponsoring Member is deemed by FICC to have knowledge that one of its Sponsored Members is insolvent or is otherwise unable to perform on any of its material contracts, obligations or agreements for purposes of the Sponsoring Member's obligation to inform FICC of such matter. Specifically, FICC is proposing to specify that if one or more duly authorized representatives of a Sponsoring Member, in its capacity as such, has knowledge that one of its Sponsored Members is insolvent or otherwise unable to perform on any of its material contracts, obligations or agreements, that such knowledge triggers the Sponsoring Member's obligation to inform FICC of such matter.

2. Statutory Basis

Section 17A(b)(3)(F) of the Act requires, in part, that the Rules be designed to (i) "promote the prompt and accurate clearance and settlement of securities transactions,"<sup>22</sup> and (ii) "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest."<sup>23</sup>

By expanding the types of entities that may participate in FICC as Sponsored Members, FICC believes that the proposed rule change would help to safeguard the U.S.

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<sup>22</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>23</sup> Id.

financial market by lowering the risk of liquidity drain (through FICC's guaranty of completion of settlement for a greater number of eligible transactions), protecting against fire sale risk (through FICC's ability to centralize and control the liquidation of a greater portion of a failed counterparty's portfolio) and decreasing settlement and operational risk (by making a greater number of transactions eligible to be netted and subject to guaranteed settlement, novation and independent risk management through FICC). By lowering the risk of liquidity drain in the U.S. financial market and protecting against fire sale risk, FICC believes the proposed rule change would "protect investors and the public interest" consistent with the requirements of the Act, cited above. By decreasing settlement and operational risk, FICC believes the proposed rule change would also "promote the prompt and accurate clearance and settlement of securities transactions" and "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions" consistent with the requirements of the Act, cited above.

By providing specificity, clarity, and additional transparency to the Rules, the proposed rule changes to Rule 1 (Definitions) and Rule 3A (Sponsoring Members and Sponsored Members) that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members would provide Members with a better understanding of the Rules, making errors in the performance of their responsibilities to FICC less likely to occur and thereby ensuring that FICC's clearing and settlement system works efficiently. Therefore, FICC believes the proposed rule change would "promote the prompt and accurate clearance and settlement of securities transactions" by FICC and also "remove impediments to and perfect the mechanism of a national system for the prompt and

accurate clearance and settlement of securities transactions” consistent with the requirements of the Act, cited above.

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

FICC believes that the proposed rule changes associated with the expansion of entity types eligible to be Sponsored Members would promote competition by increasing the types of entities that may participate in FICC as Sponsored Members and therefore permit more market participants to utilize FICC’s services.

At the same time, participation in FICC as a Sponsored Member would continue to be limited to legal entities that are either “qualified institutional buyers” as defined in Rule 144A under the Securities Act of 1933, or that otherwise satisfy the requirements that an entity enumerated in subsection (a)(1)(i)(H) of the definition of “qualified institutional buyer” in Rule 144A (e.g., a corporation) must satisfy in order to be a “qualified institutional buyer” (other than requirements relating to entity type or organizational form), and that have at least one Sponsoring Member willing to sponsor them into GSD membership. These limitations may impact institutional firms that are unable to satisfy such eligibility requirements by excluding them from being able to novate their eligible activity to FICC (and avail themselves of the commensurate benefits described in *Section 3(a)(i) – Background on the Proposed Expansion of Sponsored Member Eligibility* above). Nevertheless, FICC believes that any resulting burden on competition would be necessary and appropriate in furtherance of the Act, as permitted by Section 17A(b)(3)(I) of the Act,<sup>24</sup> in light of the fact that such eligibility requirements are designed to allow FICC to ensure the financial sophistication of Sponsored Members

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<sup>24</sup> 15 U.S.C. 78q-1(b)(3)(I).

and to prudently manage the risk associated with Sponsored Members' participation in FICC. Moreover, FICC would not restrict the ability of institutional firms to enter into eligible transactions with Netting Members (including Sponsoring Members) outside of GSD.

FICC believes that the proposed changes to Rule 1 (Definitions) and Rule 3A (Sponsoring Members and Sponsored Members) that are unrelated to the proposed expansion of entity types eligible to be Sponsored Members would not have an impact, nor impose any burden, on competition because each of such proposed changes would simply provide specificity, clarity and additional transparency within the Rules.

