

remains appointed to serve as the Public Representative.

*It is ordered:*

1. The Commission invites comments on the Request of the United States Postal Service for Exemption from Revenue Limitation on Market Test of Experimental Product—Customized Delivery, with Portions Filed Under Seal, filed April 4, 2017.

2. Pursuant to 39 U.S.C. 505, Lauren A. D'Agostino remains appointed to serve as the Public Representative in this proceeding.

3. Comments by interested persons are due no later than April 26, 2017.

4. The Secretary shall arrange for publication of this order in the **Federal Register**.

By the Commission.

**Ruth Ann Abrams,**  
*Acting Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-80383; File No. SR-FICC-2017-006]

### Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change To Enhance the Credit Risk Rating Matrix and Make Other Changes

April 5, 2017.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on March 22, 2017, Fixed Income Clearing Corporation (“FICC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared by the clearing agency.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The proposed rule change consists of amendments to FICC’s Government

Securities Division (“GSD”) Rulebook (“GSD Rules”) and Mortgage-Backed Securities Division (“MBSD”) Clearing Rules (“MBSD Rules,” and collectively with the GSD Rules, the “Rules”).<sup>4</sup> The proposed rule change would amend the Rules in order to (i) enhance the matrix (hereinafter referred to as the “Credit Risk Rating Matrix” or “CRRM”) developed by FICC to evaluate the risks posed by certain GSD Netting Members and MBSD Clearing Members (collectively, “CRRM-Rated Members”) to FICC and its members from providing services to these CRRM-Rated Members and (ii) make other amendments to the Rules to provide more transparency and clarity regarding FICC’s current ongoing membership monitoring process.

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

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

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

###### 1. Purpose

The proposed rule change would, among other things, enhance the CRRM to enable it to rate FICC members that are foreign banks or trust companies and have audited financial data that is publicly available. It would also enhance the CRRM by allowing it to take into account qualitative factors when generating credit ratings for FICC

members. In addition, it would enhance the CRRM by shifting it from a relative scoring approach to an absolute scoring approach.

This rule filing also contains proposed rule changes that are not related to the proposed CRRM enhancements but that provide specificity, clarity and additional transparency to the Rules related to FICC’s current ongoing membership monitoring process.

###### (i) Background

FICC occupies an important role in the securities settlement system by interposing itself through each of GSD and MBSD as a central counterparty between members that are counterparties to transactions accepted for clearing by FICC, thereby reducing the risk faced by members. FICC uses the CRRM, the Watch List (as defined below) and the enhanced surveillance to manage and monitor default risks of its members on an ongoing basis, as discussed below. The level and frequency of such monitoring for a member is determined by the member’s risk of default as assessed by FICC. Members that are deemed by FICC to pose a heightened risk to FICC and its members are subject to closer and more frequent monitoring.

###### Existing Credit Risk Rating Matrix

In 2004, the Commission approved a proposed rule change filed by FICC (“Initial Filing”)<sup>6</sup> with respect to GSD and MBSD to establish new criteria for placing certain members of FICC on a list for closer monitoring (“Watch List”).

FICC proposed in the Initial Filing that all U.S. broker-dealers and U.S. banks that were GSD Netting Members and/or MBSD Clearing Members would be assigned a rating generated by entering financial data of those members into an internally generated credit rating scorecard, *i.e.*, the CRRM.<sup>7</sup> In the Initial Filing, FICC stated that all other types of GSD Netting Members and MBSD Clearing Members would be monitored by credit risk staff using financial criteria deemed relevant by FICC but

<sup>4</sup> Capitalized terms not defined herein are defined in the GSD Rules, available at [www.dtcc.com/-/media/Files/Downloads/legal/rules/ficc\\_gov\\_rules.pdf](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](http://www.dtcc.com/-/media/Files/Downloads/legal/rules/ficc_mbsd_rules.pdf).

<sup>5</sup> The proposed rule changes with respect to the enhancement of the CRRM are reflected in the inclusion of (1) qualitative factors and examples thereof in the definition of “Credit Risk Rating Matrix” in GSD Rule 1 and MBSD Rule 1 and (2) certain GSD Foreign Netting Members that are banks or trust companies and MBSD Bank Clearing Members that are Foreign Persons as CRRM-Rated Members in GSD Rule 3 (Section 12(b)(i)(II)) and MBSD Rule 3 (Section 11(b)(i)(II)). The proposed enhancement to CRRM also necessitates a conforming change to the existing Section 12(b) (renumbered to Section 12(c) in this proposed rule filing) of GSD Rule 3 by deleting the reference to Foreign Netting Members and Bank Netting Members participating through their U.S. branches or agencies, as further discussed below.

