SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–83631; File No. SR–FICC–2017–022]

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Amendment No. 1 to a Proposed Rule Change To Amend the Loss Allocation Rules and Make Other Changes

July 13, 2018.

On December 18, 2017, Fixed Income Clearing Corporation (''FICC'') filed with the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'') and Rule 19b–4 thereunder, proposed rule change SR–FICC–2017–022 (''Proposed Rule Change'') to amend the loss allocation rules and make other changes; the Proposed Rule Change was published for comment in the **Federal Register** on January 8, 2018.[1] On February 8, 2018, the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the Proposed Rule Change.[2] On March 20, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the Proposed Rule Change; on June 25, 2018, the Commission designated a longer period for Commission action on the proceedings to determine whether to approve or disapprove the Proposed Rule Change.[3] On June 28, 2018, FICC filed Amendment No. 1 to the Proposed Rule Change to amend and replace in its entirety the Proposed Rule Change as originally submitted on December 18, 2017.[4] As of the date of this release, the Commission has not received any comments on the Proposed Rule Change.

The Proposed Rule Change, as amended by Amendment No. 1, is described in Items I and II below, which Items have been prepared by FICC. The Commission is publishing this notice to solicit comments on the Proposed Rule Change, as amended by Amendment No. 1, from interested persons.

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

The proposed rule change consists of modifications to FICC's Government Securities Division (''GSD'') Rulebook (''GSD Rules'') and Mortgage-Backed Securities Division (''MBSD'' and, together with GSD, the ''Divisions'' and, each, a ''Division'') Clearing Rules (''MBSD Rules,'' and collectively with the GSD Rules, the ''Rules'') in order to amend provisions in the Rules regarding loss allocation as well as make other changes, as described in greater detail below.[5]

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 III 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

Description of Amendment No. 1

This filing constitutes Amendment No. 1 (''Amendment'') to rule filing SR–FICC–2017–022 (''Rule Filing'') previously filed by FICC on December 18, 2017.[6] This Amendment amends and replaces the Rule Filing in its entirety. FICC submits this Amendment in order to further clarify the operation of the proposed rule changes on loss allocation by providing additional information and examples. In particular, this Amendment would:

(i) Clarify which Tier One Netting Members and Tier One Members would be subject to loss allocation with respect to Defaulting Member Events (as defined below and in the proposed rule change) and Declared Non-Default Loss Events (as defined below and in the proposed rule change) occurring during an Event Period (as defined below and in the proposed rule change). Specifically, pursuant to the Amendment, proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that each Tier One Netting Member or Tier One Member, as applicable, that is a Tier One Netting Member or Tier One Member on the first day of an Event Period would be obligated to pay its pro rata share of losses and liabilities arising out of or relating to each Defaulting Member Event (other than a Defaulting Member Event with respect to which it is the Defaulting Member (as defined below and in the proposed rule change)) and each Declared Non-Default Loss Event occurring during the Event Period. Proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would also make it clear

[1] 15 U.S.C. 78s(b)(1) and 17 CFR 240.19b–4, respectively. Securities Exchange Act Release No. 82427 (January 2, 2018), 83 FR 854 (January 8, 2018) (SR–FICC–2017–022). On December 18, 2017, FICC filed the Proposed Rule Change as advance notice SR–FICC–2017–806 (''Advance Notice'') with the Commission pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act entitled the Payment, Clearing, and Settlement Supervision Act of 2010 (''Clearing Supervision Act'') and Rule 19b–4(n)(1)(i) of the Act. (12 U.S.C. 5465(e)(1) and 17 CFR 240.19b–4(n)(1)(i), respectively.) On January 30, 2018, the Commission published in the **Federal Register** notice of filing of the Advance Notice. The notice also extended the review period for the Advance Notice pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act. (12 U.S.C. 5465(e)(1)(H).) *See* Securities Exchange Act Release No. 82583 (January 24, 2018), 83 FR 4358 (January 30, 2018) (SR–FICC–2017–806). On April 10, 2018, the Commission required additional information for consideration of the Advance Notice, pursuant to Section 806(e)(1)(D) of the Clearing Supervision Act, which provided the Commission with an additional 60-days in the review period beginning on the date that the information requested is received by the Commission. (12 U.S.C. 5465(e)(1)(D).) *See* Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled ''Commission's Request for Additional Information,'' *available at http://www.sec.gov/rules/sro/ficc-an.shtml.* On June 28, 2018, FICC filed Amendment No. 1 to the Advance Notice. To promote the public availability and transparency of its post-notice amendment, FICC submitted a copy of Amendment No. 1 through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Advance Notice has been posted on the Commission's website at *https://www.sec.gov/rules/sro/ficc-an.htm* and thus been publicly available since June 29, 2018. On July 6, 2018, the Commission received the information requested, which added an additional 60-days to the review period pursuant to Sections 806(e)(1)(E) and (G) of the Clearing Supervision Act. (12 U.S.C. 5465(e)(1)(E) and (G).) *See* Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled ''Response to the Commission's Request for Additional Information,'' *available at http://www.sec.gov/rules/sro/ficc-an.shtml.* The proposal, as set forth in both the Advance Notice and the Proposed Rule Change, shall not take effect until all required regulatory actions are completed.

[2] Securities Exchange Act Release No. 82670 (February 8, 2018), 83 FR 6626 (February 14, 2018) (SR–DTC–2017–022; SR–FICC–2017–022; SR–NSCC–2017–018).

[3] Securities Exchange Act Release No. 82909 (March 20, 2018), 83 FR 12990 (March 26, 2018) (SR–FICC–2017–022); Securities Exchange Act Release No. 83510 (June 25, 2018), 83 FR 30791 (June 29, 2018) (SR–DTC–2017–022; SR–FICC–2017–022; SR–NSCC–2017–018).

[4] To promote the public availability and transparency of its post-notice amendment, FICC submitted a copy of Amendment No. 1 through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Proposed Rule Change has been posted on the Commission's website at *https://www.sec.gov/rules/sro/ficc.htm* and thus been publicly available since June 29, 2018.

[5] Capitalized terms not defined herein are defined in the GSD Rules, *available at http://www.dtcc.com/~/media/Files/Downloads/legal/rules/ficc_gov_rules.pdf,* and the MBSD Rules, *available at www.dtcc.com/~/media/Files/Downloads/legal/rules/ficc_mbsd_rules.pdf.*

[6] *See* Securities Exchange Act Release No. 82427 (January 2, 2018), 83 FR 854 (January 8, 2018) (SR–FICC–2017–022).

that any Tier One Netting Member or Tier One Member, as applicable, for which FICC ceases to act on a non-Business Day, triggering an Event Period that commences on the next Business Day, would be deemed to be a Tier One Netting Member or Tier One Member, as applicable, on the first day of that Event Period.

(ii) Clarify the obligations and Loss Allocation Cap (as defined below and in the proposed rule change) of a Tier One Netting Member or a Tier One Member, as applicable, that withdraws from membership in respect of a loss allocation round. Specifically, pursuant to the Amendment, proposed Section 7b of GSD Rule 4 and MBSD Rule 4 would provide that the Tier One Netting Member or Tier One Member, as applicable, would nevertheless remain obligated for its pro rata share of losses and liabilities with respect to any Event Period for which it is otherwise obligated under GSD Rule 4 or MBSD Rule 4, as applicable; however, its aggregate obligation would be limited to the amount of its Loss Allocation Cap as fixed in the round for which it withdrew.

(iii) Clarify that a member would be obligated to FICC for all losses and liabilities incurred by FICC arising out of or relating to any Defaulting Member Event with respect to the member. Specifically, pursuant to the Amendment, proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that each member would be obligated to FICC for the entire amount of any loss or liability incurred by FICC arising out of or relating to any Defaulting Member Event with respect to such member.

(iv) Clarify that, although a Defaulting Member would not be allocated a ratable share of losses and liabilities arising out of or relating to its own Defaulting Member Event, it would remain obligated to FICC for all such losses and liabilities. Specifically, pursuant to the Amendment, proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that no loss allocation under GSD Rule 4 or MBSD Rule 4, as applicable, would constitute a waiver of any claim FICC may have against a GSD Member or MBSD Member, as applicable, for any loss or liability to which the GSD Member or MBSD Member is subject under the GSD Rules or MBSD Rules, as applicable, including, without limitation, any loss or liability to which it may be subject under GSD Rule 4 or MBSD Rule 4, as applicable.

In addition, pursuant to the Amendment, FICC is making other clarifying and technical changes to the proposed rule change, as proposed herein.

Nature of the Proposed Change

The primary purpose of this proposed rule change is to amend GSD's and MBSD's loss allocation rules in order to enhance the resiliency of the Divisions' loss allocation processes so that each Division can take timely action to address multiple loss events that occur in succession during a short period of time (defined and explained in detail below). In connection therewith, the proposed rule change would (i) align the loss allocation rules of the three clearing agencies of The Depository Trust & Clearing Corporation (''DTCC''), namely The Depository Trust Company (''DTC''), National Securities Clearing Corporation (''NSCC''), and FICC (collectively, the ''DTCC Clearing Agencies''), so as to provide consistent treatment, to the extent practicable and appropriate, especially for firms that are participants of two or more DTCC Clearing Agencies, (ii) increase transparency and accessibility of the loss allocation rules by enhancing their readability and clarity, (iii) amend language regarding FICC's use of MBSD Clearing Fund, and (iv) make conforming and technical changes.

(i) Background

Central counterparties (''CCPs'') play a key role in financial markets by mitigating counterparty credit risk on transactions between market participants. CCPs achieve this by providing guaranties to participants and, as a consequence, are typically exposed to credit risks that could lead to default losses. In addition, in performing its critical functions, a CCP could be exposed to non-default losses that are otherwise incident to the CCP's clearance and settlement business.

A CCP's rulebook should provide a complete description of how losses would be allocated to participants if the size of the losses exceeded the CCP's pre-funded resources. Doing so provides for an orderly allocation of losses, and potentially allows the CCP to continue providing critical services to the market and thereby results in significant financial stability benefits. In addition, a clear description of the loss allocation process offers transparency and accessibility to the CCP's participants.

Current FICC Loss Allocation Process

As CCPs, FICC's Divisions' loss allocation processes are key components of their respective risk management processes. Risk management is the foundation of FICC's ability to guarantee settlement in each Division, as well as the means by which FICC protects itself and its members from the risks inherent in the clearance and settlement process. FICC's risk management processes must account for the fact that, in certain extreme circumstances, the collateral and other financial resources that secure FICC's risk exposures may not be sufficient to fully cover losses resulting from the liquidation of the portfolio of a member for whom a Division has ceased to act.[7]

The GSD Rules and the MBSD Rules each currently provide for a loss allocation process through which both FICC (by applying up to 25% of its retained earnings in accordance with Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4) and its members would share in the allocation of a loss resulting from the default of a member for whom a Division has ceased to act pursuant to the Rules. The GSD Rules and the MBSD Rules also recognize that FICC may incur losses outside the context of a defaulting member that are otherwise incident to each Division's clearance and settlement business.

The current GSD and MBSD loss allocation rules provide that, in the event the Division ceases to act for a member, the amounts on deposit to the Clearing Fund from the defaulting member, along with any other resources of, or attributable to, the defaulting member that FICC may access under the GSD Rules or the MBSD Rules (*e.g.,* payments from Cross-Guaranty Agreements), are the first source of funds the Division would use to cover any losses that may result from the closeout of the defaulting member's guaranteed positions. If these amounts are not sufficient to cover all losses incurred, then each Division will apply the following available resources, in the following loss allocation waterfall order:

First, as provided in the current Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4, FICC's corporate contribution of up to 25 percent of FICC's retained earnings existing at the time of the failure of a defaulting member to fulfill its obligations to FICC,

[7] GSD is permitted to cease to act for (i) a GSD Member pursuant to GSD Rule 21 (Restrictions on Access to Services) and GSD Rule 22 (Insolvency of a Member), (ii) a Sponsoring Member pursuant to Section 14 and Section 16 of GSD Rule 3A (Sponsoring Members and Sponsored Members), and (iii) a Sponsored Member pursuant to Section 13 and Section 15 of GSD Rule 3A (Sponsoring Members and Sponsored Members). MBSD is permitted to cease to act for an MBSD Member pursuant to MBSD Rule 14 (Restrictions on Access to Services) and MBSD Rule 16 (Insolvency of a Member). GSD Rule 22A (Procedures for When the Corporation Ceases to Act) and MBSD Rule 17 (Procedures for When the Corporation Ceases to Act) set out the types of actions FICC may take when it ceases to act for a member. *Supra* note 5.

or such greater amount as the Board of Directors may determine; and

Second, if a loss still remains, use of the Clearing Fund of the Division and assessing the Division's Members in the manner provided in GSD Rule 4 and MBSD Rule 4, as the case may be. Specifically, FICC will divide the loss ratably between Tier One Netting Members and Tier Two Members with respect to GSD, or between Tier One Members and Tier Two Members with respect to MBSD, based on original counterparty activity with the defaulting member. Then the loss allocation process applicable to Tier One Netting Members or Tier One Members, as applicable, and Tier Two Members will proceed in the manner provided in GSD Rule 4 and MBSD Rule 4, as the case may be.

Specifically, the applicable Division will first assess each Tier One Netting Member or Tier One Member, as applicable, an amount up to $50,000, in an equal basis per such member. If a loss remains, the Division will allocate the remaining loss ratably among Tier One Netting Members or Tier One Members, as applicable, in accordance with the amount of each Tier One Netting Member's or Tier One Member's, as applicable, respective average daily Required Fund Deposit over the prior twelve (12) months. If a Tier One Netting Member or Tier One Member, as applicable, did not maintain a Required Fund Deposit for twelve (12) months, its loss allocation amount will be based on its average daily Required Fund Deposit over the time period during which such member did maintain a Required Fund Deposit.

Pursuant to current Section 7(g) of GSD Rule 4 and MBSD Rule 4, if, as a result of the Division's application of the Required Fund Deposit of a member, a member's actual Clearing Fund deposit is less than its Required Fund Deposit, it will be required to eliminate such deficiency in order to satisfy its Required Fund Deposit amount. In addition to losses that may result from the closeout of the defaulting member's guaranteed positions, Tier One Netting Members or Tier One Members, as applicable, can also be assessed for non-default losses incident to each Division's clearance and settlement business, pursuant to current Section 7(f) of GSD Rule 4 and MBSD Rule 4.

The Rules of both Divisions currently provide that Tier Two Members are only subject to loss allocation to the extent they traded with the defaulting member and their trades resulted in a liquidation loss. FICC will assess Tier Two Members ratably based on their loss as a percentage of the entire remaining loss attributable to Tier Two Members.[8] Tier Two Members are required to pay their loss allocation obligations in full and replenish their Required Fund Deposits as needed and as applicable. The current Rule provisions which provide for loss allocation of non-default losses incident to each Division's clearance and settlement business (*i.e.,* Section 7(f) of GSD Rule 4 and MBSD Rule 4) do not apply to Tier Two Members.

Overview of the Proposed Rule Changes

A. Changes To Enhance Resiliency of GSD's and MBSD's Loss Allocation Processes

In order to enhance the resiliency of GSD's and MBSD's loss allocation processes, FICC proposes to change the manner in which each of the aspects of the loss allocation waterfall described above would be employed. GSD and MBSD would retain the current core loss allocation process following the application of the defaulting member's resources, *i.e.,* first, by applying FICC's corporate contribution, and second, by pro rata allocations to Tier One Netting Members or Tier One Members, as applicable, and Tier Two Members. However, GSD and MBSD would clarify or adjust certain elements and introduce certain new loss allocation concepts, as further discussed below. The proposal would also retain the types of losses that can be allocated to Tier One Netting Members or Tier One Members, as applicable, and Tier Two Members as stated above. In addition, the proposed rule change would address the loss allocation process as it relates to losses arising from or relating to multiple default or non-default events in a short period of time, also as described below.