(C) Clearing Agency'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. FICC will notify the Commission of any written comments received by FICC.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate 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 or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule 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:

- 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-FICC-2017-003 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-FICC-2017-003. 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 FICC 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-FICC-2017-003 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>25</sup>

Secretary

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<sup>25</sup> 17 CFR 200.30-3(a)(12).



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

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

**FIXED INCOME CLEARING CORPORATION**

**GOVERNMENT SECURITIES DIVISION RULEBOOK**

## **RULE 1 – DEFINITIONS**

Unless the context requires otherwise, the terms defined in this Rule shall, for all purposes of these Rules, have the meanings herein specified.

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### **Sponsoring Member Omnibus Account**

The term “Sponsoring Member Omnibus Account” shall mean the Aaccount maintained by a Sponsoring Member that contains the activity of its Sponsored Members that is submitted to the Corporation. The Sponsoring Member Omnibus Account shall be separate from the Aaccounts associated with the Sponsoring Member’s activity as a Netting Member except as contemplated by Sections 10, 11 and 12 of Rule 3A and under the Sponsoring Member Guaranty.

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## RULE 3A – SPONSORING MEMBERS AND SPONSORED MEMBERS

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### Section 2 – Qualifications of Sponsoring Members, the Application Process and Continuance Standards

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(d) A Sponsoring Member shall represent to the Corporation in a writing signed by an **duly authorized** officer of the Sponsoring Member that **each of** its Sponsored Members **are registered Investment Companies under the Investment Company Act of 1940 and are (i) is a “qualified institutional buyers” as defined in Rule 144A under the Securities Act of 1933, as amended, or (ii) is a legal entity that is not organized as an entity specifically listed in Rule 144A(a)(1)(i)(H) under the Securities Act of 1933, as amended, but that satisfies the requirements that an entity listed in Rule 144A(a)(1)(i)(H) under the Securities Act of 1933, as amended, must satisfy in order to be a “qualified institutional buyer” (other than any such requirements relating to legal entity type or organizational form).** Such representation shall be provided to the Corporation within 10 business days after each quarter-end, with respect to the quarter then ended. If the Sponsoring Member fails to provide the requisite representation within the requisite 10-business day period, the Sponsoring Member shall be subject to a fine by the Corporation which shall be determined in accordance with the Fine Schedule for Failure to Timely Provide Financial and Related Information. The Corporation shall have the right to cease to act for the Sponsoring Member in its capacity as a Sponsoring Member pursuant to Section 14 of this Rule 3A if the Sponsoring Member does not provide the requisite representation regarding one or more of its Sponsored Members. The Corporation shall also have the right to cease to act, pursuant to Section 13 of this Rule 3A, for any Sponsored Members for which it does not have a requisite representation, unless the Sponsoring Member and/or the affected Sponsored Member(s) request that such action not be taken and the Corporation determines that, depending upon the specific circumstances and the records of the Sponsoring Member and the Sponsored Member(s), it is appropriate instead to establish a time period, which shall be determined by the Corporation, during which the Sponsoring Member and/or the affected Sponsored Member(s) must resume compliance with the representation requirement. In the event that the Sponsoring Member or the Sponsored Member(s) are unable to satisfy such requirement within the time period specified by the Corporation, the Corporation shall, pursuant to these Rules, cease to act for the Sponsoring Member in its capacity as a Sponsoring Member pursuant to Section 14 of this Rule 3A and/or cease to act for the Sponsored Member(s) pursuant to Section 13 of this Rule 3A.

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### Section 3 - Qualifications of Sponsored Members, Approval Process and Continuance Standard

(a) A Person shall be eligible to become a Sponsored Member if: (i) it is sponsored into membership by a Sponsoring Member, and (ii) it **(A) is a registered Investment Company under the Investment Company Act of 1940 and a “qualified institutional buyer” as defined by Rule 144A under the Securities Act of 1933, as amended, or (B) is a legal entity that is not**

**organized as an entity specifically listed in Rule 144A(a)(1)(i)(H) under the Securities Act of 1933, as amended, but that satisfies the requirements that an entity listed in Rule 144A(a)(1)(i)(H) under the Securities Act of 1933, as amended, must satisfy in order to be a “qualified institutional buyer” (other than any such requirements relating to legal entity type or organizational form).** The Corporation shall have the right to rely on the representation provided by the Sponsoring Member regarding satisfaction of (ii).