<sup>6</sup> See Securities Exchange Act Release No. 49158 (January 30, 2004), 69 FR 5624 (February 5, 2004) (SR-FICC-2003-03).

<sup>7</sup> Footnote 4 of the Initial Filing explained the new criteria for rating members: “[FICC’s] approach to the analysis of members is based on a thorough quantitative analysis. A broker-dealer member’s rating on the [CRRM] will be based on factors including size (*i.e.*, total excess net capital), capital, leverage, liquidity, and profitability. Banks will be reviewed based on size, capital, asset quality, earnings, and liquidity.” *Id.* These quantitative factors are still being applied today, and FICC currently does not plan to change them.

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

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

<sup>3</sup> On March 22, 2017, FICC filed this proposed rule change as an advance notice (SR-FICC-2017-804) 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, 12 U.S.C. 5465(e)(1), and Rule 19b-4(n)(1)(i) of the Act, 17 CFR 240.19b-4(n)(1)(i). A copy of the advance notice is available at <http://www.dtcc.com/legal/sec-rule-filings.aspx>.

would not be assigned a rating by the CRRM.<sup>8</sup>

Following the approval of the Initial Filing, the Commission approved a subsequent proposed rule change filed by FICC that provided interpretive guidance to the Initial Filing (“Interpretive Guidance Filing”).<sup>9</sup> In the Interpretive Guidance Filing, FICC reiterated that U.S. broker-dealers and U.S. banks would be assessed against the CRRM and assigned a credit rating based on quantitative factors. Unfavorably-rated members would be placed on the Watch List. In the Interpretive Guidance Filing, FICC explained that credit risk staff could downgrade a particular member’s credit rating based on various qualitative factors. An example of such qualitative factors might be that the member in question received a qualified audit opinion on its annual audit. In the Interpretive Guidance Filing, FICC noted that, in order to protect FICC and its other members, it was important that credit risk staff maintain the discretion to downgrade a member’s credit rating on the CRRM and thus subject the member to closer monitoring.

The current CRRM is comprised of two credit rating models—one for the U.S. broker-dealers and one for the U.S. banks—and generates credit ratings for the relevant members based on a 7-point rating system, with “1” being the strongest credit rating and “7” being the weakest credit rating.

Over time, the current CRRM has not kept pace with FICC’s evolving membership base and heightened expectations from regulators and stakeholders for robustness of financial models. Specifically, the current CRRM only generates credit ratings for those GSD Netting Members and MBSD Clearing Members that are U.S. banks or U.S. broker-dealers that file standard reports with their regulators, which currently comprise 77% of GSD Netting Members and 85% of MBSD Clearing Members, respectively; foreign banks and trust companies currently account for 21% of GSD Netting Members and 1% of MBSD Clearing Members.<sup>10</sup> The

numbers of GSD and MBSD members that are foreign banks or trust companies increased from 16 and zero in 2012 to 22 and one in 2017, respectively, and are expected to continue to grow over the coming years. Foreign banks and trust companies are typically large global financial institutions that have complex businesses and conduct a high volume of activities. Although foreign banks and trust companies are not currently rated by the CRRM, they are monitored by FICC’s credit risk staff using financial criteria deemed relevant by FICC and can be placed on the Watch List if they experience a financial change that presents risk to FICC. Given the increase in the number of foreign bank or trust company members in FICC in the recent years, there is a need to formalize FICC’s credit risk evaluation process of these members by assigning credit ratings to them in order to better facilitate the comparability of credit risks among members.<sup>11</sup>

In addition, the current CRRM assigns each GSD Netting Member and MBSD Clearing Member that is a U.S. bank or U.S. broker-dealer and that files standard reports with its regulator(s) a credit rating based on inputting certain quantitative data relative to the applicable member into the CRRM. Accordingly, a member’s credit rating is currently based solely upon quantitative factors. It is only after the CRRM has generated a credit rating with respect to a particular member that such member’s credit rating may be downgraded manually by credit risk staff, after taking into consideration relevant qualitative factors. The inability of the current CRRM to take into account qualitative factors requires frequent and manual overrides by credit risk staff, which may result in inconsistent and/or incomplete credit ratings for members.

Furthermore, the current CRRM uses a relative scoring approach and relies on peer grouping of members to calculate the credit rating of a member. This approach is not ideal because a member’s credit rating can be affected by changes in its peer group even if the member’s financial condition is unchanged.