Accordingly, FICC is proposing five (5) key changes to enhance each Division's loss allocation process:

(1) Changing the Calculation and Application of FICC's Corporate Contribution

As stated above, Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4 currently provide that FICC will contribute up to 25% of its retained earnings (or such higher amount as the Board of Directors shall determine) to a loss or liability that is not satisfied by the defaulting member's Clearing Fund deposit. Under the proposal, FICC would amend the calculation of its corporate contribution from a percentage of its retained earnings to a mandatory amount equal to 50% of the FICC General Business Risk Capital Requirement.[9] FICC's General Business Risk Capital Requirement, as defined in FICC's Clearing Agency Policy on Capital Requirements,[10] is, at a minimum, equal to the regulatory capital that FICC is required to maintain in compliance with Rule 17Ad–22(e)(15) under the Act.[11] The proposed Corporate Contribution (as defined below and in the proposed rule change) would be held in addition to FICC's General Business Risk Capital Requirement.

Currently, the Rules do not require FICC to contribute its retained earnings to losses and liabilities other than those from member defaults. Under the proposal, FICC would apply its corporate contribution to non-default losses as well. The proposed Corporate Contribution would apply to losses arising from Defaulting Member Events and Declared Non-Default Loss Events (as such terms are defined below and in the proposed rule change), and would be a mandatory contribution by FICC prior to any allocation of the loss among the applicable Division's members.[12] As proposed, if the Corporate Contribution is fully or partially used against a loss or liability relating to an Event Period by one or both Divisions, the Corporate Contribution would be reduced to the remaining unused amount, if any, during the following two hundred fifty (250) Business Days in order to permit FICC to replenish the Corporate Contribution.[13] To ensure transparency,

[8] GSD Rule 3B, Section 7 (Loss Allocation Obligations of CCIT Members) provides that CCIT Members will be allocated losses as Tier Two Members and will be responsible for the total amount of loss allocated to them. With respect to CCIT Members with a Joint Account Submitter, loss allocation will be calculated at the Joint Account level and then applied pro rata to each CCIT Member within the Joint Account based on the trade settlement allocation instructions. *Supra* note 5.

[9] FICC calculates its General Business Risk Capital Requirement as the amount equal to the greatest of (i) an amount determined based on its general business profile, (ii) an amount determined based on the time estimated to execute a recovery or orderly wind-down of FICC's critical operations, and (iii) an amount determined based on an analysis of FICC's estimated operating expenses for a six (6) month period.

[10] *See* Securities Exchange Act Release No. 81105 (July 7, 2017), 82 FR 32399 (July 13, 2017) (SR–FICC–2017–007).

[11] 17 CFR 240.17Ad–22(e)(15).

[12] The proposed rule change would not require a Corporate Contribution with respect to the use of each Division's Clearing Fund as a liquidity resource; however, if FICC uses a Division's Clearing Fund as a liquidity resource for more than 30 calendar days, as set forth in proposed Section 5 of GSD Rule 4 and MBSD Rule 4, then FICC would have to consider the amount used as a loss to the respective Division's Clearing Fund incurred as a result of a Defaulting Member Event and allocate the loss pursuant to proposed Section 7 of Rule 4, which would then require the application of FICC's Corporate Contribution.

[13] FICC believes that two hundred and fifth (250) Business Days would be a reasonable estimate of

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all GSD Members and MBSD Members would receive notice of any such reduction to the Corporate Contribution. There would be one FICC Corporate Contribution, the amount of which would be available to both Divisions and would be applied against a loss or liability in either Division in the order in which such loss or liability occurs, *i.e.,* FICC would not have two separate Corporate Contributions, one for each Division. In the event of a loss or liability relating to an Event Period, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, attributable to only one Division, the Corporate Contribution would be applied to that Division up to the amount then available. If a loss or liability relating to an Event Period, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, occurs simultaneously at both Divisions, the Corporate Contribution would be applied to the respective Divisions in the same proportion that the aggregate Average RFDs (as defined below and in the proposed rule change) of all members in that Division bear to the aggregate Average RFDs of all members in both Divisions.[14]

As compared to the current approach of applying ''up to'' a percentage of retained earnings to defaulting member losses, the proposed Corporate Contribution would be a fixed percentage of FICC's General Business Risk Capital Requirement, which would provide greater transparency and accessibility to members. The proposed Corporate Contribution would apply not only towards losses and liabilities arising out of or relating to Defaulting Member Events but also those arising out of or relating to Declared Non-Default Loss Events, which is consistent with the current industry guidance that ''a CCP should identify the amount of its own resources to be applied towards losses arising from custody and investment risk, to bolster confidence that participants' assets are prudently safeguarded.''[15]

Under current Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4, FICC has the discretion to contribute amounts higher than the specified percentage of retained earnings, as determined by the Board of Directors, to any loss or liability incurred by FICC as result of the failure of a Defaulting Member to fulfill its obligations to FICC. This option would be retained and expanded under the proposal so that it would be clear that FICC can voluntarily apply amounts greater than the Corporate Contribution against any loss or liability (including non-default losses) of the Divisions, if the Board of Directors, in its sole discretion, believes such to be appropriate under the factual situation existing at the time.

The proposed rule changes relating to the calculation and application of Corporate Contribution are set forth in proposed Sections 7 and 7a of GSD Rule 4 and Sections 7 and 7a of MBSD Rule 4, as further described below.

(2) Introducing an Event Period

In order to clearly define the obligations of each Division and its respective Members regarding loss allocation and to balance the need to manage the risk of sequential loss events against members' need for certainty concerning their maximum loss allocation exposures, FICC is proposing to introduce the concept of an ''Event Period'' to the GSD Rules and the MBSD Rules to address the losses and liabilities that may arise from or relate to multiple Defaulting Member Events and/or Declared Non-Default Loss Events that arise in quick succession in a Division. Specifically, the proposal would group Defaulting Member Events and Declared Non-Default Loss Events occurring in a period of ten (10) Business Days (''Event Period'') for purposes of allocating losses to Members of the respective Divisions in one or more rounds (as described below), subject to the limitations of loss allocation set forth in the proposed rule change and as explained below.[16] In the case of a loss or liability arising from or relating to a Defaulting Member Event, an Event Period would begin on the day one or both Divisions notify their respective members that FICC has ceased to act[17] for the GSD Defaulting Member and/or the MBSD Defaulting Member (or the next Business Day, if such day is not a Business Day). In the case of a loss or liability arising from or relating to a Declared Non-Default Loss Event, an Event Period would begin on the day that FICC notifies members of the respective Divisions of the Declared Non-Default Loss Event (or the next Business Day, if such day is not a Business Day). If a subsequent Defaulting Member Event or Declared Non-Default Loss Event occurs during an Event Period, any losses or liabilities arising out of or relating to any such subsequent event would be resolved as losses or liabilities that are part of the same Event Period, without extending the duration of such Event Period. An Event Period may include both Defaulting Member Events and Declared Non-Default Loss Events, and there would not be separate Event Periods for Defaulting Member Events or Declared Non-Default Loss Events occurring during overlapping ten (10) Business Day periods.

The amount of losses that may be allocated by each Division, subject to the required Corporate Contribution, and to which a Loss Allocation Cap would apply for any member that elects to withdraw from membership in respect of a loss allocation round, would include any and all losses from any Defaulting Member Events and any Declared Non-Default Loss Events during the Event Period, regardless of the amount of time, during or after the Event Period, required for such losses to be crystallized and allocated.[18]

The proposed rule changes relating to the implementation of an Event Period are set forth in proposed Section 7 of GSD Rule 4 and Section 7 of MBSD Rule 4, as further described below.

(3) Introducing the Concept of ''Rounds'' and Loss Allocation Notice

Pursuant to the proposed rule change, a loss allocation ''round'' would mean a series of loss allocations relating to an Event Period, the aggregate amount of which is limited by the sum of the Loss

the time frame that FICC would require to replenish the Corporate Contribution by equity in accordance with FICC's Clearing Agency Policy on Capital Requirements, including a conservative additional period to account for any potential delays and/or unknown exigencies in times of distress.

[14] FICC believes that if a loss or liability relating to an Event Period, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, occurs simultaneously at both Divisions, allocating the Corporate Contribution ratably between the two Divisions based on the aggregate Average RFDs of their respective members is appropriate because the aggregate Average RFDs of all members in a Division represent the amount of risks that those members bring to FICC over the look-back period of seventy (70) Business Days.

[15] *See Resilience of central counterparties (CCPs): Further guidance on the PFMI,* issued by the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions, at 42 (July 2017), *available at www.bis.org/cpmi/publ/d163.pdf.*

[16] FICC believes that having a ten (10) Business Day Event Period would provide a reasonable period of time to encompass potential sequential Defaulting Member Events or Declared Non-Default Loss Events that are likely to be closely linked to an initial event and/or a severe market dislocation episode, while still providing appropriate certainty for members concerning their maximum exposure to mutualized losses with respect to such events.

[17] *Supra* note 7.

[18] As discussed below, each Tier One Netting Member or Tier One Member, as applicable, that is a Tier One Netting Member or Tier One Member on the first day of an Event Period would be obligated to pay its pro rata share of losses and liabilities arising out of or relating to each Defaulting Member Event (other than a Defaulting Member Event with respect to which it is the Defaulting Member) and each Declared Non-Default Loss Event occurring during the Event Period.

Allocation Caps of affected Tier One Netting Members or Tier One Members, as applicable (a ''round cap''). When the aggregate amount of losses allocated in a round equals the round cap, any additional losses relating to the applicable Event Period would be allocated in one or more subsequent rounds, in each case subject to a round cap for that round. FICC may continue the loss allocation process in successive rounds until all losses from the Event Period are allocated among Tier One Netting Members or Tier One Members, as applicable, that have not submitted a Loss Allocation Withdrawal Notice (as defined below and in the proposed rule change) in accordance with proposed Section 7b of GSD Rule 4 or MBSD Rule 4.

Each loss allocation would be communicated to Tier One Netting Members or Tier One Members, as applicable, by the issuance of a notice that advises the Tier One Netting Members or Tier One Members, as applicable, of the amount being allocated to them (''Loss Allocation Notice''). Each Tier One Netting Member's or Tier One Member's, as applicable, pro rata share of losses and liabilities to be allocated in any round would be equal to (i) the average of its Required Fund Deposit for the seventy (70) business days preceding the first day of the applicable Event Period or such shorter period of time that the member has been a member (each member's ''Average RFD''), divided by (ii) the sum of Average RFD amounts of all members subject to loss allocation in such round.

Each Loss Allocation Notice would specify the relevant Event Period and the round to which it relates. The first Loss Allocation Notice in any first, second, or subsequent round would expressly state that such Loss Allocation Notice reflects the beginning of the first, second, or subsequent round, as the case may be, and that each Tier One Netting Member or Tier One Member, as applicable, in that round has five (5) Business Days from the issuance of such first Loss Allocation Notice for the round to notify FICC of its election to withdraw from membership with GSD or MBSD, as applicable, pursuant to proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, and thereby benefit from its Loss Allocation Cap.[19] The ''Loss Allocation Cap'' of a Tier One Netting Member or Tier One Member, as applicable, would be equal to the greater of (x) its Required Fund Deposit on the first day of the applicable Event Period and (y) its Average RFD.

After a first round of loss allocations with respect to an Event Period, only Tier One Netting Members or Tier One Members, as applicable, that have not submitted a Loss Allocation Withdrawal Notice in accordance with proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, would be subject to further loss allocation with respect to that Event Period.

The amount of any second or subsequent round cap may differ from the first or preceding round cap because there may be fewer Tier One Netting Members or Tier One Members, as applicable, in a second or subsequent round if Tier One Netting Members or Tier One Members, as applicable, elect to withdraw from membership with GSD or MBSD, as applicable, as provided in proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, following the first Loss Allocation Notice in any round.

For example, for illustrative purposes only, after the required Corporate Contribution, if FICC has a $5 billion loss determined with respect to an Event Period and the sum of Loss Allocation Caps for all Tier One Netting Members or Tier One Members, as applicable, subject to the loss allocation is $4 billion, the first round would begin when FICC issues the first Loss Allocation Notice for that Event Period. FICC could issue one or more Loss Allocation Notices for the first round until the sum of losses allocated equals $4 billion. Once the $4 billion is allocated, the first round would end and FICC would need a second round in order to allocate the remaining $1 billion of loss. FICC would then issue a Loss Allocation Notice for the $1 billion and this notice would be the first Loss Allocation Notice for the second round. The issuance of the Loss Allocation Notice for the $1 billion would begin the second round.

The proposed rule change would link the Loss Allocation Cap to a round in order to provide Tier One Netting Members or Tier One Members, as applicable, the option to limit their loss allocation exposure at the beginning of each round. As proposed and as described further below, a Tier One Netting Member or Tier One Member, as applicable, could limit its loss allocation exposure to its Loss Allocation Cap by providing notice of its election to withdraw from membership within five (5) Business Days after the issuance of the first Loss Allocation Notice in any round.

The proposed rule changes relating to the implementation of ''rounds'' and Loss Allocation Notices are set forth in proposed Section 7 of GSD Rule 4 and Section 7 of MBSD Rule 4, as further described below.

(4) Implementing a Revised ''Look-Back'' Period To Calculate a Member's Loss Allocation Pro Rata Share and Its Loss Allocation Cap

Currently, the GSD Rules and the MBSD Rules calculate a Tier One Netting Member's or a Tier One Member's pro rata share for purposes of loss allocation based on the member's average daily Required Fund Deposit over the prior twelve (12) months (or such shorter period as may be available in the case of a member which has not maintained a deposit over such time period). The Rules currently do not anticipate the possibility of more than one Defaulting Member Event or Declared Non-Default Loss Event in quick succession.

GSD and MBSD are proposing to calculate each Tier One Netting Member's or Tier One Member's, as applicable, pro rata share of losses and liabilities to be allocated in any round (as described above and in the proposed rule change) to be equal to (i) the member's Average RFD divided by (ii) the sum of Average RFD amounts for all members that are subject to loss allocation in such round.

Additionally, as described above and in the proposed rule change, if a Tier One Netting Member or Tier One Member, as applicable, withdraws from membership pursuant to proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, GSD and MBSD are proposing that the member's Loss Allocation Cap be equal to the greater of (i) its Required Fund Deposit on the first day of the applicable Event Period or (ii) its Average RFD.

FICC believes that employing a revised look-back period of seventy (70)

[19] Pursuant to current Section 7(g) of GSD Rule 4 and MBSD Rule 4, the time period for a member to give notice, pursuant to Section 13 of GSD Rule 3 and MBSD Rule 3, of its election to terminate its membership in GSD or MBSD, as applicable, in respect of an allocation arising from any Remaining Loss allocated by FICC pursuant to Section 7(d) of GSD Rule 4 or Section 7(e) of MBSD Rule 4, as applicable, and any Other Loss, is the Close of Business on the Business Day on which the loss allocation payment is due to FICC. Current Section 13 of GSD Rule 4 and MBSD Rule 4 requires a 10-day notice period. *Supra* note 5.

FICC believes that it is appropriate to shorten such time period from 10 days to five (5) Business Days because FICC needs timely notice of which Tier One Netting Members or Tier One Members, as applicable, would remain in its membership for purpose of calculating the loss allocation for any subsequent round. FICC believes that five (5) Business Days would provide Tier One Netting Members or Tier One Members, as applicable, with sufficient time to decide whether to cap their loss allocation obligations by withdrawing from their membership in GSD or MBSD, as applicable.

Business Days instead of twelve (12) months to calculate a Tier One Netting Member's or a Tier One Member's, as applicable, loss allocation pro rata share and Loss Allocation Cap is appropriate, because FICC recognizes that the current look-back period of twelve (12) months is a very long period during which a member's business strategy and outlook could have shifted significantly, resulting in material changes to the size of its portfolios. A look-back period of seventy (70) Business Days would minimize that issue yet still would be long enough to enable FICC to capture a full calendar quarter of such members' activities and smooth out the impact from any abnormalities and/or arbitrariness that may have occurred.

The proposed rule changes relating to the implementation of the revised look-back period are set forth in proposed Section 7 of GSD Rule 4 and Section 7 of MBSD Rule 4, as further described below.

(5) Capping Withdrawing Members' Loss Allocation Exposure and Related Changes

Currently, pursuant to Section 7(g) of GSD Rule 4 and MBSD Rule 4, a member can withdraw from membership in order to avail itself of a cap on loss allocation if the member notifies FICC via a written notice, in accordance with Section 13 of GSD Rule 3 or MBSD Rule 3, as applicable, of its election to terminate its membership. Such notice must be provided by the Close of Business on the Business Day on which the loss allocation payment is due to FICC and, if properly provided to FICC, would limit the member's liability for a loss allocation to its Required Fund Deposit for the Business Day on which the notification of allocation is provided to the member.[20] As discussed above, the proposed rule change would continue providing members the opportunity to limit their loss allocation exposure by offering withdrawal options; however, the cap on loss allocation would be calculated differently and the associated withdrawal process would also be modified as it relates to withdrawals associated with the loss allocation process. In particular, the proposed rule change would shorten the withdrawal notification period from 10 days to five (5) Business Days, as further described below.