\* \* \* \*

(c) Each Person to become a Sponsored Member shall sign and deliver to the Corporation a Sponsored Member Agreement whereby the Person shall agree to any terms and conditions deemed by the Corporation to be necessary in order to protect itself and its Members. **Each Person to become a Sponsored Member that shall be an FFI Member must be FATCA Compliant.**

\* \* \* \*

#### Section 4—Compliance with Laws

Each of the Sponsoring Members and Sponsored Members shall comply in all material respects with all applicable laws, including applicable laws relating to securities, taxation and money laundering, **as well as global sanctions laws,** in connection with the use of the Corporation’s services.

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#### Section 7 – The Netting System and Guaranty of Settlement

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(c) Fail Net Settlement Positions per CUSIP shall be calculated at the level of the Sponsoring Member Omnibus Account in the same way as they are calculated for Netting Members pursuant to Rule 11. At the request of the Corporation, the Sponsoring Member shall inform the Corporation as to the manner in which the Sponsoring Member allocates a Fail Net Settlement Position among its Sponsored Members. **Fail charges shall be applied at the level of the Sponsoring Member Omnibus Account in the same way as they are applied to Netting Members pursuant to Rule 11.**

(d) The Corporation’s guaranty of settlement shall apply to Sponsored Member Trades and such trades shall be novated in the same manner in which trades of Netting Members are novated and settlement is guaranteed pursuant to Section **58** of Rule **85**.

\* \* \* \*

Section 9—Funds-Only Settlement

\* \* \* \*

(d) Section ~~67~~ of Rule 13 shall apply to the Sponsored Member activity in the same manner in which it applies to Netting Member activity, except that the Sponsoring Member shall have all obligations arising thereunder even if caused by its Sponsored Members.

Section 10—Clearing Fund Obligations

\* \* \* \*

(c) The amount of the Sponsoring Member Omnibus Account Required Fund Deposit to be made and maintained by each Sponsoring Member on each Business Day shall be determined as follows: A Required Fund Deposit calculation shall be performed for each Sponsored Member whose activity is represented in the Sponsoring Member Omnibus Account pursuant to Rule 4, subject to the provisions of this Section 10 of this Rule 3A. The Sponsoring Member Omnibus Account Required Fund Deposit shall be equal to the sum of the following:—(1) the sum of the ~~Required Fund Deposit calculations~~ VaR Charges for all of the Sponsored Members whose activity is represented in the Sponsoring Member Omnibus Account as derived pursuant to Section 1b(a)(i) of Rule 4, and (2) all amounts derived pursuant to the provisions of Rule 4 other than pursuant to Section 1b(a)(i) of Rule 4 the Clearing Fund components related to Fail Net Settlement Positions and Funds-Only Settlement amounts computed at the level of the Sponsoring Member Omnibus Account. For purposes of calculating the Unadjusted GSD Margin Portfolio Amount applicable to a Sponsoring Member Omnibus Account, the Corporation shall apply the higher of the Required Fund Deposit calculation as of the beginning of the current Business Day and intraday on the current Business Day adjust for any over-collateralization in the Funds-Only Settlement Amount by determining such amount to be zero, if applicable, and excluding Fail Net Settlement Positions from such calculation, except under extraordinary circumstances.

(d) The lesser of \$5,000,000 or 10 percent of the total amount arrived at in subsection (c) of this Section 10, with a minimum of \$100,000 must be made and maintained in cash, with the remaining portion to be made and maintained in the form specified in, and subject to the requirements of, Section ~~43~~ of Rule 4, and subject to subsection (~~of~~) of Section 2 of Rule 4.

(e) The Corporation shall have the right to increase the Sponsoring Member Omnibus Account Required Fund Deposit in the same way and for the same reasons as set forth in subsections (~~g~~), (~~h~~), and (~~ne~~) of Section 2 of Rule 4.

(f) Sections 2a, 3, 3a, 3b, 4, 5, ~~68~~, 9, 10, and 11 and 12 of Rule 4 shall apply to the Sponsoring Member Omnibus Account Required Fund Deposit with respect to obligations of a Sponsoring Member under the Rules, including its obligations arising under the Sponsoring Member Omnibus Account, and the obligations of a Sponsoring Member under its Sponsoring Member Guaranty to the same extent as such Sections apply to any Required Fund Deposit and any other obligations of a Member. For purposes of Section ~~54~~ of Rule 4, obligations and liabilities of a Netting Member to the Corporation that shall be secured shall include, without limitation, a Netting Member's obligations as a Sponsoring Member under the Rules, including,

without limitation, any obligation of any such Sponsoring Member to provide the Sponsoring Member Omnibus Account Required Fund Deposit, such Sponsoring Member's obligations arising under the Sponsoring Member Omnibus Account of such Sponsoring Member and such Sponsoring Member's obligations under its Sponsoring Member Guaranty.