## Proposed Credit Risk Rating Matrix Enhancements

To improve the coverage and the effectiveness of the current CRRM, FICC is proposing three enhancements. The first proposed enhancement would expand the scope of CRRM coverage by enabling the CRRM to generate credit ratings for GSD Netting Members and MBSD Clearing Members that are foreign banks or trust companies and that have audited financial data that is publicly available. The second proposed enhancement would incorporate qualitative factors into the CRRM and therefore is expected to reduce the need and the frequency of manual overrides of member credit ratings. The third enhancement would replace the relative scoring approach currently used by CRRM with a statistical approach to estimate the absolute probability of default of each member.

### *A. Enable the CRRM To Generate Credit Ratings for Foreign Bank or Trust Company Members*

The current CRRM is comprised of two credit rating models—one for the U.S. broker-dealers and one for the U.S. banks. FICC is proposing to enhance the CRRM by adding an additional credit rating model for the foreign banks and trust companies. The additional model would expand the membership classes to which the CRRM would apply to include foreign banks and trust companies that are GSD Netting Members and/or MBSD Clearing Members and that have audited financial data that is publicly available. The CRRM credit rating of a foreign bank or trust company that is a GSD Netting Member and/or MBSD Clearing Member would be based on quantitative factors, including size, capital, leverage, liquidity, profitability and growth, and qualitative factors, including market position and sustainability, information reporting and compliance, management quality, capital management and business/product diversity. By enabling the CRRM to generate credit ratings for these GSD Netting Members and MBSD Clearing Members, the enhanced CRRM would provide more comprehensive credit risk coverage of FICC’s membership base.

With the proposed enhancement to the CRRM as described above, applicable foreign bank or trust company GSD Netting Members and MBSD Clearing Members would be included in the CRRM process and be evaluated more effectively and efficiently because financial data with respect to these foreign bank or trust company members could be extracted

<sup>8</sup> In the Initial Filing, FICC noted that these members would be monitored by credit risk staff by reviewing similar criteria as those reviewed for members included on the [CRRM] but such review would occur outside of the [CRRM] process. *Id.*

<sup>9</sup> See Securities Exchange Act Release No. 51355 (March 10, 2005), 70 FR 12919 (March 16, 2005) (SR-FICC-2004-08).

<sup>10</sup> As of March 16, 2017, there are 105 GSD Netting Members and 78 MBSD Clearing Members. Of the 105 GSD Netting Members, 13 (or 12%) are U.S. banks, 68 (or 65%) are U.S. broker-dealers and 22 (or 21%) are foreign banks or trust companies. Of the 78 MBSD Clearing Members, 14 (or 18%) are U.S. banks, 52 (or 67%) are U.S. broker-dealers and one (or 1%) is a foreign bank or trust company.

<sup>11</sup> In the Interpretive Guidance Filing, FICC noted that CRRM is applied across FICC and its affiliated clearing agencies, National Securities Clearing Corporation (“NSCC”) and The Depository Trust Company (“DTC”). Specifically, in order to run the CRRM, credit risk staff uses the financial data of the applicable GSD and MBSD members in addition to data of applicable members and participants of NSCC and DTC, respectively. In this way, each applicable GSD and MBSD member is rated against other applicable members and participants of NSCC and DTC, respectively. SR-FICC-2004-08, 70 FR 12919.

from data sources in an automated form.<sup>12</sup>

After the proposed enhancement, CRRM would be able to generate credit ratings on an ongoing basis for all GSD Netting Members and MBSD Clearing Members that are U.S. banks, U.S. brokers-dealers and foreign banks and trust companies, which together represent approximately 99% of the GSD Netting Members and 86% of the MBSD Clearing Members, respectively.<sup>13</sup>

#### *B. Incorporate Qualitative Factors Into the CRRM*

In addition, as proposed, the enhanced CRRM would blend qualitative factors with quantitative factors to produce a credit rating for each applicable member in relation to the member's credit risk. For U.S. and foreign banks and trust companies, the enhanced CRRM would use a 70/30 weighted split between quantitative and qualitative factors to generate credit ratings. For U.S. broker-dealers, the weight split between quantitative and qualitative factors would be 60/40. These weight splits are chosen by FICC based on the industry best practice as well as research and sensitivity analysis conducted by FICC. FICC would review and adjust the weight splits as well as the quantitative and qualitative factors, as needed, based on recalibration of the CRRM to be conducted by FICC approximately every three to five years.