As proposed, if a member timely provides notice of its withdrawal from membership in respect of a loss allocation round, the maximum amount of losses it would be responsible for would be its Loss Allocation Cap,[21] provided that the member complies with the requirements of the withdrawal process in proposed Section 7b of GSD Rule 4 and Section 7b of MBSD Rule 4.

Currently, pursuant to Section 7(g) of GSD Rule 4 and MBSD Rule 4, if notification is provided to a member that an allocation has been made against the member pursuant to GSD Rule 4 or MBSD Rule 4, as applicable, and that application of the member's Required Fund Deposit is not sufficient to satisfy such obligation to make payment to FICC, the member is required to deliver to FICC by the Close of Business on the next Business Day, or by the Close of Business on the Business Day of issuance of the notification if so determined by FICC, that amount which is necessary to eliminate any such deficiency, unless the member elects to terminate its membership in FICC. To increase transparency of the timeframe under which FICC would require funds from members to satisfy their loss allocation obligations, FICC is proposing that members would receive two (2) Business Days' notice of a loss allocation, and members would be required to pay the requisite amount no later than the second Business Day following issuance of such notice.[22] Members would have five (5) Business Days[23] from the issuance of the first Loss Allocation Notice in any round of an Event Period to decide whether to withdraw from membership.

Each round would allow a Tier One Netting Member or Tier One Member, as applicable, the opportunity to notify FICC of its election to withdraw from membership after satisfaction of the losses allocated in such round. Multiple Loss Allocation Notices may be issued with respect to each round to allocate losses up to the round cap.

Specifically, the first round and each subsequent round of loss allocation would allocate losses up to a round cap of the aggregate of all Loss Allocation Caps of those Tier One Netting Members or Tier One Members, as applicable, included in the round. If a Tier One Netting Member or Tier One Member, as applicable, provides notice of its election to withdraw from membership, it would be subject to loss allocation in that round, up to its Loss Allocation Cap. If the first round of loss allocation does not fully cover FICC's losses, a second round will be noticed to those members that did not elect to withdraw from membership in the previous round; however, as noted above, the amount of any second or subsequent round cap may differ from the first or preceding round cap because there may be fewer Tier One Netting Members or Tier One Members, as applicable, in a second or subsequent round if Tier One Netting Members or Tier One Members, as applicable, elect to withdraw from membership with GSD or MBSD, as applicable, as provided in proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, following the first Loss Allocation Notice in any round.

Pursuant to the proposed rule change, in order to avail itself of its Loss Allocation Cap, a Tier One Netting Member or Tier One Member, as applicable, would need to follow the requirements in proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, which would provide that the Tier One Netting Member or Tier One Member, as applicable, must: (i) Specify in its Loss Allocation Withdrawal Notice an effective date of withdrawal, which date shall not be prior to the scheduled final settlement date of any remaining obligations owed by the member to FICC, unless otherwise approved by FICC, and (ii) as of the time of such member's submission of the Loss Allocation Withdrawal Notice, cease submitting transactions to FICC for processing, clearance or settlement, unless otherwise approved by FICC.

As proposed, a Tier One Netting Member or a Tier One Member, as applicable, that withdraws in compliance with proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, would remain obligated for its pro rata share of losses and liabilities with respect to any Event Period for which it is otherwise obligated under GSD Rule 4 or MBSD Rule 4, as applicable; however, its aggregate obligation would be limited to the amount of its Loss Allocation Cap (as fixed in the round for which it withdrew).

The proposed rule changes are designed to enable FICC to continue the loss allocation process in successive rounds until all of FICC's losses are allocated. To the extent that the Loss Allocation Cap of a Tier One Netting Member or Tier One Member, as applicable, exceeds such member's

[20] Current Section 13 of GSD Rule 3 and MBSD Rule 3 requires a member to provide FICC with 10 days written notice of the member's termination; however, FICC, in its discretion, may accept such termination within a shorter notice period. *Supra* note 5.

[21] If a member's Loss Allocation Cap exceeds the member's then-current Required Fund Deposit, it must still cover the excess amount.

[22] FICC believes that allowing members two (2) Business Days to satisfy their loss allocation obligations would provide Members sufficient notice to arrange funding, if necessary, while allowing FICC to address losses in a timely manner.

[23] *Supra* note 19.

Required Fund Deposit on the first day of an Event Period, FICC may in its discretion retain any excess amounts on deposit from the member, up to the Loss Allocation Cap of a Tier One Netting Member or Tier One Member, as applicable.

The proposed rule changes relating to capping withdrawing members' loss allocation exposure and related changes to the withdrawal process are set forth in proposed Sections 7 and 7b of GSD Rule 4 and Sections 7 and 7b of MBSD Rule 4, as further described below.

B. Changes To Align Loss Allocation Rules

The proposed rule changes would align the loss allocation rules, to the extent practicable and appropriate, of the three DTCC Clearing Agencies so as to provide consistent treatment, especially for firms that are participants of two or more DTCC Clearing Agencies. As proposed, the loss allocation waterfall and certain related provisions, *e.g.,* returning a former member's Clearing Fund, would be consistent across the DTCC Clearing Agencies to the extent practicable and appropriate. The proposed rule changes of FICC that would align loss allocation rules of the DTCC Clearing Agencies are set forth in proposed Sections 1, 5, 6, 10, and 11 of GSD Rule 4 and MBSD Rule 4, as further described below.

C. Clarifying Changes Relating to Loss Allocation

The proposed rule changes are intended to make the provisions in the Rules governing loss allocation more transparent and accessible to members. In particular, FICC is proposing the following changes relating to loss allocation to clarify members' obligations for Declared Non-Default Loss Events.

Aside from losses that FICC might face as a result of a Defaulting Member Event, FICC could incur non-default losses incident to each Division's clearance and settlement business.[24] The GSD Rules and the MBSD Rules currently permit FICC to apply Clearing Fund to non-default losses.[25] Section 5 of GSD Rule 4 and MBSD Rule 4 provides that the use of Clearing Fund deposits is limited to satisfaction of losses or liabilities of FICC, which includes losses or liabilities that are otherwise incident to the operation of the clearance and settlement business of FICC, although the application of Clearing Fund to such losses or liabilities is more limited under MBSD Rule 4 when compared to GSD Rule 4.[26] Section 7(f) of GSD Rule 4 and MBSD Rule 4 provides that any loss or liability incurred by the Corporation incident to its clearance and settlement business arising other than from a Remaining Loss shall be allocated among Tier One Netting Members or Tier One Members, as applicable, ratably, in accordance with their Average Required Clearing Fund Deposits.[27]

If there is a failure of FICC following a non-default loss, such occurrence would affect members in much the same way as a failure of FICC following a Defaulting Member Event. Accordingly, FICC is proposing rule changes to enhance the provisions relating to non-default losses by clarifying members' obligations for such losses and aligning the non-default loss provisions in the GSD Rules and the MBSD Rules.

Specifically, for both the GSD Rules and the MBSD Rules, FICC is proposing enhancement of the governance around non-default losses that would trigger loss allocation to Tier One Netting Members or Tier One Members, as applicable, by specifying that the Board of Directors would have to determine that there is a non-default loss that may be a significant and substantial loss or liability that may materially impair the ability of FICC to provide clearance and settlement services in an orderly manner and will potentially generate losses to be mutualized among the Tier One Netting Members or Tier One Members, as applicable, in order to ensure that FICC may continue to offer clearance and settlement services in an orderly manner. The proposed rule change would provide that FICC would then be required to promptly notify members of this determination (a ''Declared Non-Default Loss Event''). In addition, FICC is proposing to better align the interest of FICC with those of its members by stipulating a mandatory Corporate Contribution apply to a Declared Non-Default Loss Event prior to any allocation of the loss among members, as described above. Additionally, FICC is proposing language to clarify members' obligations for Declared Non-Default Loss Events.

Under the proposal, FICC would clarify the Rules of both Divisions to make clear that Tier One Netting Members or Tier One Members, as applicable, are subject to loss allocation for non-default losses (*i.e.,* Declared Non-Default Loss Events under the proposal) and Tier Two Members are not subject to loss allocation for non-default losses.

The proposed rule changes relating to Declared Non-Default Loss Events and members' obligations for such events are set forth in proposed Section 7 of GSD Rule 4 and Section 7 of MBSD Rule 4, as further described below.

D. Amending Language Regarding FICC's Use of MBSD Clearing Fund

The proposed rule change would delete language currently in Section 5 of MBSD Rule 4 that limits certain uses by FICC of the MBSD Clearing Fund to ''unexpected or unusual'' requirements for funds that represent a ''small percentage'' of the MBSD Clearing Fund. FICC believes that these limiting phrases (which appear in connection with FICC's use of MBSD Clearing Fund to cover losses and liabilities incident to its clearance and settlement business outside the context of an MBSD Defaulting Member Event as well as to cover certain liquidity needs) are vague and imprecise, and should be replaced in their entirety. Specifically, FICC is proposing to delete the limiting language with respect to FICC's use of MBSD Clearing Fund to cover losses and liabilities incident to its clearance and settlement business outside the context of an MBSD Defaulting Member Event so as to not have such language be interpreted as impairing FICC's ability to access the MBSD Clearing Fund in order to manage non-default losses. FICC is also proposing to delete

[24] Non-default losses may arise from events such as damage to physical assets, a cyber-attack, or custody and investment losses.

[25] Arguably there is an ambiguity created by the first paragraph of Section 7 in both GSD Rule 4 and MBSD Rule 4, which suggests that losses or liabilities may only be allocated in a member default scenario, while Section 5 in both GSD Rule 4 and MBSD Rule 4 makes it clear that the applicable Division's Clearing Fund may be used to satisfy non-default losses.

[26] Section 5 of GSD Rule 4 provides that ''The use of the Clearing Fund deposits shall be limited to satisfaction of losses or liabilities of the Corporation . . . otherwise incident to the clearance and settlement business of the Corporation . . .'' *Supra* note 5.

Section 5 of MBSD Rule 4 provides that ''The use of the Clearing Fund deposits and assets and property on which the Corporation has a lien on shall be limited to satisfaction of losses or liabilities of the Corporation . . . otherwise incident to the clearance and settlement business of the Corporation with respect to losses and liabilities to meet unexpected or unusual requirements for funds that represent a small percentage of the Clearing Fund. . .'' *Supra* note 5.

[27] Section 7(f) of GSD Rule 4 provides that ''Any loss or liability incurred by the Corporation incident to its clearance and settlement business . . . arising other than from a Remaining Loss (hereinafter, an ''Other Loss'') shall be allocated among Tier One Netting Members, ratably, in accordance with the respective amounts of their Average Required FICC Clearing Fund Deposits. *Supra* note 5.

Section 7(f) of MBSD Rule 4 provides that ''Any loss or liability incurred by the Corporation incident to its clearance and settlement business . . . arising other than from a Remaining Loss (hereinafter, an ''Other Loss''), shall be allocated among Tier One Members, ratably, in accordance with the respective amounts of their Average Required Clearing Fund Deposits. *Supra* note 5.

the limiting language with respect to FICC's use of MBSD Clearing Fund to cover certain liquidity needs because the effect of the limitation in this context is confusing and unclear.

The proposed rule changes relating to FICC's use of MBSD Clearing Fund are set forth in proposed Section 5 of MBSD Rule 4, as further described below.

The foregoing changes as well as other changes (including a number of conforming and technical changes) that FICC is proposing in order to improve the transparency and accessibility of the Rules are described in detail below.

E. Loss Allocation Waterfall Comparison

The following example [28] illustrates the differences between the current and proposed loss allocation provisions:

Assumptions

(i) Firms A, B, and X are each a GSD Netting Member and an MBSD Clearing Member and are referred to as Member A, Member B, and Member X, respectively.

(ii) Member A defaults on a Business Day (Day 1). On the same day, FICC ceases to act for Member A and notifies members of the cease to act. After liquidating Member A's portfolio and applying Member A's Clearing Fund deposit, FICC has a total loss of $350 million, with $200 million in GSD and $150 million in MBSD.

(iii) Member X voluntarily retires from membership five (5) Business Days after FICC ceases to act for Member A (Day 6).

(iv) Member B defaults seven (7) Business Days after FICC ceases to act for Member A (Day 8). On the same day, FICC ceases to act for Member B and notifies members of the cease to act. After liquidating Member B's portfolio and applying Member B's Clearing Fund deposit, FICC has a total loss of $350 million, with $200 million in GSD and $150 million in MBSD.

(v) The current FICC loss provisions require FICC to contribute up to 25% of its retained earnings as a corporate contribution. For the purposes of this example, it is assumed that FICC will contribute 25% of its retained earnings. The amount of FICC's retained earnings is $176 million.

(vi) FICC's General Business Risk Capital Requirement is $98 million.

Current Loss Allocation

Under the current loss allocation provisions, with respect to the losses arising out of Member A's default, FICC will contribute a total of $44 million ($176 million * 25%) from retained earnings,[29] with approximately $25 million ($44 million* ($200 million/$350 million)) for GSD and approximately $19 million ($44 million* ($150 million/$350 million)) for MBSD. FICC will then allocate the remaining GSD loss of $175 million ($200 million − $25 million) to GSD Tier One Netting Members and the remaining MBSD loss of $131 million ($150 million − $19 million) to MBSD Tier One Members.

With respect to losses arising out of Member B's default, FICC will contribute a total of approximately $33 million (($176 million − $44 million) * 25%) from retained earnings, with approximately $19 million ($33 million * ($200 million/$350 million)) for GSD and approximately $14 million ($33 million * ($150 million/$350 million)) for MBSD. FICC will then allocate the remaining GSD loss of $181 million ($200 million − $19 million) to GSD Tier One Netting Members and the remaining MBSD loss of $136 million ($150 million − $14 million) to MBSD Tier One Members.

Altogether, with respect to losses arising out of defaults of Member A and Member B, FICC will contribute a total of approximately $77 million of retained earnings, with approximately $44 million for GSD and approximately $33 million for MBSD. FICC will allocate losses of $356 million to GSD Tier One Netting Members and $267 million to MBSD Tier One Members.

Proposed Loss Allocation

Under the proposed loss allocation provisions, a Defaulting Member Event with respect to Member A's default would have occurred on Day One, and a Defaulting Member Event with respect to Member B's default would have occurred on Day 8. Because the Defaulting Member Events occurred during a 10-business day period, they would be grouped together into an Event Period for purposes of allocating losses to members. The Event Period would begin on the 1st business day and end on the 10th business day.

With respect to losses arising out of Member A's default, FICC would apply a Corporate Contribution of $49 million ($98 million * 50%),[30] with approximately $32 million ($49 million * ($10 billion/$15.2 billion)) for GSD and approximately $17 million ($49 million * ($5.2 billion/$15.2 billion)) for MBSD. FICC would then allocate the remaining GSD loss of $168 million ($200 million − $32 million) to GSD Tier One Netting Members and the remaining MBSD loss of $133 million ($150 million − $17 million) to MBSD Tier One Members. With respect to losses arising out of Member B's default, FICC would not apply a Corporate Contribution since it would have already contributed the maximum Corporate Contribution of 50% of its General Business Risk Capital Requirement. With respect to losses arising out of Member B's default, FICC would allocate the GSD loss of $200 million to GSD Tier One Netting Members and the MBSD loss of $150 million to MBSD Tier One Members. Because Member X was a member in both Divisions on the first day of the Event Period, Member X would be subject to loss allocation with respect to all events occurring during the Event Period, even if the event occurred after its retirement. Therefore, Member X would be subject to loss allocation with respect to Member B's default.

Altogether, with respect to losses arising out of defaults of Member A and Member B, FICC would apply a Corporate Contribution of $49 million, with approximately $32 million for GSD and approximately $17 million for MBSD. FICC would allocate losses of $368 million to GSD Tier One Netting Members and $283 million to MBSD Tier One Members.

The principal differences in the above example are due to (i) the proposed changes to the calculation and application of the Corporate Contribution and (ii) the proposed introduction of an Event Period.