\* \* \* \*

#### Section 12—Loss Allocation Obligations

(a) Sponsored Members shall ~~be~~ not be obligated for allocations, pursuant to Rule 4, of loss or liability incurred by the Corporation. To the extent that a Remaining Loss (as defined in Section ~~87~~ of Rule 4) is determined by the Corporation to arise in connection with ~~Sponsored Member Trades~~**Direct Transactions that the Sponsored Members had with their Sponsoring Member** (i.e., in connection with the insolvency or default of a Sponsoring Member), the Sponsored Members shall not be responsible for or considered in the loss allocation calculation, but rather such loss shall be **allocated to Tier One Netting Members covered by the other Netting Members that had Direct Transactions with the Sponsoring Member in its capacity as a Netting Member** in accordance with the principles set forth in Section ~~87(d)(i)~~ of Rule 4.

(b) To the extent the Corporation incurs a Remaining Loss ~~other than one referred to in (a), a loss pursuant to Section 8(e) of Rule 4~~ or an Other Loss (as defined in Section ~~87(f)~~ of Rule 4) and a loss allocation obligation arises that would be the responsibility of the Sponsoring Member Omnibus Account if the Sponsoring Member Omnibus Account were a Netting Member, the Corporation shall calculate such loss allocation obligation as if the affected Sponsored Members were subject to such allocations pursuant to Section ~~87~~ of Rule 4, but the Sponsoring Member shall be responsible for satisfying such obligations.

\* \* \* \*

#### Section 13—Restrictions on Access to Services by a Sponsored Member

(a) Based upon the judgment of the Corporation that adequate cause exists to do so, the Corporation may at any time upon providing notice to the Sponsored Member and its Sponsoring Member, suspend a Sponsored Member from any service provided by the Corporation either with respect to a particular transaction or transactions or with respect to transactions generally, or prohibit or limit such Sponsored Member with respect to access to services offered by the Corporation in the event that one or more of the factors set forth in Section 1(a) through ~~(f)~~**(g)** of Rule 21, with the Corporation making the determinations set forth therein, is present with respect to the Sponsored Member, and the Corporation, in its sole discretion, has reasonable grounds to believe that such action is appropriate either for the protection of the Corporation or other Members or to facilitate the orderly and continuous performance of the Corporation's services.

\* \* \* \*

Section 14—Restrictions on Access to Services by a Sponsoring Member

(a) Based upon the judgment of the Corporation that adequate cause exists to do so, the Corporation may at any time upon providing notice to the Sponsoring Member, suspend a Sponsoring Member in its capacity as a Sponsoring Member from any service provided by the Corporation either with respect to a particular transaction or transactions or with respect to transactions generally or prohibit or limit such Sponsoring Member with respect to access to services offered by the Corporation in the event that if one or more of the factors set forth in Section 1(a) through (~~f~~**g**) of Rule 21, with the Corporation making the determinations set forth therein, is present with respect to the Sponsoring Member, and the Corporation, in its sole discretion, has reasonable grounds to believe that such action is appropriate either for the protection of the Corporation or other Members or to facilitate the orderly and continuous performance of the Corporation's services.

\* \* \* \*

Section 15—Insolvency of a Sponsored Member

(a) A Sponsored Member and its Sponsoring Member (to the extent it has knowledge thereof) shall be obligated to inform the Corporation that the Sponsored Member is insolvent or that the Sponsored Member will be unable to perform any of its material contracts, obligations or agreements in the same manner as required by Section 1 of Rule 22 for other Members. **For purposes of this section, a Sponsoring Member shall be deemed to have knowledge that a Sponsored Member is insolvent or will be unable to perform on any of its material contracts, obligations or agreements if one or more duly authorized representatives of the Sponsoring Member, in its capacity as such, has knowledge of such matters.** A Sponsored Member shall be treated by the Corporation in all respects as insolvent under the same circumstances set forth in Section 2 of Rule 22 for other Members. Section 3 of Rule 22 shall apply, in the same manner in which such Section applies to other Members, in the case where the Corporation treats a Sponsored Member as insolvent.