Although there are advantages to measuring credit risk quantitatively, quantitative evaluation models alone are incapable of fully capturing all credit risks. Certain qualitative factors may indicate that a member is or will soon be undergoing financial distress, which may in turn signal a higher default exposure to FICC and its other members. As such, a key enhancement being proposed to the CRRM is the incorporation of relevant qualitative factors into each of the three credit rating models mentioned above. By including qualitative factors in the three credit rating models, the enhanced

CRRM would capture risks that would otherwise not be accounted for with quantitative factors alone.<sup>14</sup> Adding qualitative factors to the CRRM would not only enable it to generate more consistent and comprehensive credit ratings for applicable members, but it would also help reduce the need and frequency of manual credit rating overrides by the credit risk staff because overrides would likely only be required under more limited circumstances.<sup>15</sup>

#### *C. Shifting From Relative Scoring to Absolute Scoring*

As proposed, the enhanced CRRM would use an absolute scoring approach and rank each member based on its individual probability of default rather than the relative scoring approach that is currently in use. This proposed change is designed to have a member's CRRM-generated credit rating reflect an absolute measure of the member's default risk and eliminate any potential distortion of a member's credit rating from the member's peer group that may occur under the relative scoring approach used in the existing CRRM.

#### *D. Watch List and Enhanced Surveillance*

In addition to the Watch List, FICC also maintains an enhanced surveillance list (referenced herein and in the proposed rule text as "enhanced surveillance") for membership monitoring. The enhanced surveillance list is generally used when members are undergoing drastic and unexpected changes in their financial conditions or operation capabilities and thus are deemed by FICC to be of the highest risk level and/or warrant additional scrutiny due to FICC's ongoing concerns about these members. Accordingly, members that are subject to enhanced surveillance are reported to FICC's management committees and are also regularly reviewed by a cross-functional team comprised of senior management of FICC. More often than not, members

that are subject to enhanced surveillance are also on the Watch List. The group of members that is subject to enhanced surveillance is generally much smaller than the group on the Watch List. The enhanced surveillance list is an internal tool for FICC that triggers increased monitoring of a member above the monitoring that occurs when a member is on the Watch List.

A member could be placed on the Watch List either based on its credit rating of 5, 6 or 7, which can either be generated by the CRRM or from a manual downgrade, or when FICC deems such placement as necessary to protect FICC and its members. In contrast, a member would be subject to enhanced surveillance only when close monitoring of the member is deemed necessary to protect FICC and its members.

The Watch List and enhanced surveillance tools are not mutually exclusive; they may complement each other under certain circumstances. A key distinction between the Watch List and enhanced surveillance is that being placed on the Watch List may result in Clearing Fund related consequences under the Rules, whereas enhanced surveillance does not.<sup>16</sup> For example, a member that is in a precarious situation could be placed on the Watch List and be subject to enhanced surveillance; however, because the Watch List status could require additional Clearing Fund deposits, when FICC has preliminary concerns about a member, to avoid potential increase to a member's Clearing Fund deposit, FICC may opt not to place the member on the Watch List until it is certain that such concerns would not be alleviated in the short-term. Instead, in such a situation, FICC might first subject the member to enhanced surveillance in order to closely monitor the member's situation without affecting the member's Clearing Fund deposits. If the member's situation improves, then it will no longer be subject to enhanced surveillance. If the situation of the member worsens, the member may then be placed on the Watch List as deemed necessary by FICC.

#### *(ii) Detailed Description of the Proposed Rule Changes Related to the Proposed CRRM Enhancements*

In connection with the proposed enhancements to the CRRM, FICC proposes to amend the GSD Rules and

<sup>12</sup> In the Initial Filing, FICC noted that these members would be monitored by credit risk staff by reviewing similar criteria as those reviewed for members included on the CRRM, but such review would occur outside of the CRRM process. SR-FICC-2003-03, 69 FR 5624.

<sup>13</sup> As of March 16, 2017, there are two GSD Netting Members that are government sponsored entities and therefore would not be rated by the enhanced CRRM, as proposed; there are also 11 MBSD Clearing Members that would not be rated by the enhanced CRRM, as proposed, because they are government sponsored entities, registered investment companies, unregistered investment pools ("UIPs") or other entities that are eligible for MBSD Clearing Membership pursuant to Section 1(i) of MBSD Rule 2A. MBSD Rules, *supra* note 4.

<sup>14</sup> The initial set of qualitative factors that would be incorporated into the CRRM includes (a) for U.S. broker dealers, market position and sustainability, management quality, capital management, liquidity management, geographic diversification, business/product diversity and access to funding, (b) for U.S. banks, environment, compliance/litigation, management quality, liquidity management and parental demands and (c) for foreign banks and trust companies, market position and sustainability, information reporting and compliance, management quality, capital management and business/product diversity.