(ii) Detailed Description of the Proposed Rule Changes Related to Loss Allocation

A. Proposed Changes to GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation)

Overview of GSD Rule 4 and MBSD Rule 4

GSD Rule 4 and MBSD Rule 4 currently address Clearing Fund requirements and loss allocation obligations, as well as permissible uses of the Clearing Fund. These Rules address the various Clearing Fund calculations for each Division's Clearing

[28] For purposes of this example, FICC has assumed that no losses have arisen that apply to Tier Two Netting Members, Tier Two Members, or CCIT Members.

[29] The retained earnings are applied to the respective Divisions in the same proportion that the losses of that Division bear to the total losses of both Divisions.

[30] The Corporate Contribution would be applied to the respective Divisions in the same proportion that the aggregate Average RFDs of all members in that Division bear to the aggregate Average RFDs of all members in both Divisions. For the purposes of this example, FICC has assumed that the aggregate Average RFDs of all GSD members is $10 billion and the aggregate Average RFDs of all MBSD members is $5.2 billion.

Fund and set forth rights, obligations and other aspects associated with each Division's Clearing Fund, as well as each Division's loss allocation process. GSD Rule 4 and MBSD Rule 4 are each currently organized into 12 sections. Sections of these Rules that FICC is proposing to change are described below.

Section 1 of GSD Rule 4 and MBSD Rule 4

Currently, Section 1 of GSD Rule 4 and MBSD Rule 4 set forth the requirement that each GSD Netting Member and each MBSD Clearing Member make and maintain a deposit to the Clearing Fund at the minimum level set forth in the respective Rule 4 and note that the timing of such payment is set forth in another section of the respective Rule 4. Current Section 1 of the respective rule also provides that the deposits to the Clearing Fund will be held by FICC or its designated agents. Current Section 1 of MBSD Rule 4 also defines the term ''Transaction'' for purposes of MBSD Rule 4 and references a Member's obligation to replenish the deficit in its Required Fund Deposit if it is charged by FICC under certain circumstances.

FICC is proposing to rename the subheading of Section 1 of Rule 4 in both the GSD Rules and MBSD Rules from ''General'' to ''Required Fund Deposits'' and to restructure the wording of the provisions for clarity and readability.

Under the proposed rule change, Section 1 of GSD Rule 4 and Section 1 of MBSD Rule 4 would continue to have the same provisions as they relate to Netting Members or Clearing Members, as applicable, except for the following: (i) The language throughout the sections would be reorganized, streamlined and clarified, and (ii) language would be added regarding additional deposits maintained by the Netting Members or Clearing Members, as applicable, at FICC, and highlight for members that such additional deposits would be deemed to be part of the Clearing Fund and the member's Actual Deposit (as discussed below and as defined in the proposed rule change) but would not be deemed to be part of the member's Required Fund Deposit.

The proposed language regarding maintenance of a member's Actual Deposit would also make it clear that FICC will not be required to segregate such deposit, but shall maintain books and records concerning the assets that constitute each member's Actual Deposit.

In addition, FICC proposes a technical change to update a cross reference in Section 1 of GSD Rule 4 and MBSD Rule 4.

Furthermore, in Section 1 of MBSD Rule 4, FICC is proposing to move the definition of ''Transactions'' to proposed Section 2(a) of MBSD Rule 4, where the first usage of ''Transactions'' in MBSD Rule 4 appears. FICC is also proposing to delete the last sentence in Section 1 of MBSD Rule 4, which references a Member's obligation to replenish the deficit in its Required Fund Deposit if it is charged by FICC under certain circumstances, because it would no longer be relevant under the proposed rule change to Section 7 of MBSD Rule 4, as FICC would require members to pay their loss allocation amounts instead of charging their Required Fund Deposits for Clearing Fund losses.

Section 2 of GSD Rule 4 and MBSD Rule 4

Current Section 2 of GSD Rule 4 and MBSD Rule 4 set forth more detailed requirements pertaining to members' Required Fund Deposits. FICC is proposing to rename the subheadings in these sections from ''Required Fund Deposit'' to ''Required Fund Deposit Requirements'' in order to better reflect the purpose of this section.

In addition, FICC is proposing to expand the definition of ''Legal Risk'' in both the GSD and MBSD provisions (current Section 2(e) of GSD Rule 4 and Section 2(f) of MBSD Rule 4) by revising the parameters of Legal Risk so that it would not be limited to laws applicable to a member's insolvency or bankruptcy, as FICC believes that Legal Risk may arise outside the context of an insolvency or bankruptcy event regarding a member, and FICC should be permitted to adequately protect itself in those non- insolvency/bankruptcy circumstances as well.

For better organization of Rule 4, FICC is also proposing to relocate the provision on minimum Clearing Fund cash requirements (current Section 2(b) of GSD Rule 4 and Section 2(d) of MBSD Rule 4) to the section in each of GSD Rule 4 and MBSD Rule 4 dealing specifically with the form of Clearing Fund deposits (proposed Section 3 of GSD Rule 4 and MBSD Rule 4). This would necessitate the re-lettering of the provisions in Section 2. In addition, as stated above, the provision regarding the definition of ''Transactions'' for purposes of MBSD Rule 4 would be moved to proposed Section 2(a) from current Section 1.

FICC is proposing technical changes to correct typographical errors in current Section 2 of GSD Rule 4.

Sections 3, 3a and 3b of GSD Rule 4 and MBSD Rule 4

Currently, Sections 3, 3a and 3b of GSD Rule 4 and MBSD Rule 4 address the permissible form of Clearing Fund deposits and contain detailed requirements regarding each form. FICC is proposing changes to improve the readability of these sections.

In addition, for better organization of the subject matter, FICC is proposing to move certain paragraphs from one section to another, including (i) moving clauses (b) and (d) in current Section 2 of GSD Rule 4 and MBSD Rule 4, respectively, to proposed Section 3 of GSD Rule 4 and MBSD Rule 4 and (ii) moving the last paragraph of current Section 3 in GSD Rule 4 and MBSD Rule 4 to proposed Section 3b of GSD Rule 4 and MBSD Rule 4.

Under the proposed rule change, FICC is also proposing to update the cash investment provision in Section 3a of GSD Rule 4 and MBSD Rule 4 to reflect the Clearing Agency Investment Policy adopted by FICC [31] and to define Clearing Fund Cash as (i) cash deposited by a Netting Member or Clearing Member, as applicable, as part of its Actual Deposit, (ii) the proceeds of (x) any loans made to FICC secured by the pledge by FICC of Eligible Clearing Fund Securities pledged to FICC or (y) any sales of Eligible Clearing Fund Securities pledged to FICC, (iii) cash receipts from any investment of, repurchase or reverse repurchase agreements relating to, or liquidation of, Clearing Fund assets, and (iv) cash payments on Eligible Letters of Credit. Lastly, FICC is proposing technical changes to correct typographical errors in current Section 3 of MBSD Rule 4 and current Section 3b of GSD Rule 4.

[31] *See* Securities Exchange Act Release No. 79528 (December 12, 2016), 81 FR 91232 (December 16, 2016) (SR–FICC–2016–005). The Clearing Agency Investment Policy (the ''Policy'') governs the management, custody, and investment of cash deposited to the GSD and MBSD Clearing Funds, the proprietary liquid net assets (cash and cash equivalents) of FICC and other funds held by FICC. The Policy sets forth guiding principles for the investment of those funds, which include adherence to a conservative investment philosophy that places the highest priority on maximizing liquidity and avoiding risk, as well as mandating the segregation and separation of funds. The Policy also addresses the process for evaluating credit ratings of counterparties and identifies permitted investments within specified parameters. In general, assets are required to be held by regulated and creditworthy financial institution counterparties and invested in financial instruments that, with respect to the GSD and MBSD Clearing Funds, may include deposits with banks, including the Federal Reserve Bank of New York, collateralized reverse-repurchase agreements, direct obligations of the U.S. government and money-market mutual funds.

Section 4 of GSD Rule 4 and MBSD Rule 4

Currently, Section 4 of GSD Rule 4 and MBSD Rule 4 address the granting of a first priority perfected security interest by each Netting Member or Clearing Member, as applicable, in all assets and property placed by the member in the possession of FICC (or its agents acting on its behalf). FICC is not proposing any substantive changes to these sections except for streamlining the provisions for readability and clarity, and adding ''Actual Deposit'' as a defined term to refer to Eligible Clearing Fund Securities, funds and assets pledged to FICC to secure any and all obligations and liabilities of a Netting Member or a Clearing Member, as applicable, to FICC.

Section 5 of GSD Rule 4 and MBSD Rule 4

Currently, Section 5 of GSD Rule 4 and MBSD Rule 4 describe the use of each Division's Clearing Fund. FICC is proposing to rename the subheading of this section from ''Use of Deposits and Payments'' to ''Use of Clearing Fund'' to better reflect the purpose of the section.

Under the proposed rule change, FICC is also proposing changes to streamline this section for clarity and readability and to align the GSD Rules and MBSD Rules. Specifically, FICC is proposing to delete the first paragraph of current Section 5 of GSD Rule 4 and MBSD Rule 4 and replace it with clearer language that sets forth the permitted uses of each Division's Clearing Fund. Specifically, the proposed Section 5 of GSD Rule 4 and MBSD Rule 4 provides that each Division's Clearing Fund would only be used by FICC (i) to secure each member's performance of obligations to FICC, including, without limitation, each member's obligations with respect to any loss allocations as set forth in proposed Section 7 of GSD Rule 4 and MBSD Rule 4 and any obligations arising from a Cross-Guaranty Agreement pursuant to GSD Rule 41 or MBSD Rule 32, as applicable, or a Cross-Margining Agreement pursuant to GSD Rule 43, (ii) to provide liquidity to FICC to meet its settlement obligations, including, without limitation, through the direct use of cash in the GSD Clearing Fund or MBSD Clearing Fund, as applicable, or through the pledge or rehypothecation of pledged Eligible Clearing Fund Securities in order to secure liquidity, and (iii) for investment as set forth in proposed Section 3a of GSD Rule 4 and MBSD Rule 4.

The current first paragraph of Section 5 of GSD Rule 4 and MBSD Rule 4 provides that if FICC pledges, hypothecates, encumbers, borrows, or applies any part of the respective Division's Clearing Fund deposits to satisfy any liability, obligation, or liquidity requirements for more than thirty (30) days, FICC, at the Close of Business on the 30th day (or on the first Business Day thereafter) will consider the amount used as an actual loss to the respective Division's Clearing Fund and immediately allocate such loss in accordance with Section 7 of GSD Rule 4 or MBSD Rule 4, as applicable. As proposed, FICC would retain this provision conceptually but replace it with clearer and streamlined language that provides that each time FICC uses any part of the respective Division's Clearing Fund for more than 30 calendar days to provide liquidity to FICC to meet its settlement obligations, including, without limitation, through the direct use of cash in the Clearing Fund or through the pledge or rehypothecation of pledged Eligible Clearing Fund Securities in order to secure liquidity, FICC, at the Close of Business on the 30th calendar day (or on the first Business Day thereafter) from the day of such use, would consider the amount used but not yet repaid as a loss to the Clearing Fund incurred as a result of a Defaulting Member Event and immediately allocate such loss in accordance with proposed Section 7 of GSD Rule 4 or MBSD Rule 4, as applicable.

The proposed rule change also includes deleting language currently in Section 5 of MBSD Rule 4 that limits certain uses by FICC of the MBSD Clearing Fund to ''unexpected or unusual'' requirements for funds that represent a ''small percentage'' of the MBSD Clearing Fund. FICC believes that these limiting phrases (which appear in connection with FICC's use of MBSD Clearing Fund to cover losses and liabilities incident to its clearance and settlement business outside the context of an MBSD Defaulting Member Event as well as to cover certain liquidity needs) are vague and imprecise, and should be replaced in their entirety. Specifically, FICC is proposing to delete the limiting language with respect to FICC's use of MBSD Clearing Fund to cover losses and liabilities incident to its clearance and settlement business outside of an MBSD Defaulting Member Event so as to not have such language be interpreted as impairing FICC's ability to access the MBSD Clearing Fund in order to manage non-default losses. FICC is also proposing to delete the limiting language with respect to FICC's use of MBSD Clearing Fund to cover certain liquidity needs because the effect of the limitation in this context is confusing and unclear.

In addition, FICC is proposing to delete the last paragraph in current Section 5 of GSD Rule 4 and MBSD Rule 4 because these paragraphs address the application of a member's deposits to the applicable Clearing Fund to cover the allocation of a loss or liability incurred by FICC. These paragraphs would no longer be relevant, because, under the proposed Section 7 of GSD Rule 4 and MBSD Rule 4 (discussed below), FICC would not apply the member's deposit to the Clearing Fund unless the member does not satisfy payment of its allocated loss amount within the required timeframe. These paragraphs also currently include provisions regarding other agreements, such as a Cross-Guaranty Agreement, that pertain to a Defaulting Member, and such provisions would now be covered by proposed Section 6 of GSD Rule 4 and MBSD Rule 4.

Section 6 of GSD Rule 4 and MBSD Rule 4

Currently, Section 6 of GSD Rule 4 and MBSD Rule 4 are reserved for future use. FICC is proposing to use this section for provisions relating to the application of deposits to the respective Division's Clearing Fund and other amounts held by FICC to a Defaulting Member's obligations.

FICC is proposing to add a subheading of ''Application of Clearing Fund Deposits and Other Amounts to Defaulting Members' Obligations'' to Section 6 of GSD Rule 4 and MBSD Rule 4. Under the proposed rule change, for better organization by subject matter, FICC is also proposing to relocate certain provisions to these sections from the respective current Section 7 of GSD Rule 4 and MBSD Rule 4, which addresses FICC's application of Clearing Fund deposits and other assets held by FICC securing a Defaulting Member's obligations to FICC.

For additional clarity and for consistency with the loss allocation rules of the other DTCC Clearing Agencies, FICC proposes to add a provision which makes it clear that, if FICC applies a Defaulting Member's Clearing Fund deposits, FICC may take any and all actions with respect to the Defaulting Member's Actual Deposits, including assignment, transfer, and sale of any Eligible Clearing Fund Securities, that FICC determines is appropriate.

Sections 7, 7a and 7b of GSD Rule 4 and MBSD Rule 4

Current Section 7 of GSD Rule 4 and MBSD Rule 4 contains FICC's current loss allocation waterfall for losses or

liabilities incurred by FICC. With respect to any loss or liability incurred by FICC as the result of the failure of a Defaulting Member to fulfill its obligations to FICC, the loss allocation waterfall for each Division currently provides:

(i) Application of any Clearing Fund deposits and other collateral held by FICC securing a Defaulting Member's obligations to FICC and additional resources as are applicable to the Defaulting Member.

(ii) If a loss or liability remains after the application of the Defaulting Member's collateral and resources, FICC would apply up to 25% of FICC's existing retained earnings, or such higher amount as the Board of Directors determines.

(iii) If a loss or liability still remains after the application of the retained earnings, FICC would apply the loss or liability to members as follows:

(a) If the remaining loss or liability is attributable to Tier One Netting Members or Tier One Members, as applicable, then FICC will allocate such loss or liability to Tier One Netting Members or Tier One Members, as applicable, by assessing the Required Fund Deposit maintained by each such member an amount up to $50,000, in an equal basis per Tier One Netting Member or Tier One Member, as applicable.

(b) If the remaining loss or liability is attributable to Tier Two Members, then FICC will allocate such loss or liability to Tier Two Members based upon their trading activity with the Defaulting Member that resulted in a loss.

(iv) If there is any loss or liability that still remains after the application of (ii) and (iii) above that is attributable to Tier One Netting Members or Tier One Members, as applicable, then FICC will allocate such loss or liability among Tier One Netting Members or Tier One Members, as applicable, ratably based on the amount of each Tier One Netting Member's or Tier One Member's Required Fund Deposit and based on the average daily level of such deposit over the prior twelve (12) months (or such shorter period as may be available if the member has not maintained a deposit over such time period).

Current Section 7(f) of GSD Rule 4 and MBSD Rule 4 also provides that Other Losses shall be allocated among Tier One Netting Members or Tier One Members, as applicable, ratably in accordance with the respective amounts of each Tier One Netting Member's or Tier One Member's Required Fund Deposit and based on the average daily level of such deposit over the prior twelve (12) months (or such shorter period as may be available if the member has not maintained a deposit over such time period).