<sup>15</sup> Once a member is assigned a credit rating, if circumstances warrant, credit risk staff would still have the ability to override the CRRM-issued credit rating by manually downgrading such rating as they do today. To ensure a conservative approach, the CRRM-issued credit ratings cannot be manually upgraded.

<sup>16</sup> FICC expects to provide additional clarity to members regarding the Watch List and its impact on Clearing Fund deposits in a subsequent proposed rule change to be filed with the Commission in 2017.

the MBSD Rules to (1) incorporate qualitative factors into CRRM and (2) add foreign banks and trust companies that are GSD Netting Members and MBSD Clearing Members to the categories of members that would be assigned credit ratings by FICC using the CRRM.

*A. Proposed Changes to GSD Rule 1 (Definitions) and MBSD Rule 1 (Definitions)*

FICC is proposing to amend the “Credit Risk Rating Matrix” definition in GSD Rule 1 and MBSD Rule 1 to include qualitative factors, such as management quality, market position/environment and capital and liquidity risk management, because, as proposed, the enhanced CRRM would blend both qualitative factors and quantitative factors to produce a credit rating for each applicable FICC member.

*B. Proposed Changes to Section 12(b)(i)(II) of GSD Rule 3 (Ongoing Membership Requirements) and Section 11(b)(i)(II) of MBSD Rule 3 (Ongoing Membership Requirements)*

FICC is proposing to amend Section 12(b)(i)(III) of GSD Rule 3 and Section 11(b)(i)(III) of MBSD Rule 3 to expand the membership types to which the CRRM would apply to include GSD Netting Members and MBSD Clearing Members, as applicable, that are foreign banks or trust companies and that have audited financial data that are publicly available.

The enhanced CRRM would assign credit ratings for each GSD Netting Member and/or MBSD Clearing Member that is a foreign bank or trust company based on its publicly available audited financial data. The credit rating would be based on an 18-point scale, which is then mapped to the 7-point rating system currently in use today, with “1” being the strongest credit rating and “7” being the weakest credit rating.

*(iii) Other Proposed Rule Changes*

This rule filing also contains proposed rule changes that are unrelated to the proposed enhancement of the CRRM. These proposed rule changes would provide specificity, clarity and additional transparency to the Rules with respect to FICC’s current ongoing membership monitoring process, as described below.

*A. Proposed Changes to the Definitions of “Credit Risk Rating Matrix” and “Watch List” in GSD Rule 1 (Definitions) and MBSD Rule 1 (Definitions)*

FICC is proposing to amend the definition of “Credit Risk Rating

Matrix” in GSD Rule 1 and MBSD Rule 1 to state that, in addition to the proposed qualitative factors described above, the CRRM is also based on quantitative factors, such as capital, assets, earnings and liquidity.

FICC is also proposing to amend the definition of “Watch List” in GSD Rule 1 and MBSD Rule 1 to state that the Watch List is comprised of members whose credit ratings derived from the CRRM are 5, 6 or 7 as well as members that are deemed by FICC to pose a heightened risk to FICC and its members based on FICC’s consideration of relevant factors, including those set forth in Section 12(d) of GSD Rule 3 and Section 11(d) of MBSD Rule 3, as applicable.

*B. Proposed Changes to GSD Rule 3 and MBSD Rule 3*

Section 7 of GSD Rule 3 and Section 6 of MBSD Rule 3

FICC is proposing to amend Section 7 of GSD Rule 3 and Section 6 of MBSD Rule 3 to state that review of a GSD Member’s or MBSD Member’s financial or operational conditions may (1) include FICC requesting information regarding the businesses and operations of the member and its risk management practices with respect to FICC’s services utilized by the member for another Person and (2) result in the member being placed on the Watch List and/or being subject to enhanced surveillance as determined by FICC.

FICC members are direct participants of GSD and/or MBSD, as applicable. However, there are firms that rely on the services provided by GSD Members or MBSD Members in order to have their activity cleared and settled through FICC’s facilities (the “indirect participants”). These indirect participants pose certain risks to FICC that need to be identified and monitored as part of FICC’s ongoing member due diligence process. In order for FICC to understand (1) the material dependencies between FICC members and the indirect participants that rely on the FICC members for the clearance and settlement of the indirect participants’ transactions, (2) significant FICC member-indirect participant relationships and (3) the various risk controls and mitigants that these FICC members employ to manage their risks with respect to such relationships, FICC may request information from GSD Members or MBSD Members regarding the members’ businesses and operations as well as their risk management practices with respect to services of FICC utilized by the FICC members for indirect participants. The information

provided by FICC members would then be taken into consideration by FICC when determining whether a GSD Member or an MBSD Member, as applicable, may need to be placed on the Watch List, be subject to enhanced surveillance or both.