Currently, pursuant to Section 7(e) of GSD Rule 4, an Inter-Dealer Broker Netting Member, or a Non-IDB Repo Broker with respect to activity in its Segregated Broker Account, will not be subject to an aggregate allocation loss for any single loss-allocation event that exceeds $5 million. FICC believes that it is appropriate for GSD to retain this cap under the proposed rule change because the Inter-Dealer Broker Netting Members are required to limit their business as provided in Section 8(e) of GSD Rule 3, which would in turn minimize the potential losses or liabilities that could be incurred by FICC from Inter-Dealer Broker Netting Members.[32] FICC believes that it is also appropriate for GSD to retain this cap under the proposed rule change for Non-IDB Repo Brokers because their activity in their respective Segregated Broker Accounts would be subject to similar limitations as the Inter-Dealer Broker Netting Members. However, the proposal would apply the cap to an Event Period instead of a single loss event in order to conform with the concept of the Event Period under the proposal. FICC believes applying the cap to an Event Period would continue to reasonably represent the risk profiles of the Inter-Dealer Broker Netting Members, and Non-IDB Repo Brokers with respect to their Segregated Broker Accounts, because they submit affirmed trades from their systems to GSD, with each trade already matched to the counterparty that will ultimately deliver or receive the securities. Therefore, Inter-Dealer Broker Netting Members, and Non-IDB Repo Brokers with respect to their Segregated Broker Accounts, do not generally maintain positions with FICC and present minimal risk to FICC. FICC is also proposing technical changes to replace (i) the term ''Segregated Broker Account'' with ''Segregated Repo Account'' and (ii) the term ''Non-IDB Broker'' with ''Non-IDB Repo Broker,'' both of which are the correct terms defined in GSD Rule 1.

Current Section 7(g) of GSD Rule 4 and MBSD Rule 4 further provides that if the Required Fund Deposit of the member being allocated the loss is not sufficient to satisfy its loss allocation obligation, the member is required to deliver to FICC an amount that is necessary to eliminate the deficiency by the Close of Business on the next Business Day, or by the Close of Business on the Business Day of issuance of the notification if so determined by FICC. Under the current Rules, a member may elect to terminate its membership, which would limit its loss allocation to the amount of its Required Fund Deposit for the Business Day on which the notification of such loss allocation is provided to the member. If the member does not elect to terminate its membership and fails to satisfy its Required Fund Deposit within the timeframe specified in the Rules, FICC will cease to act generally with regard to such member pursuant to GSD Rules 21 and 22A or MBSD Rules 14 and 17, as applicable, and may take disciplinary action against such member pursuant to GSD Rule 48 or MBSD Rule 38, as applicable.

Current Section 7(h) of GSD Rule 4 and MBSD Rule 4 requires FICC to promptly notify members and the Commission of the amount involved and the causes if a Remaining Loss or Other Loss occurs. In addition, current Section 7(i) of GSD Rule 4 and MBSD Rule 4 also provides that any increase in Clearing Fund deposit as required by subsection (f) of current Section 2 of GSD Rule 4 or provisions of MBSD Rule 4 regarding special charges or other premiums will not be taken into account when calculating loss allocation based on a GSD Member's Average Required FICC Clearing Fund Deposit amount or an MBSD Member's Average Required Fund Deposit amount, as applicable, under current Section 7 of GSD Rule 4 and MBSD Rule 4.

Under the proposed rule change, FICC is proposing to rename the subheading of Section 7 of GSD Rule 4 and MBSD Rule 4 to ''Loss Allocation Waterfall, Off-the-Market Transactions.'' In addition, FICC is proposing to restructure its loss allocation waterfall as described below.

For better organization of the subject matter, FICC is proposing to move certain paragraphs from one section to another, including (i) relocating the last sentence of current Section 7(h) of GSD Rule 4 and MBSD Rule 4 regarding recovery of allocated losses or liabilities by FICC to the fifth paragraph of proposed Section 7 of GSD Rule 4 and MBSD Rule 4, (ii) relocating from current Section 7(a) of GSD Rule 4 and MBSD Rule 4 provisions which address FICC's application of Clearing Fund deposits and other assets held by FICC

[32] Pursuant to Section 8(e) of GSD Rule 3, an Inter-Dealer Broker Netting Member is required to (A) limit its business to acting exclusively as a broker, (B) conduct all of its business in Repo Transactions with Netting Members, and (C) conduct at least 90 percent of its business in transactions that are not Repo Transactions with Netting Members. If an Inter-Dealer Broker Netting Member fails to comply with these requirements, then the Inter-Dealer Broker Netting Member shall be considered by FICC as a Dealer Netting Member. *Supra* note 5.

securing a Defaulting Member's obligations to FICC to proposed Section 6 of GSD Rule 4 and MBSD Rule 4, (iii) relocating from current Section 7 of GSD Rule 4 to proposed Section 6 of GSD Rule 4 the provision regarding FICC's right to treat certain payments to an FCO under a Cross-Margining Guaranty as a loss to be allocated, (iv) relocating the provisions in current Section 7(i) of GSD Rule 4 and MBSD Rule 4 regarding certain increases in Clearing Fund deposits not being taken into account when calculating loss allocation so that such provisions would come right after the loss allocation calculation provision, with an updated reference to proposed renumbered Sections 2(d) and 2(e) in GSD Rule 4 and MBSD Rule 4, respectively, and (v) relocating the provision regarding withdrawing members reapplying to become members [33] in the second paragraph of current Section 7(g) of GSD Rule 4 and MBSD Rule 4 to come right after the paragraph regarding the election of a Tier One Netting Member or Tier One Member, as applicable, to withdraw from membership in proposed Section 7 of GSD Rule 4 and MBSD Rule 4.

Furthermore, in order to enhance readability and clarity, FICC is proposing a number of changes to streamline the language in these provisions.

In Section 7 of GSD Rule 4 and MBSD Rule 4, as applicable, FICC is proposing to make it clear that no loss allocation under proposed GSD Rule 4 or proposed MBSD Rule 4, as applicable, would constitute a waiver of any claim FICC may have against a member for any losses or liabilities to which the member is subject under the Rules, including, without limitation, any loss or liability to which it may be subject under proposed GSD Rule 4 or proposed MBSD Rule 4, as applicable. FICC is proposing this change to preserve its legal rights and to make it clear to members that loss allocation under proposed GSD Rule 4 and proposed MBSD Rule 4 would not be deemed as FICC waiving any claims it may have against a member for any losses or liabilities to which the member is subject under the Rules.

Under the proposal, Section 7 of GSD Rule 4 and MBSD Rule 4 would make clear that the loss allocation waterfall applies to losses and liabilities (i) arising out of or relating to a default of a member or (ii) otherwise incident to the clearance and settlement business of FICC (*i.e.,* non-default losses). The loss allocation waterfall would be triggered if FICC incurs a loss or liability arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event.

As proposed, Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that, for the purposes of GSD Rule 4 or MBSD Rule 4, as applicable, the term ''Defaulting Member'' would mean a GSD Member or MBSD Member, as applicable, for which FICC has ceased to act pursuant to GSD Rule 21 or GSD Rule 22,[34] or MBSD Rule 14 or MBSD Rule 16,[35] as applicable, the term ''Defaulting Member Event'' would mean the determination by FICC to cease to act for a GSD Member or MBSD Member, as applicable, pursuant to GSD Rule 21 or GSD Rule 22, or MBSD Rule 14 or MBSD Rule 16, as applicable, and the term ''Declared Non-Default Loss Event'' would mean the determination by the Board of Directors that a loss or liability incident to the clearance and settlement business of FICC may be a significant and substantial loss or liability that may materially impair the ability of FICC to provide clearance and settlement services in an orderly manner and will potentially generate losses to be mutualized among members in order to ensure that FICC may continue to offer clearance and settlement services in an orderly manner.

As proposed, each member would be obligated to FICC for the entire amount of any loss or liability incurred by FICC arising out of or relating to any Defaulting Member Event with respect to such member. Under the proposal, to the extent that such loss or liability is not satisfied pursuant to proposed Section 6 of GSD Rule 4 or MBSD Rule 4, as applicable, FICC would apply a Corporate Contribution thereto and charge the remaining amount of such loss or liability ratably to other members, as provided in proposed Section 7 of GSD Rule 4 and MBSD Rule 4.

Under proposed Section 7 of GSD Rule 4 and MBSD Rule 4, the loss allocation waterfall would begin with a corporate contribution from FICC (''Corporate Contribution''), as is the case under the current Rules, but in a different form than under the current Section 7 of GSD Rule 4 and MBSD Rule 4 described above. Today, Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4 provide that, if FICC incurs any loss or liability as the result of the failure of a Defaulting Member to fulfill its obligations to FICC, FICC will contribute up to 25% of its existing retained earnings (or such higher amount as the Board of Directors shall determine), to such loss or liability; however, no corporate contribution from FICC is currently required for losses resulting other than those from Member impairments. Under the proposal, FICC would add a proposed new Section 7a to GSD Rule 4 and MBSD Rule 4 with a subheading of ''Corporate Contribution'' and define FICC's Corporate Contribution with respect to any loss allocation pursuant to proposed Section 7 of GSD Rule 4 or MBSD Rule 4, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, as an amount that is equal to fifty (50) percent of the amount calculated by FICC in respect of its General Business Risk Capital Requirement as of the end of the calendar quarter immediately preceding the Event Period.[36] The proposed rule change would specify

[33] Current Section 7(g) of GSD Rule 4 provides that a Member that elects to terminate its membership pursuant to alternative (ii) in Section 7(g) of GSD Rule 4 in lieu of being liable to pay an additional assessment amount above its Required Fund Deposit shall not be eligible to re-apply to become a Comparison-Only Member or a Netting Member unless, prior to submitting such application, it makes the payment to FICC provided for in alternative (i) in Section 7(g) of GSD Rule 4, together with interest on that amount at the average of the Federal Funds Rate plus one percent, calculated from the date on which the Remaining Loss or Other Loss was incurred by FICC until the date of such payment. *Supra* note 5.

Current Section 7(g) of MBSD Rule 4 provides that a Member that elects to terminate its membership pursuant to alternative (ii) in Section 7(g) of MBSD Rule 4 in lieu of being liable to pay an additional assessment amount above its Required Fund Deposit shall not be eligible to re-apply to become a Clearing Member unless, prior to submitting such application, it makes the payment to FICC provided for in alternative (i) in Section 7(g) of MBSD Rule 4, together with interest on that amount at the average of the Federal Funds Rate plus one percent, calculated from the date on which the Remaining Loss or Other Loss was incurred by FICC until the date of such payment. *Supra* note 5.

The condition for re-application was historically in the rules of Government Securities Clearing Corporation (''GSCC'') (FICC's predecessor) to solidify GSCC's membership base and thereby discourage members from withdrawing from membership during a time of stress solely to avoid their loss allocation obligations. This condition was later incorporated into the GSD Rules and MBSD Rules. In the interest of continuing to encourage members to remain in FICC central clearing in order to preserve the robustness of the Treasury and mortgage-backed securities markets, FICC would like to retain this condition for re-application in the GSD and MBSD Rules as is. As the provision applies to a remote contingency and, without an immediate business need, NSCC and DTC would prefer not to add this provision at this time.

[34] FICC may cease to act for a GSD Member pursuant to any of the circumstances set forth under GSD Rule 21 (Restrictions on Access to Services) or GSD Rule 22 (Insolvency of a Member). *Supra* note 5.

[35] FICC may cease to act for an MBSD Member pursuant to any of the circumstances set forth under MBSD Rule 14 (Restrictions on Access to Services) or MBSD Rule 16 (Insolvency of a Member). *Supra* note 5.

[36] *Supra* note 9.

that FICC's General Business Risk Capital Requirement, as defined in FICC's Clearing Agency Policy on Capital Requirements,[37] is, at a minimum, equal to the regulatory capital that FICC is required to maintain in compliance with Rule 17Ad–22(e)(15) under the Act.[38]

As proposed, if FICC applies the Corporate Contribution to a loss or liability arising out of or relating to one or more Defaulting Member Events or Declared Non-Default Loss Events relating to an Event Period, then for any subsequent Event Periods that occur during the two hundred fifty (250) Business Days thereafter,[39] the Corporate Contribution would be reduced to the remaining unused portion of the Corporate Contribution amount that was applied for the first Event Period. Proposed Section 7a of both GSD Rule 4 and MBSD Rule 4 would require FICC to notify members of any such reduction to the Corporate Contribution.

Proposed Section 7a to GSD Rule 4 and MBSD Rule 4 would also make clear that there would be one FICC Corporate Contribution, the amount of which would be available to both Divisions and would be applied against a loss or liability in either Division in the order in which such loss or liability occurs, *i.e.,* FICC would not have two separate Corporate Contributions, one for each Division. As proposed, in the event of a loss or liability relating to an Event Period, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, attributable to only one Division, the Corporate Contribution would be applied to that Division up to the amount then available. Under the proposal, if a loss or liability relating to an Event Period, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, occurs simultaneously at both Divisions, the Corporate Contribution would be applied to the respective Divisions in the same proportion that the aggregate Average RFDs of all members in that Division bears to the aggregate Average RFDs of all members in both Divisions.[40]

Currently, the Rules do not require FICC to contribute its retained earnings to losses and liabilities other than those from member defaults. Under the proposal, FICC would expand the application of its corporate contribution beyond losses and liabilities as the result of the failure of a Defaulting Member to fulfill its obligations to FICC. The proposed Corporate Contribution would apply to losses or liabilities relating to or arising out of Defaulting Member Events and Declared Non-Default Loss Events, and would be a mandatory loss contribution by FICC prior to any allocation of the loss among the applicable Division's members.

Current Section 7(b) of GSD Rule 4 and Section 7(c) of MBSD Rule 4 provide FICC the option to contribute amounts higher than the specified percentage of retained earnings as determined by the Board of Directors, to any loss or liability incurred by FICC as the result of the failure of a Defaulting Member to fulfill its obligations to FICC. This option would be retained and expanded under the proposal to also cover non-default losses. Proposed Section 7a of GSD Rule 4 and MBSD Rule 4 would provide that nothing in the Rules would prevent FICC from voluntarily applying amounts greater than the Corporate Contribution against any FICC loss or liability, whether arising out of or relating to a Defaulting Member Event or a Declared Non-Default Loss Event, if the Board of Directors, in its sole discretion, believes such to be appropriate under the factual situation existing at the time.

Proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that FICC shall apply the Corporate Contribution to losses and liabilities that arise out of or relate to one or more Defaulting Member Events and/or (ii) Declared Non-Default Loss Events that occur within an Event Period. The proposed rule change also provides that if losses and liabilities with respect to such Event Period remain unsatisfied following application of the Corporate Contribution, FICC would allocate such losses and liabilities to members, as described below.

As proposed, Section 7 of GSD Rule 4 and MBSD Rule 4 would retain the differentiation in allocating losses to Tier One Netting Members or Tier One Members, as applicable, and Tier Two Members. Specifically, as is the case today, losses or liabilities that arise out of or relate to one or more Defaulting Member Events would be attributable to Tier One Netting Members or Tier One Members, as applicable, and Tier Two Members, while losses or liabilities that arise out of or relate to one or more Declared Non-Default Loss Events would only be attributable to Tier One Netting Members or Tier One Members, as applicable. Tier Two Members would not be subject to loss allocation with respect to Declared Non-Default Loss Events.

Under the proposal, FICC would delete the provision in current Section 7(h) of GSD Rule 4 and MBSD Rule 4 that requires FICC to promptly notify members and the Commission of the amounts involved and the causes if a Remaining Loss or Other Loss occurs because such notification would no longer be necessary under the proposed rule change. Under the proposed rule change, FICC would notify members subject to loss allocation of the amounts being allocated to them in one or more Loss Allocation Notices for both Defaulting Member Events and Declared Non-Default Loss Events. As such, in order to conform to the proposed rule change, FICC is proposing to eliminate the notification to members regarding the amounts involved and the causes if a Remaining Loss or Other Loss occurs that is required under current Section 7(h) of GSD Rule 4 and MBSD Rule 4. FICC is also proposing to delete the notification to the Commission regarding the amounts involved and the causes if a Remaining Loss or Other Loss occurs as required in the same section. While as a practical matter, FICC would notify the Commission of a decision to loss allocate, FICC does not believe such notification needs to be specified in the Rules.

In addition, FICC is proposing to clarify the provision related to Off-the-Market Transactions so that it is clear that loss or liability of FICC in connection with the close-out or liquidation of an Off-the-Market Transaction in the portfolio of a Defaulting Member would be allocated to the Member that was the counterparty to such transaction.

Tier One Netting Members/Tier One Members

For Tier One Netting Members or Tier One Members, as applicable, proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would establish the concept of an ''Event Period'' to provide for a clear and transparent way of handling multiple loss events occurring in a period of ten (10) Business Days, which would be grouped into an Event Period.[41] As stated above, both Defaulting Member Events or Declared Non-Default Loss Events could occur within the same Event Period.

Under the proposal, an Event Period with respect to a Defaulting Member Event would begin on the day FICC notifies members that it has ceased to act for the Defaulting Member (or the next Business Day, if such day is not a Business Day). In the case of a Declared Non-Default Loss Event, an Event Period

[37] *Supra* note 10.

[38] *Supra* note 11.

[39] *Supra* note 13.

[40] *Supra* note 14.

[41] *Supra* note 16.

would begin on the day that FICC notifies members of the Declared Non-Default Loss Event (or the next Business Day, if such day is not a Business Day). If a subsequent Defaulting Member Event or Declared Non-Default Loss Event occurs during an Event Period, any losses or liabilities arising out of or relating to any such subsequent event would be resolved as losses or liabilities that are part of the same Event Period, without extending the duration of such Event Period.

Proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would also retain the requirement of loss allocation among Tier One Netting Members or Tier One Members, as applicable, if a loss or liability remains after the application of the Corporate Contribution, as described above. In contrast to the current Section 7 where FICC would assess the Required Fund Deposits of Tier One Netting Members or Tier One Members, as applicable, to allocate losses, under the proposal, FICC would require Tier One Netting Members or Tier One Members, as applicable, to pay their loss allocation amounts (leaving their Required Fund Deposits intact).[42] Loss allocation obligations would continue to be calculated based upon a Tier One Netting Member's or Tier One Member's, as applicable, pro rata share of losses and liabilities (although the pro rata share would be calculated differently than it is today), and Tier One Netting Members or Tier One Members, as applicable, would still retain the ability to voluntarily withdraw from membership and cap their loss allocation obligation (although the loss allocation obligation would also be calculated differently than it is today).

The proposed rule change to Section 7 of GSD Rule 4 and MBSD Rule 4 would clarify that each Tier One Netting Member or Tier One Member, as applicable, that is a Tier One Netting Member or Tier One Member on the first day of an Event Period would be obligated to pay its pro rata share of losses and liabilities arising out of or relating to each Defaulting Member Event (other than a Defaulting Member Event with respect to which it is the Defaulting Member) and each Declared Non-Default Loss Event occurring during the Event Period. The proposal would make it clear that any Tier One Netting Member or Tier One Member, as applicable, for which FICC ceases to act on a non-Business Day, triggering an Event Period that commences on the next Business Day, shall be deemed to be a Tier One Netting Member or Tier One Member, as applicable, on the first day of that Event Period.

Under the proposed rule change, a loss allocation ''round'' would mean a series of loss allocations relating to an Event Period, the aggregate amount of which is limited by the round cap. When the aggregate amount of losses allocated in a round equals the round cap, any additional losses relating to the applicable Event Period would be allocated in one or more subsequent rounds, in each case subject to a round cap for that round. FICC may continue the loss allocation process in successive rounds until all losses from the Event Period are allocated among Tier One Netting Members or Tier One Members, as applicable, that have not submitted a Loss Allocation Withdrawal Notice in accordance with proposed Section 7b of GSD Rule 4 or MBSD Rule 4.

As proposed, each loss allocation would be communicated to the Tier One Netting Members or Tier One Members, as applicable, by the issuance of a Loss Allocation Notice. Under the proposal, each Tier One Netting Member's or Tier One Member's, as applicable, pro rata share of losses and liabilities to be allocated in any round would be equal to (i) the member's Average RFD divided by (ii) the sum of Average RFD amounts of all members subject to loss allocation in such round.

Each Loss Allocation Notice would specify the relevant Event Period and the round to which it relates. The first Loss Allocation Notice in any first, second, or subsequent round would expressly state that such Loss Allocation Notice reflects the beginning of the first, second, or subsequent round, as the case may be, and that each Tier One Netting Member or Tier One Member, as applicable, in that round has five (5) Business Days from the issuance of such first Loss Allocation Notice for the round to notify FICC of its election to withdraw from membership with GSD or MBSD, as applicable, pursuant to proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, and thereby benefit from its Loss Allocation Cap.[43] As proposed, the ''Loss Allocation Cap'' of a Tier One Netting Member or a Tier One Member, as applicable, would be equal to the greater of (x) its Required Fund Deposit on the first day of the applicable Event Period and (y) its Average RFD.

FICC is proposing to clarify that after a first round of loss allocation with respect to an Event Period, only Tier One Netting Members or Tier One Members, as applicable, that have not submitted a Loss Allocation Withdrawal Notice in accordance with proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, would be subject to further loss allocation with respect to that Event Period.

As proposed, each such member's pro rata share of losses and liabilities to be allocated in any round would be equal to (i) the member's Average RFD, divided by (ii) the sum of the Average RFD amounts of all members subject to loss allocation in such round. Each such member would have a maximum payment obligation with respect to any loss allocation round that would be equal to the greater of (x) its Required Fund Deposit on the first day of the applicable Event Period or (y) its Average RFD (such amount would be each member's ''Loss Allocation Cap''). Therefore, the sum of the Loss Allocation Caps of the members subject to loss allocation would constitute the maximum amount that FICC would be permitted to allocate in each round. FICC would retain the loss allocation limit of $5 million for Inter-Dealer Broker Netting Members, or Non-IDB Repo Brokers with respect to activities in their Segregated Broker Accounts, as discussed above.

As proposed, Section 7 of GSD Rule 4 and MBSD Rule 4, would also provide that, to the extent that a Tier One Netting Member's or Tier One Member's, as applicable, Loss Allocation Cap exceeds such member's Required Fund Deposit on the first day of the applicable Event Period, FICC may, in its discretion, retain any excess amounts on deposit from the member, up to the Loss Allocation Cap of the Tier One Netting Member or Tier One Member, as applicable.

[42] FICC believes that shifting from the two-step methodology of applying the respective Division's Clearing Fund and then requiring members to immediately replenish it to requiring direct payment would increase efficiency, while preserving the right to charge the member's Clearing Fund deposits in the event the member does not timely pay. Such a failure to pay would trigger recourse to the Clearing Fund deposits of the member under proposed Section 6 of GSD Rule 4 or MBSD Rule 4, as applicable. In addition, this change would provide greater stability for FICC in times of stress by allowing FICC to retain the respective Division's Clearing Fund, its critical prefunded resource, while charging loss allocations. FICC believes doing so would allow FICC to cover the respective Division's current credit exposures to its Members at all times. By retaining the GSD and MBSD Clearing Funds as proposed, FICC could use the Clearing Funds to secure the performance obligations of Members to their respective Division, including their payment obligation for any loss allocation, while maintaining access to prefunded resources. By being able to manage the respective Division's current credit exposures throughout the loss allocation process, FICC would be able to continue to provide its critical operations and services during what would be expected to be a stressful period.

[43] *Supra* note 19.

As proposed, Tier One Netting Members or Tier One Members, as applicable, would have two (2) Business Days after FICC issues a first round Loss Allocation Notice to pay the amount specified in any such notice.[44] On a subsequent round (*i.e.,* if the first round did not cover the entire loss of the Event Period because FICC was only able to allocate up to the round cap), these members would also have two (2) Business Days after notice by FICC to pay their loss allocation amounts (again subject to their Loss Allocation Caps), unless the members have notified (or will timely notify) FICC of their election to withdraw from membership with respect to a prior loss allocation round.

Under the proposal, if a Tier One Netting Member or Tier One Member, as applicable, fails to make its required payment in respect of a Loss Allocation Notice by the time such payment is due, FICC would have the right to proceed against such member as a Defaulting Member that has failed to satisfy an obligation in accordance with proposed Section 6 of GSD Rule 4 or MBSD Rule 4 described above. Members who wish to withdraw from membership would be required to comply with the requirements in proposed Section 7b of GSD Rule 4 and MBSD Rule 4, described further below. Specifically, proposed Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that if, after notifying FICC of its election to withdraw from membership pursuant to proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, the Tier One Netting Member or Tier One Member, as applicable, fails to comply with the provisions of proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, its notice of withdrawal would be deemed void and any further losses resulting from the applicable Event Period may be allocated against it as if it had not given such notice.

FICC is proposing to delete the provisions in the current GSD Rule 4 and MBSD Rule 4 that require FICC to assess the Required Fund Deposit maintained by each Tier One Netting Member or Tier One Member, as applicable, an amount up to $50,000, in an equal basis per such member, before allocating losses to Tier One Netting Members or Tier One Members, as applicable, ratably, in accordance with each such member's Required Fund Deposit and Average Required FICC Clearing Fund Deposit or Average Required Clearing Fund Deposit, as applicable. FICC believes that in the event of a loss or liability, this assessment is unlikely to alleviate the need for loss mutualization and creates an unnecessary administrative burden for each Division. FICC believes that moving straight to the loss mutualization described herein would be more practical. This proposed change would also streamline each Division's loss allocation waterfall processes and align such processes with those of the other DTCC Clearing Agencies.

Tier Two Members

FICC is not proposing any substantive change to the provisions regarding Tier Two Members in current Section 7 of GSD Rule 4 and MBSD Rule 4, except to (i) add a subheading of ''Tier Two Members'' in the beginning of these provisions for ease of identification and (ii) add a paragraph that makes it clear that if a Tier Two Member fails to make its required payment in respect of a Loss Allocation Notice by the time such payment is due, FICC would have the right to proceed against such member as a Defaulting Member that has failed to satisfy an obligation in accordance with proposed Section 6 of GSD Rule 4 or MBSD Rule 4 described above, consistent with the proposed change regarding Tier One Netting Members or Tier One Members, as applicable.

Withdrawal From Membership

Proposed Section 7b of GSD Rule 4 and MBSD Rule 4 would include the provisions regarding withdrawal from membership currently covered by Section 7(g) of GSD Rule 4 and MBSD Rule 4. FICC believes that relocating the provisions on withdrawal from membership as it pertains to loss allocation, so that it comes right after the section on the loss allocation waterfall, would provide for the better organization of GSD Rule 4 and MBSD Rule 4. As proposed, the subheading for Section 7b of GSD Rule 4 and MBSD Rule 4 would read ''Withdrawal Following Loss Allocation.''

Currently, Section 7(g) of GSD Rule 4 and MBSD Rule 4 provides that a member may, pursuant to current Section 13 of GSD Rule 3 or MBSD Rule 3, notify FICC by the Close of Business on the Business Day on which a payment in an amount necessary to cover losses allocated to such member after the application of its Required Fund Deposit is due, of its election to terminate its membership and thereby avail itself of a cap on loss allocation, which is currently its Required Fund Deposit as fixed on the Business Day the pro rata charge loss allocation notification is provided to such member.

As stated above, under the proposed rule change, Section 7 of GSD Rule 4 and MBSD Rule 4 would provide that a Tier One Netting Member or a Tier One Member, as applicable, who wishes to withdraw from membership in respect of a loss allocation round must provide notice of its election to withdraw (''Loss Allocation Withdrawal Notice'') within five (5) Business Days from the issuance of the first Loss Allocation Notice in any round.[45] In order to avail itself of its Loss Allocation Cap, such member would need to follow the requirements in proposed Section 7b of GSD Rule 4 and MBSD Rule 4, as applicable, which would provide that such member must: (i) Specify in its Loss Allocation Withdrawal Notice an effective date for withdrawal from membership, which date shall not be prior to the scheduled final settlement date of any remaining obligations owed by the member to FICC, unless otherwise approved by FICC, and (ii) as of the time of such member's submission of the Loss Allocation Withdrawal Notice, cease submitting transactions to FICC for processing, clearance or settlement, unless otherwise approved by FICC.

Proposed Section 7b of GSD Rule 4 and MBSD Rule 4 would provide that a Tier One Netting Member or a Tier One Member, as applicable, that withdraws in compliance with the requirements of proposed Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, would nevertheless remain obligated for its pro rata share of losses and liabilities with respect to any Event Period for which it is otherwise obligated under proposed GSD Rule 4 or MBSD Rule 4, as applicable; however, the Tier One Netting Member's or Tier One Member's, as applicable, aggregate obligation would be limited to the amount of its Loss Allocation Cap (as fixed in the round for which it withdrew).

FICC is proposing to include a sentence in proposed Section 7b of GSD Rule 4 and MBSD Rule 4 to make it clear that if the Tier One Netting Member or Tier One Member, as applicable, fails to comply with the requirements set forth in that section, its Loss Allocation Withdrawal Notice will be deemed void, and such member will remain subject to further loss allocations pursuant to proposed Section 7 of GSD Rule 4 and MBSD Rule 4 as if it had not given such notice.

For better organization of the subject matter, FICC is also proposing to move the provision that covers members' obligations to eliminate any deficiency in their Required Fund Deposits from the last sentence in the first paragraph of current Section 7(g) of GSD Rule 4

[44] *Supra* note 22.

[45] *Supra* note 19.

and MBSD Rule 4 to proposed Section 9 of GSD Rule 4 and MBSD Rule 4.

Section 8

As proposed, Section 8 of GSD Rule 4 and MBSD Rule 4 would cover the provisions on the return of a member's Clearing Fund deposit that are currently covered by Section 10 of GSD Rule 4 and MBSD Rule 4. Proposed Section 8's subheading would be ''Return of Members' Clearing Fund Deposits.''

FICC is proposing changes to streamline and enhance the clarity and readability of this section, including adding language to clarify that a member's obligations to FICC would include both matured as well as contingent obligations, but is otherwise retaining the substantive provisions of this section.

Section 9

FICC is proposing to renumber Section 8 of GSD Rule 4 and MBSD Rule 4, which addresses the timing of members' payment of the respective Division's Clearing Fund. Under the proposal, this section would be renumbered as Section 9 of GSD Rule 4 and MBSD Rule 4 and retitled to ''Initial Required Fund Deposit and Changes in Members' Required Fund Deposits'' to better reflect the subject matter of this section.

Currently, Section 8 of GSD Rule 4 and MBSD Rule 4 requires members to satisfy any increase in their Required Fund Deposit requirement within such time as FICC requires. FICC is proposing to clarify that at the time the increase becomes effective, the member's obligations to FICC will be determined in accordance with the increased Required Fund Deposit whether or not the member has satisfied such increased amount. FICC is also proposing to add language to clarify that (i) if FICC applies a GSD Netting Member's or an MBSD Clearing Member's Clearing Fund deposits as permitted pursuant to GSD Rule 4 or MBSD Rule 4, as applicable, FICC may take any and all actions with respect to the GSD Netting Member's or MBSD Clearing Member's Actual Deposit, including assignment, transfer, and sale of any Eligible Clearing Fund Securities, that FICC determines is appropriate, and (ii) if such application results in any deficiency in the GSD Netting Member's or MBSD Clearing Member's, as applicable, Required Fund Deposit, such member shall immediately replenish it. These clarifications are consistent with the Divisions' rights as set forth in current Sections 4 and 11 of GSD Rule 4 and current Sections 4 and 11 of MBSD Rule 4. In addition, the provisions in clause (ii) of the previous sentence is consistent with the requirements in current Section 1 of GSD Rule 4 and MBSD Rule 4 that a member must maintain its Required Fund Deposit.

As discussed above, for better organization of the subject matter, FICC is proposing to move the provision that covers members' obligations to eliminate any deficiency in their Required Fund Deposits from the last sentence in the first paragraph of current Section 7(g) of GSD Rule 4 and MBSD Rule 4 to proposed Section 9 of GSD Rule 4 and MBSD Rule 4.