Section 12(a) of GSD Rule 3 and Section 11(a) of MBSD Rule 3

FICC is proposing to amend Section 12(a) of GSD Rule 3 and Section 11(a) of MBSD Rule 3 in order to specify the membership types that are currently subject to FICC’s ongoing monitoring and review. FICC currently monitors and reviews all (a) GSD Netting Members, Sponsoring Members and Funds-Only Settling Bank Members and (b) MBSD Members on an ongoing and periodic basis, which may include monitoring news and market developments relating to these members and conducting reviews of financial reports and other public information of these members.

Section 12(b)(i) of GSD Rule 3 and Section 11(b)(i) of MBSD Rule 3

FICC is proposing to add Section 12(b)(i) of GSD Rule 3 and Section 11(b)(i) of MBSD Rule 3 to (1) clarify that FICC is currently using the CRRM to generate credit ratings for (A) GSD Members that are Bank Netting Members and MBSD Members that are Bank Clearing Members; provided that each such member files the Consolidated Report of Condition and Income (“Call Report”) and (B) GSD Members that are Dealer Netting Members or Inter-Dealer Broker Netting Members and MBSD Members that are Dealer Clearing Members or Inter-Dealer Broker Clearing Members; provided that each such member files the Financial and Operational Combined Uniform Single Report (“FOCUS Report”) or the equivalent with its regulator, (2) clarify that each CRRM-Rated Member’s credit rating would be reassessed upon receipt of additional information from the member and (3) delete language that states members may be placed on the Watch List based on their ratings as determined by CRRM or based on their failure to comply with operational standards and requirements.

Currently, Section 11(a) of MBSD Rule 3 states that UIPs are rated by the CRRM. FICC proposes to delete this statement and amend it to state that FICC reviews and monitors UIPs (as with all MBSD Members).<sup>17</sup> This

<sup>17</sup> Amendment No. 1 to SR-FICC-2008-01, approved by the Commission in 2012, eliminated any reference to the CRRM with regards to UIPs; however, due to a clerical error, this change was not

proposed change corrects an error in the MBSD Rules and does not affect any rights or obligations of the MBSD Members because UIPs are still reviewed by FICC through proposed Section 11(a) of MBSD Rule 3.

Section 12(b)(ii) of GSD Rule 3 and Section 11(b)(ii) of MBSD Rule 3

FICC is proposing to add Section 12(b)(ii) of GSD Rule 3 and Section 11(b)(ii) of MBSD Rule 3 to provide that, because the factors used as part of the CRRM may not identify all risks that a member may pose to FICC, FICC may, in addition to other actions permitted by the Rules, downgrade the member's credit rating derived from the CRRM if FICC believes the CRRM-generated rating is insufficiently conservative or if it deems such downgrade as necessary to protect FICC and its members. Depending on the credit rating of the member, a downgrade may result in the member being placed on the Watch List and/or being subject to enhanced surveillance based on relevant factors.

Section 12(c) of GSD Rule 3 and Section 11(c) of MBSD Rule 3

FICC is proposing to re-number the existing Section 12(b) of GSD Rule 3 and Section 11(b) of MBSD Rule 3 to Section 12(c) and Section 11(c) of the respective Rules as well as to amend these sections to state that, other than those members specified in Section 12(b)(i) of GSD Rule 3 and Section 11(b)(i) of MBSD Rule 3, FICC may place (1) GSD Sponsoring Members, Funds-Only Settling Bank Members and Netting Members and (2) MBSD Members, on the Watch List and/or subject them to enhanced surveillance even though they are not being assigned credit ratings by FICC in accordance with the CRRM.

Section 12(d) of GSD Rule 3 and Section 11(d) of MBSD Rule 3

FICC is proposing to add Section 12(d) to GSD Rule 3 and Section 11(d) to MBSD Rule 3 to describe some of the factors that could be taken into consideration by FICC when downgrading a member's credit rating, placing a member on the Watch List and/or subjecting a member to enhanced surveillance. These factors include but are not limited to (i) news reports and/or regulatory observations that raise reasonable concerns relating to the member, (ii) reasonable concerns around the member's liquidity arrangements, (iii) material changes to the member's organizational structure,

(iv) reasonable concerns of FICC about the member's financial stability due to particular facts and circumstances, such as material litigation or other legal and/or regulatory risks, (v) failure of the member to demonstrate satisfactory financial condition or operational capability or if FICC has a reasonable concern regarding the member's ability to maintain applicable membership standards and (vi) failure of the member to provide information required by FICC to assess risk exposures posed by the member's activity.

Section 12(e) of GSD Rule 3 and Section 11(e) of MBSD Rule 3

FICC is proposing to re-number the existing Section 12(c) of GSD Rule 3 and Section 11(c) of MBSD Rule 3 to Section 12(e) and Section 11(e) of the respective Rules and refer to FICC's ability to retain any Excess Clearing Fund Deposits of a GSD Netting Member or an MBSD Clearing Member, as applicable, that has been placed on the Watch List pursuant to Section 9 of GSD Rule 4 or Section 9 of MBSD Rule 4, as applicable. In addition, FICC is proposing technical modifications in these sections to correct grammatical errors and add a section reference.

Section 12(f) of GSD Rule 3 and Section 11(f) of MBSD Rule 3

FICC is proposing to re-number the existing Section 12(d) of GSD Rule 3 and Section 11(d) of MBSD Rule 3 to Section 12(f) and Section 11(f) of the respective Rules and provide that FICC would, in addition to other actions permitted by the Rules, conduct a more thorough monitoring of the financial condition and/or operational capability of, and require more frequent financial disclosures from, not only those members that are placed on the Watch List but also members subject to enhanced surveillance, including examples of how the monitoring could be conducted and the types of disclosures that may be required. In addition, members that are subject to enhanced surveillance would be reported to FICC's management committees and regularly reviewed by a cross-functional team comprised of senior management of FICC.

Other Proposed Changes to GSD Rule 3 and MBSD Rule 3

In addition to the proposed changes described above, FICC is proposing to delete the existing Section 12(e) of GSD Rule 3 and Section 11(e) of MBSD Rule 3 to eliminate FICC's right to place a member with an Excess Capital Ratio of 0.5 or greater on the Watch List because

FICC has not used, nor does it plan to use, this threshold.

In addition, FICC is proposing to delete the existing Section 12(f) of GSD Rule 3 and Section 11(f) of MBSD Rule 3 to eliminate language that requires FICC to place a GSD Netting Member or an MBSD Clearing Member, as applicable, on the Watch List if FICC takes any action against the GSD Netting Member or the MBSD Clearing Member under GSD Rule 3, Section 7 (General Continuance Standards) and MBSD Rule 3, Section 6 (General Continuance Standards), respectively. FICC is proposing these deletions because placement of a member on the Watch List would be covered by the proposed changes to Sections 12(b), (c) and (d) of GSD Rule 3 and Sections 11(b), (c) and (d) of MBSD Rule 3. As such, the language being deleted by this proposed change would no longer be needed.

Similarly, FICC is proposing to delete language that requires a GSD Netting Member or an MBSD Clearing Member, as applicable, to remain on the Watch List until the condition(s) that resulted in its placement on the Watch List are no longer present or if close monitoring by FICC is no longer warranted. FICC is proposing this deletion because whether a member remains on the Watch List would be covered by the proposed changes to Sections 12(b), (c) and (d) of GSD Rule 3 and Sections 11(b), (c) and (d) of MBSD Rule 3. As such, the language being deleted by this proposed change would no longer be needed.

### *C. Proposed Changes to GSD Rules 5, 11 and 18*

FICC is also proposing to amend GSD Rules 5 (Comparison System), 11 (Netting System) and 18 (Special Provisions for Repo Transactions) to clarify that FICC may subject (1) a Comparison-Only Member to enhanced surveillance if FICC has determined that the Comparison-Only Member has violated its obligations under Section 1 of GSD Rule 5 and (2) a Netting Member to enhanced surveillance if FICC has determined that the Netting Member has violated its obligations under Section 3 of GSD Rule 11 or Section 2 of GSD Rule 18. In addition, FICC is proposing to amend GSD Rule 11 to correct a typographical error.

### *Implementation Timeframe*

Pending Commission approval, FICC expects to implement this proposal promptly. Members would be advised of the implementation date of this proposal through issuance of a FICC Important Notice.

included in the Exhibit 5 thereto and therefore not reflected in the current MBSD Rules. See Securities Exchange Act Release No. 66550 (March 9, 2012), 77 FR 15155 (March 14, 2012) (SR-FICC-2008-01). FICC is proposing to correct this error.