Section 10

Currently, Section 9 of GSD Rule 4 and MBSD Rule 4 addresses situations where a member has excess on deposit in the Clearing Fund (*i.e.,* amounts above its Required Fund Deposit). The current provision provides that FICC will notify a member of any Excess Clearing Fund Deposit as FICC determines from time to time. Upon the request of a member, FICC will return an excess amount requested by a member that follows the formats and timeframe established by FICC for such request. The current provision makes clear that FICC may, in its discretion, withhold any or all of a member's Excess Clearing Fund Deposit (i) if the member has an outstanding payment obligation to FICC, (ii) if FICC determines that the member's anticipated activity over the next 90 calendar days may reasonably be expected to be materially different than the prior 90 calendar days, or (iii) if the member has been placed on the Watch List. Section 9 also makes clear that the return of an Excess Clearing Fund Deposit to any member is subject to (i) such return of Excess Clearing Fund Deposit not being done in a manner that would cause the member to violate any other section of the Rules, (ii) such return not reducing the amount of the member's Cross-Guaranty Repayment Deposit to the Clearing Fund below the amount required to be maintained by the member pursuant to GSD Rule 41 or MBSD Rule 32, as applicable, and (iii) with respect to GSD Members only, such return not reducing the amount of a GSD Member's Cross-Margining Repayment Deposit to the Clearing Fund below the amount required to be maintained by the GSD Member pursuant to GSD Rule 43.

FICC is proposing to renumber Section 9 as Section 10 for both GSD Rule 4 and MBSD Rule 4 and to retitle its subheading to ''Excess Clearing Fund Deposits'' to better reflect the subject matter of the provisions. FICC is not proposing any changes to this section except to streamline and clarify the provisions as well as to align GSD Rule 4 and MBSD Rule 4, including adding a sentence to clarify that nothing in this section limits FICC's rights under Section 7 of GSD Rule 3 or Section 6 of MBSD Rule 3, as applicable.

Section 11

Current Section 11 of GSD Rule 4 and MBSD Rule 4 provides that FICC has certain rights with respect to the Clearing Fund. FICC is proposing to add a sentence which would make it clear that GSD Rule 4 or MBSD Rule 4, as applicable, would govern in the event of any conflict or inconsistency between such rule and any agreement between FICC and any member. FICC believes that this proposed change would facilitate members' understanding of the Rules and their obligations thereunder. It would also align the Rules with the Rules and Procedures of NSCC so as to provide consistent treatment for firms that are members of both FICC and NSCC.[46] Furthermore, in order to enhance the readability and clarity, FICC is proposing a number of changes to streamline the language in this section.

(ii) Other Proposed Rule Changes

FICC is proposing changes to GSD Rule 1 (Definitions), GSD Rule 3 (Ongoing Membership Requirements), GSD Rule 3A (Sponsoring Members and Sponsored Members), GSD Rule 3B (Centrally Cleared Institutional Triparty Service), GSD Rule 13 (Funds-Only Settlement), GSD Rule 18 (Special Provisions for Repo Transactions), GSD Rule 21A (Wind-Down of a Netting Member), GSD Rule 22B (Corporation Default), GSD Rule 41 (Cross Guaranty Agreements), GSD Rule 43 (Cross-Margining Arrangements), GSD Board Interpretations and Statements of Policy, and GSD Interpretive Guidance with Respect to Watch List Consequences. FICC is also proposing changes to MBSD Rule 1 (Definitions), MBSD Rule 3 (Ongoing Membership Requirements), MBSD Rule 5 (Trade Comparison), MBSD Rule 11 (Cash Settlement), MBSD Rule 17A (Corporation Default), MBSD Rule 32 (Cross Guaranty Agreements), and MBSD Interpretive Guidance with Respect to Watch List Consequences. FICC is proposing changes to these Rules in order to conform them with the proposed changes to GSD Rule 4 and MBSD Rule 4, as applicable, as well as

[46] *See* Section 12 of Rule 4 in NSCC's Rules and Procedures, *available at http://www.dtcc.com/~/media/Files/Downloads/legal/rules/nscc_rules.pdf.*

to make certain technical changes to these Rules, as further described below.

Adding Defined Terms

Specifically, FICC is proposing to add the following defined terms to GSD Rule 1, in alphabetical order: Actual Deposit, Average RFD, CCIT Member Termination Date, CCIT Member Voluntary Termination Notice, Clearing Fund Cash, Corporate Contribution, Declared Non-Default Loss Event, Defaulting Member Event, Event Period, Excess Clearing Fund Deposit, Former Sponsored Members, Lender, Loss Allocation Cap, Loss Allocation Notice, Loss Allocation Withdrawal Notice, Sponsored Member Termination Date, Sponsored Member Voluntary Termination Notice, Sponsoring Member Termination Date, Sponsoring Member Voluntary Termination Notice, Termination Date, and Voluntary Termination Notice.

FICC is also proposing to add the following defined terms to MBSD Rule 1, in alphabetical order: Actual Deposit, Average RFD, Clearing Fund Cash, Corporate Contribution, Declared Non-Default Loss Event, Defaulting Member Event, Event Period, Excess Clearing Fund Deposit, Lender, Loss Allocation Cap, Loss Allocation Notice, Loss Allocation Withdrawal Notice, Termination Date, and Voluntary Termination Notice.

Technical Changes

In addition, FICC is proposing technical changes (i) to delete the defined term ''The Corporation'' in GSD Rule 1 and replace it with ''Corporation'' in GSD Rule 1, (ii) to correct cross-references in Section 8 of MBSD Rule 5 and the definition of ''Legal Risk'' in GSD Rule 1, (iii) to update references to sections that would be changed under this proposal in Section 12 of GSD Rule 3, Sections 10 and 12(a) of GSD Rule 3A, Section 3(f) of GSD Rule 18, GSD Rule 21A, Sections 3(a), 3(b) and 4 of GSD Rule 41, Section 6 of GSD Rule 43, GSD Interpretive Guidance with Respect to Watch List Consequences, Sections 11, 14, and 15 of MBSD Rule 3, Section 3(b) of MBSD Rule 32, and MBSD Interpretive Guidance with Respect to Watch List Consequences, (iv) to update the reference to a subheading that would be changed under this proposal in Section 7 of GSD Rule 3B, and (v) to delete a reference to the Cross-Margining Agreement between FICC and NYPC that is no longer in effect. FICC believes that these proposed technical changes would ensure the Rules remain clear and accurate, which would in turn allow Members to readily understand their obligations under the Rules.

Voluntary Termination

FICC is also proposing changes to the voluntary termination provisions in GSD Rule 3, GSD Rule 3A, GSD Rule 3B, and MBSD Rule 3 in order to ensure that termination provisions in the GSD Rules and MBSD Rules, whether voluntary or in response to a loss allocation, are consistent with one another to the extent appropriate.

Currently, the voluntary termination provisions in GSD Rule 3, GSD Rule 3A, GSD Rule 3B, and MBSD Rule 3 generally provide that a member may elect to terminate its membership by providing FICC with 10 days written notice of such termination. Such termination will not be effective until accepted by FICC, which shall be no later than 10 Business Days after the receipt of the notice. FICC's acceptance shall be evidenced by a notice to FICC's members announcing the member's termination and the effective date of the termination (''Termination Date''), and that the terminating member will no longer be eligible to submit transactions to FICC as of the Termination Date.[47] This provision also provides that a member's voluntary termination of membership shall not affect its obligations to FICC.

Where appropriate, FICC is proposing changes to align the voluntary termination provisions in Section 13 of GSD Rule 3, Sections 2(i) and 3(e) of GSD Rule 3A, Section 6 of GSD Rule 3B, and Section 14 of MBSD Rule 3 with the proposed new Section 7b of GSD Rule 4 and MBSD Rule 4, given that they all address termination of membership. Specifically, in Section 13 of GSD Rule 3, FICC is proposing that when a GSD Member elects to voluntarily terminate its membership by providing FICC a written notice of such termination (''Voluntary Termination Notice''), the GSD Member must specify in its Voluntary Termination Notice a desired date for its withdrawal from membership; provided, however, if the GSD Member is terminating its membership in GSD (*i.e.,* not terminating its membership just in the Netting System), such date shall not be prior to the scheduled final settlement date of any remaining obligation owed by the GSD Member to FICC as of the time such Voluntary Termination Notice is submitted to FICC, unless otherwise approved by FICC. FICC is proposing to delete the provision that requires a member to provide FICC with 10 days written notice of the member's termination; however, FICC is retaining the provision that states termination will not be effective until accepted by FICC,[48] which shall be no later than 10 Business Days after the receipt of the notice. FICC is also retaining the provision that states FICC's acceptance shall be evidenced by a notice to FICC's members announcing the member's termination and the Termination Date, and that the terminating member will no longer be eligible to submit transactions to FICC as of the Termination Date.

As an example, Member A submits a Voluntary Termination Notice to GSD on April 1st indicating its desired termination date is June 15th. GSD would accept such termination request by issuing a notice to GSD Members within 10 Business Days from April 1st; such notice would provide that the effective date of Member A's GSD membership termination is June 15th. In contrast, if Member A submits a Voluntary Termination Notice on April 1st and indicates its desired termination date is April 5th, GSD would either (i) accept such termination notice by issuing a notice to GSD Members on or before April 5th, and such notice would provide that the effective date of Member A's GSD membership termination is April 5th or (ii) if GSD requires additional time to process the termination, GSD would accept such termination notice by issuing notice to GSD Members after April 5th but still within 10 Business Days from April 1st; and such notice would provide that the effective date of Member A's GSD membership termination as a date after April 5th.

The proposed change to Section 13 of GSD Rule 3 would also provide that if any trade is submitted to FICC either by the withdrawing GSD Member or its authorized submitter that is scheduled to settle on or after the Termination Date, the GSD Member's Voluntary Termination Notice would be deemed void and the GSD Member would remain subject to the GSD Rules as if it had not given such notice. Furthermore, FICC is proposing to add a sentence to Section 13 of GSD Rule 3 to refer GSD Members to Section 8 of GSD Rule 4

[47] Account(s) of a terminating member would generally be deactivated before the open of business on the Termination Date.

[48] Unlike the Voluntary Termination Notice, the Loss Allocation Withdrawal Notice as proposed in Section 7b of GSD Rule 4 and MBSD Rule 4 does not require explicit acceptance by FICC to be effective. FICC believes that requiring explicit acceptance of the Loss Allocation Withdrawal Notice could complicate the loss allocation process and potentially result in membership withdrawal being delayed as well as detract from the objective to have FICC know on a timely basis which members would remain subject to the subsequent rounds of loss allocation.

regarding provisions on the return of a GSD Member's Clearing Fund deposit and to specify that if an Event Period were to occur after a Tier One Netting Member has submitted its Voluntary Termination Notice but prior to the Termination Date, in order for such Tier One Netting Member to benefit from its Loss Allocation Cap pursuant to Section 7 of GSD Rule 4, the Tier One Netting Member would need to comply with the provisions of Section 7b of GSD Rule 4 and submit a Loss Allocation Withdrawal Notice, which notice, upon submission, would supersede and void any pending Voluntary Termination Notice previously submitted by the Tier One Netting Member.[49] As an example, if an Event Period occurs after submission of the Voluntary Termination Notice by a Tier One Netting Member or Tier One Member, as applicable, but prior to the Termination Date, and the Tier One Netting Member or Tier One Member, as applicable, does not subsequently submit a Loss Allocation Withdrawal Notice as proposed in Section 7b of GSD Rule 4 or MBSD Rule 4, as applicable, then the Tier One Netting Member or Tier One Member, as applicable, would not benefit from its Loss Allocation Cap, *i.e.,* the Tier One Netting Member or Tier One Member, as applicable, would remain obligated for its pro rata share of losses and liabilities with respect to any Event Period that commenced prior to the Termination Date.

Parallel changes are also being proposed to Section 2(i) of GSD Rule 3A and Section 14 of MBSD Rule 3 with additional language in Section 2(i) of GSD Rule 3A and Section 14 of MBSD Rule 3 making it clear that the acceptance by FICC of a member's Voluntary Termination Notice shall be no later than ten (10) Business Days after the receipt of such notice from the member, in order to provide certainty to members as well as to align these sections with the current Section 13 of GSD Rule 3.

With respect to Section 3(e) of GSD Rule 3A and Section 6 of GSD Rule 3B, changes similar to the ones described above in the previous paragraph are also being proposed for Sponsored Members and CCIT Members, except there would be no references to the return of a member's Clearing Fund deposits and to Loss Allocation Caps because they would not apply to these member types. In addition, FICC is proposing a technical change in Section 6 of GSD Rule 3B to reflect a defined term that would be changed under this proposal.

Other MBSD Proposed Rule Changes

FICC is proposing to delete Section 15 of MBSD Rule 3 because FICC believes that this section is akin to a loss allocation provision and therefore would no longer be necessary under the proposed rule change, as the scenarios envisioned by Section 15 of MBSD Rule 3 would be governed by the proposed loss allocation provisions in MBSD Rule 4.

Other GSD Proposed Rule Changes

Under the proposal, Section 12(c) of GSD Rule 3A would also be revised to incorporate the concept of the Loss Allocation Cap and to reference the applicable proposed sections in GSD Rule 4 that would apply when a Sponsoring Member elects to terminate its status as a Sponsoring Member.

FICC is also proposing to delete an Interpretation of the Board of Directors of the Government Securities Clearing Corporation (the predecessor to GSD), which currently clarifies certain provisions of GSD Rule 4 and the extent to which the GSD Clearing Fund and other required deposits of GSD Netting Members may be applied to a loss or liability incurred by FICC. FICC is proposing this deletion because this interpretation would no longer be necessary following the proposed rule change. This is because the proposed rule change to GSD Rule 4 would cover the extent to which the GSD Clearing Fund and other collateral or assets of GSD Netting Members would be applied to a loss or liability incurred by FICC.

Other GSD Proposed Rule Changes and MBSD Proposed Rule Changes

FICC is proposing changes to Section 11 of GSD Rule 4 and MBSD Rule 4. Specifically, FICC is proposing to replace ''letters of credit'' with ''Eligible Letters of Credit,'' which is already a defined term in the Rules. In addition, FICC is proposing to specify that a reference to 30 days means 30 calendar days.

FICC is proposing to delete ''Remaining Loss'' and ''Other Loss'' in Sections 12(a) and 12(b) of GSD Rule 3A, Section 5 of GSD Rule 13, Section 4 of GSD Rule 41, Section 6 of GSD Rule 43, Section 9(o) of MBSD Rule 11, and Section 4 of MBSD Rule 32 because these terms would no longer be used under the proposed GSD Rule 4 and MBSD Rule 4, and to add clarifying language that conforms to the proposed changes to GSD Rule 4 and MBSD Rule 4.

In addition, FICC is proposing changes to GSD Rule 22B (Corporation Default) and MBSD Rule 17A (Corporation Default). FICC is proposing to relocate the interpretational parenthetical in each rule to come right after the reference to GSD Rule 22A and MBSD Rule 17. FICC is proposing this change because, in the event of a Corporation Default, the portfolio of each GSD Member or MBSD Member, as applicable, would be closed out in the same way as the portfolio of a GSD Defaulting Member or MBSD Defaulting Member, *i.e.,* by applying the close out procedures of GSD Rule 22A (Procedures for When the Corporation Ceases to Act) or MBSD Rule 17 (Procedures for When the Corporation Ceases to Act), as applicable. In addition, in the proposed GSD Rule 22B and MBSD Rule 17A, FICC is proposing to add a reference to the loss allocation provisions of GSD Rule 4 and MBSD Rule 4 and delete references to specific sections of GSD Rule 4 and MBSD Rule 4, because those sections are being modified under the proposed rule change.

Member Outreach

Beginning in August 2017, FICC conducted outreach to Members in order to provide them with advance notice of the proposed changes. As of the date of this filing, no written comments relating to the proposed changes have been received in response to this outreach. The Commission will be notified of any written comments received.

Implementation Timeframe

Pending Commission approval, FICC expects to implement this proposal within two (2) Business Days after approval. Members would be advised of the implementation date of this proposal through issuance of a FICC Important Notice.

2. Statutory Basis

FICC believes that the proposed rule change is consistent with the requirements of the Act, and the rules and regulations thereunder applicable to a registered clearing agency. Specifically, FICC believes that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act[50] and Rules 17Ad–22(e)(13) and 17Ad–22(e)(23)(i),[51] each as promulgated

[49] Loss Allocation Caps would not apply to Tier Two Netting Members and Tier Two Members because the loss allocation obligations of Tier Two Netting Members and Tier Two Members are already capped to the liquidation losses that resulted from their trading activity with the Defaulting Member. Tier Two Netting Members and Tier Two Members are required to pay their loss allocation obligations in full.

[50] 15 U.S.C. 78q–1(b)(3)(F).

[51] 17 CFR 240.17Ad–22(e)(13) and (e)(23)(i).

under the Act, for the reasons described below.

Section 17A(b)(3)(F) of the Act requires that the Rules be designed to promote the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds which are in the custody or control of each Division or for which it is responsible.[52] The proposed rule changes to (1) modify the calculation and application of FICC's corporate contribution, (2) introduce an Event Period, (3) introduce the concept of ''rounds'' (and accompanying Loss Allocation Notices) and apply this concept to the timing of loss allocation payments and the member withdrawal process in connection with the loss allocation process, and (4) implement a revised ''look-back'' period to calculate a member's loss allocation obligation and its Loss Allocation Cap, taken together, are intended to enhance the overall resiliency of each Division's loss allocation process.

By modifying the calculation of FICC's corporate contribution, FICC would apply a mandatory fixed percentage of its General Business Risk Capital Requirement (as compared to the current Rules which provide for ''up to'' a percentage of retained earnings), which would provide greater transparency and accessibility to members as to how much FICC would contribute in the event of a loss or liability. By modifying the application of FICC's corporate contribution to apply to Declared Non-Default Loss Events, in addition to Defaulting Member Events, on a mandatory basis, FICC would expand the application of its corporate contribution beyond losses and liabilities from member defaults, which would better align the interests of FICC with those of its respective Division's members by stipulating a mandatory application of the Corporate Contribution to a Declared Non-Default Loss Event prior to any allocation of the loss among Tier One Netting Members or Tier One Members, as applicable. Taken together, these proposed rule changes would enhance the overall resiliency of each Division's loss allocation process by enhancing the calculation and application of FICC's Corporate Contribution, which is one of the key elements of each Division's loss allocation process. Moreover, by providing greater transparency and accessibility to members, as stated above, the proposed rule changes regarding the Corporate Contribution, including the proposed replenishment period and proposed allocation of FICC Corporate Contribution between Divisions, would allow members to better assess the adequacy of each Division's loss allocation process.

By introducing the concept of an Event Period, FICC would be able to group Defaulting Member Events and Declared Non-Default Loss Events occurring in a period of ten (10) Business Days for purposes of allocating losses to members. FICC believes that the Event Period would provide a defined structure for the loss allocation process to encompass potential sequential Defaulting Member Events or Declared Non-Default Loss Events that are likely to be closely linked to an initial event and/or market dislocation episode. Having this structure would enhance the overall resiliency of FICC's loss allocation process because FICC would be better equipped to address losses that may arise from multiple Defaulting Member Events and/or Declared Non-Default Loss Events that arise in quick succession. Moreover, the proposed Event Period structure would provide certainty for members concerning their maximum exposure to mutualized losses with respect to such events.

By introducing the concept of ''rounds'' (and accompanying Loss Allocation Notices) and applying this concept to the timing of loss allocation payments and the member withdrawal process in connection with the loss allocation process, FICC would (i) set forth a defined amount that it would allocate to members during each round (*i.e.,* the round cap), (ii) advise members of loss allocation obligation information as well as round information through the issuance of Loss Allocation Notices, and (iii) provide members with the option to limit their loss allocation exposure after the issuance of the first Loss Allocation Notice in each round. These proposed rule changes would enhance the overall resiliency of FICC's loss allocation process because they would enable FICC to continue the loss allocation process in successive rounds until all of FICC's losses are allocated and enable FICC to identify continuing members for purposes of calculating subsequent loss allocation obligations in successive rounds. Moreover, the proposed rule changes would define for members a clear manner and process in which they could cap their loss allocation exposure to FICC.

By implementing a revised ''look-back'' period to calculate a member's loss allocation obligations and its Loss Allocation Cap, FICC would be able to capture a full calendar quarter of the member's activities and smooth out the impact from any abnormalities and/or arbitrariness that may have occurred. By determining a member's loss allocation obligations based on the average of its Required Fund Deposit over a look-back period and its Loss Allocation Cap based on the greater of its Required Fund Deposit or the average thereof over a look-back period, FICC would be able to calculate a member's pro rata share of losses and liabilities based on the amount of risk that the member brings to FICC. These proposed rule changes would enhance the overall resiliency of each Division's loss allocation process because they would align a member's loss allocation obligation and its Loss Allocation Cap with the amount of risk that the member brings to FICC.

Taken together, the foregoing proposed rule changes would establish a stronger (for all the reasons discussed above) and clearer loss allocation process for each Division, which FICC believes would allow each Division to take timely action to address losses. The ability to timely address losses would allow each Division to continue to meet its clearance and settlement obligations, especially in circumstances that may involve a series of substantially contemporaneous loss events. Therefore, FICC believes that these 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.

By deleting certain vague and imprecise limiting language that could be interpreted as impairing FICC's ability to access the MBSD Clearing Fund to cover losses and liabilities incident to its clearance and settlement business outside the context of an MBSD Defaulting Member Event, as well as to cover certain liquidity needs, the proposed rule change to amend FICC's permitted use of MBSD Clearing Fund would enhance FICC's ability to ensure that it can continue its operations and clearance and settlement services in an orderly manner in the event that it would be necessary or appropriate for FICC to access MBSD Clearing Fund deposits to address losses, liabilities or liquidity needs to meet its settlement obligations. Therefore, FICC believes that this proposed rule change would promote the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.

Rule 17Ad–22(e)(13) under the Act requires, in part, that FICC establish, implement, maintain and enforce written policies and procedures reasonably designed to ensure each

[52] 15 U.S.C. 78q–1(b)(3)(F).

Division has the authority and operational capacity to take timely action to contain losses and continue to meet its obligations.[53] As described above, the proposed rule changes to (1) modify the calculation and application of FICC's corporate contribution, (2) introduce an Event Period, (3) introduce the concept of ''rounds'' (and accompanying Loss Allocation Notices) and apply this concept to the timing of loss allocation payments and the member withdrawal process in connection with the loss allocation process, and (4) implement a revised ''look-back'' period to calculate a member's loss allocation obligation and its Loss Allocation Cap, taken together, are designed to enhance the resiliency of each Division's loss allocation process. Having a resilient loss allocation process would help ensure that each Division can effectively and timely address losses relating to or arising out of either the default of one or more members or one or more non-default loss events, which in turn would help each Division contain losses and continue to meet its clearance and settlement obligations. Therefore, FICC believes that the proposed rule changes to enhance the resiliency of each Division's loss allocation process are consistent with Rule 17Ad–22(e)(13) under the Act.

Rule 17Ad–22(e)(23)(i) under the Act requires FICC to establish, implement, maintain and enforce written policies and procedures reasonably designed to publicly disclose all relevant rules and material procedures, including key aspects of each Division's default rules and procedures.[54] The proposed rule changes to (i) align the loss allocation rules of the DTCC Clearing Agencies, (ii) improve the overall transparency and accessibility of the provisions in the Rules governing loss allocation and (iii) make conforming and technical changes, would not only ensure that each Division's loss allocation rules are, to the extent practicable and appropriate, consistent with the loss allocation rules of other DTCC Clearing Agencies, but also would help to ensure that each Division's loss allocation rules are transparent and clear to members. Aligning the loss allocation rules of the DTCC Clearing Agencies would provide consistent treatment, to the extent practicable and appropriate, especially for firms that are participants of two or more DTCC Clearing Agencies. Having transparent and clear loss allocation rules would enable members to better understand the key aspects of each Division's default rules and procedures and provide members with increased predictability and certainty regarding their exposures and obligations. As such, FICC believes that the proposed rule changes to align the loss allocation rules of the DTCC Clearing Agencies as well as to improve the overall transparency and accessibility of each Division's loss allocation rules are consistent with Rule 17Ad–22(e)(23)(i) under the Act.

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

FICC does not believe that the proposed rule changes to enhance the resiliency of each Division's loss allocation process would impact competition.[55] As described above, the proposed rule changes to (1) modify the calculation and application of FICC's corporate contribution, (2) introduce an Event Period, (3) introduce the concept of ''rounds'' (and accompanying Loss Allocation Notices) and apply this concept to the timing of loss allocation payments and the member withdrawal process in connection with the loss allocation process, and (4) implement a revised ''look-back'' period to calculate a member's loss allocation obligation and its Loss Allocation Cap, taken together, are intended to enhance the overall resiliency of each Division's loss allocation process, and would apply equally to all members. While the proposed rule changes would amend the manner in which FICC's corporate contribution and loss allocation are calculated and applied, such proposed rule changes would maintain FICC's current core loss allocation waterfall in the case of a loss relating to or arising out of the default of a member for whom FICC has ceased to act following application of the defaulting member's resources, *i.e.,* FICC's corporate contribution and loss allocation among members. With respect to a loss or liability arising from a non-default loss event, the proposed rule changes clarify FICC's contribution to such loss and liability, but, as with losses and liabilities arising from a member default event, the proposed rule changes would maintain the loss mutualization requirement under the current GSD Rules and MBSD Rules. While the calculation of the loss obligations associated with non-default losses would change under the proposal, the FICC Divisions would maintain this aspect of the loss allocation waterfall (*i.e.,* loss mutualization among members for non-default losses). Based on the foregoing, FICC believes that these proposed rule changes to enhance the resiliency of each Division's loss allocation process would not have any impact on competition.

FICC does not believe the proposed rule change to delete certain vague and imprecise limiting language regarding FICC's use of MBSD Clearing Fund would impact competition.[56] This proposed rule change would enhance FICC's ability to ensure that it can continue its operations and clearance and settlement services in an orderly manner in the event that it would be necessary or appropriate for FICC to access MBSD Clearing Fund deposits to address losses, liabilities or liquidity needs to meet its settlement obligations. In the event that it would be necessary or appropriate for FICC to access MBSD Clearing Fund deposits, FICC's use of MBSD Clearing Fund deposits would remain subject to the parameters in the proposed rule that limit FICC's use of MBSD Clearing Fund, *i.e.,* (A) to secure each MBSD Member's performance of obligations to FICC, (B) to provide liquidity to FICC to meet its settlement obligations, and (C) for certain investments. FICC does not believe that FICC's utilization of MBSD Clearing Fund under these parameters would impact competition. Specifically, FICC does not believe that using MBSD Clearing Fund to secure each MBSD Member's performance of obligations to FICC and for certain investments would have an impact on the MBSD Members because the fund and/or investments are still being held by FICC. With respect to FICC's use of MBSD Clearing Fund pursuant to parameter (B), FICC believes that there may be an impact on MBSD Members if FICC uses the MBSD Clearing Fund for more than 30 calendar days. This is because FICC would then consider the amount of MBSD Clearing Fund used but not yet repaid as a loss to the MBSD Clearing Fund incurred as a result of a Defaulting Member Event and immediately allocate such loss in accordance with the proposal. However, because loss allocation among the MBSD Members would be based on the Average RFDs of those MBSD Members, any loss allocation among MBSD Members would affect MBSD Members in proportion to the amount of risks they bring to FICC, as represented by their Average RFDs. Based on the foregoing, FICC does not believe that the proposed deletion of the limiting language regarding FICC's use of MBSD Clearing Fund would have any impact on competition.

FICC also does not believe that the proposed rule changes to (i) align the

[53] 17 CFR 240.17Ad–22(e)(13).

[54] 17 CFR 240.17Ad–22(e)(23)(i).

[55] 15 U.S.C. 78q–1(b)(3)(I).

[56] *Id.*

loss allocation rules of the DTCC Clearing Agencies, (ii) increase the transparency and accessibility of provisions in the Rules governing loss allocation, and (iii) make conforming and technical changes, would impact competition.[57] These changes would apply equally to all members. Alignment of the loss allocation rules of the DTCC Clearing Agencies are intended to increase the consistency of the Rules with the rules of other DTCC Clearing Agencies in order to provide consistent treatment, to the extent practicable and appropriate, especially for firms that are participants of two or more DTCC Clearing Agencies. Having transparent and accessible provisions in the Rules governing loss allocation are intended to improve the readability and clarity of the Rules regarding the loss allocation process. Making conforming and technical changes to ensure the Rules remain clear and accurate would facilitate members' understanding of the Rules and their obligations thereunder. As such, FICC believes that these proposed rule changes would not have any impact on competition.

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

Written comments relating to this proposed rule change have not been solicited or received. FICC will notify the Commission of any written comments received by FICC.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing. 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 email to *rule-comments@sec.gov.* Please include File Number SR–FICC–2017–022 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090.

All submissions should refer to File Number SR–FICC–2017–022. This file number should be included on the subject line if email 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. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–FICC–2017–022 and should be submitted on or before August 3, 2018.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[58]

Eduardo A. Aleman,

Assistant Secretary.

[FR Doc. 2018–15366 Filed 7–18–18; 8:45 am]

BILLING CODE 8011–01–P

[57] *Id.*

[58] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–83630; File No. SR–FICC–2017–021]

Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Amendment No. 1 to a Proposed Rule Change To Adopt a Recovery & Wind-down Plan and Related Rules

July 13, 2018.

On December 18, 2017, Fixed Income Clearing Corporation (''FICC'') filed with the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'') and Rule 19b–4 thereunder, proposed rule change SR–FICC–2017–021 (''Proposed Rule Change'') to adopt a recovery and wind-down plan and related rules.[1] The Proposed Rule Change was published for comment in the **Federal Register** on January 8, 2018.[2] On February 8, 2018, the Commission designated a longer period within which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove the Proposed Rule Change.[3] On March 20, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the Proposed Rule Change.[4] On June 25, 2018, the Commission designated a longer period for Commission action on the proceedings to determine whether to

[1] 15 U.S.C. 78s(b)(1) and 17 CFR 240.19b–4, respectively. On December 18, 2017, FICC filed the Proposed Rule Change as advance notice SR–FICC–2017–805 (''Advance Notice'') with the Commission pursuant to Section 806(e)(1) of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act entitled the Payment, Clearing, and Settlement Supervision Act of 2010 (''Clearing Supervision Act'') and Rule 19b–4(n)(1)(i) of the Act. (12 U.S.C. 5465(e)(1) and 17 CFR 240.19b–4(n)(1)(i), respectively.) On January 30, 2018, the Commission published in the **Federal Register** notice of filing of the Advance Notice. The notice also extended the review period for the Advance Notice pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act. (12 U.S.C. 5465(e)(1)(H).) *See* Securities Exchange Act Release No. 82580 (January 24, 2018), 83 FR 4341 (January 30, 2018) (SR–FICC–2017–805). On April 10, 2018, the Commission required additional information for consideration of the Advance Notice, pursuant to Section 806(e)(1)(D) of the Clearing Supervision Act, which provided the Commission with an additional 60-days in the review period beginning on the date that the information requested is received by the Commission. (12 U.S.C. 5465(e)(1)(D).) *See* Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled ''Commission's Request for Additional Information,'' *available at https://www.sec.gov/rules/sro/ficc-an.htm.* On June 28, 2018, FICC filed Amendment No. 1 to the Advance Notice. To promote the public availability and transparency of its post-notice amendment, FICC submitted a copy of Amendment No. 1 through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Advance Notice has been posted on the Commission's website at *https://www.sec.gov/rules/sro/ficc-an.htm* and thus been publicly available since June 29, 2018. On July 6, 2018, the Commission received the information requested, which added an additional 60-days to the review period pursuant to Sections 806(e)(1)(E) and (G) of the Clearing Supervision Act. (12 U.S.C. 5465(e)(1)(E) and (G).) *See* Memorandum from the Office of Clearance and Settlement Supervision, Division of Trading and Markets, titled ''Response to the Commission's Request for Additional Information,'' *available at https://www.sec.gov/rules/sro/ficc-an.htm.* The proposal, as set forth in both the Advance Notice and the Proposed Rule Change, shall not take effect until all required regulatory actions are completed.

[2] Securities Exchange Act Release No. 82431 (January 2, 2018), 83 FR 871 (January 8, 2018) (SR–FICC–2017–021).

[3] Securities Exchange Act Release No. 82669 (February 8, 2018), 83 FR 6653 (February 14, 2018) (SR–DTC–2017–021; SR–FICC–2017–021; SR–NSCC–2017–017).

[4] Securities Exchange Act Release No. 82913 (March 20, 2018), 83 FR 12997 (March 26, 2018) (SR–FICC–2017–021).