## 2. Statutory Basis

Section 17A(b)(3)(F) of the Act requires that FICC's 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 FICC or for which it is responsible.<sup>18</sup>

By enhancing the CRRM to enable it to assign credit ratings to members that are foreign banks or trust companies and that have audited financial data that is publicly available, FICC believes that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act. This is because the proposed rule change expands the CRRM's applicability to a wider group of members, which further improves FICC's membership monitoring process and better enables FICC to safeguard the securities and funds which are in its custody or control or for which it is responsible in furtherance of the Act.

Similarly, by enhancing the CRRM to enable it to incorporate qualitative factors when assigning a member's credit rating, FICC believes that this proposed rule change is consistent with Section 17A(b)(3)(F) of the Act. This is because the proposed rule change would enable FICC to take into account relevant qualitative factors in an automated and more effective manner when monitoring the credit risks presented by the GSD Netting Members and MBSD Clearing Members, thus improving FICC's membership monitoring process overall, which would in turn better enable FICC to safeguard the securities and funds which are in its custody or control or for which it is responsible in furtherance of the Act.

Likewise, by enhancing the CRRM to shift from a relative scoring approach to an absolute scoring approach when assigning a member's credit rating, FICC believes that this proposed rule change is consistent with Section 17A(b)(3)(F) of the Act. This is because the proposed rule change would enable FICC to generate credit ratings for members that are more reflective of the members' default risk, thus improving FICC's membership monitoring process overall, which would in turn better enable FICC to safeguard the securities and funds which are in its custody or control or for which it is responsible in furtherance of the Act.

By providing specificity, clarity and additional transparency to the Rules related to FICC's current ongoing membership monitoring process, FICC

believes that the proposed rule changes to (1) GSD Rule 1 (Definitions of Credit Risk Rating Matrix and Watch List), GSD Rule 3 (Sections 7 and 12), GSD Rule 5 (Comparison System), GSD Rule 11 (Netting System) and GSD Rule 18 (Special Provisions for Repo Transactions) and (2) MBSD Rule 1 (Definitions of Credit Risk Rating Matrix and Watch List) and MBSD Rule 3 (Sections 6 and 11), which are unrelated to the proposed enhancements of the CRRM, are consistent with Section 17A(b)(3)(F) of the Act because the proposed rule changes would help ensure that the Rules remain accurate and clear. Collectively, the proposed changes would help ensure that the Rules are more transparent, accurate and clear, which would help enable all stakeholders to readily understand their respective rights and obligations with GSD's and MBSD's clearance and settlement of securities transactions. Therefore, FICC believes that the proposed rule changes would promote the prompt and accurate clearance and settlement of securities transactions, consistent with Section 17A(b)(3)(F) of the Act.

The proposed enhancements to the CRRM are consistent with Rule 17Ad-22(e)(3)(i) under the Act, which was recently adopted by the Commission.<sup>19</sup> Rule 17Ad-22(e)(3)(i) will require FICC to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing risks that arise in or are born by FICC, which includes . . . systems designed to identify, measure, monitor and manage the range of risks that arise in or are borne by FICC.<sup>20</sup> The proposed enhancements to the CRRM have been designed to assist FICC in identifying, measuring, monitoring and managing the credit risks to FICC posed by its members. The proposed enhancements to the CRRM accomplish this by (i) expanding the CRRM's applicability to a wider group of members to include members that are foreign banks or trust companies, (ii) enabling the CRRM to take into account relevant qualitative factors in an automated and more effective manner when monitoring the credit risks presented by FICC's

members and (iii) enabling the CRRM to generate credit ratings for members that are more reflective of the members' default risk by shifting to an absolute scoring approach, all of which would improve FICC's membership monitoring process overall. Therefore, FICC believes the proposed enhancements to the CRRM would assist FICC in identifying, measuring, monitoring and managing risks that arise in or are born by FICC, consistent with the requirements of Rule 17Ad-22(e)(3)(i).

The proposed rule change to Section 7 of GSD Rule 3 and Section 6 of MBSD Rule 3 with respect to the scope of information that may be requested by FICC from its members has been designed to be consistent with Rule 17Ad-22(e)(19) under the Act, which was recently adopted by the Commission.<sup>21</sup> Rule 17Ad-22(e)(19) will require FICC to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify, monitor, and manage the material risk to FICC arising from arrangements in which firms that are indirect participants in FICC rely on the services provided by GSD Members and MBSD Members to access FICC's payment, clearing, or settlement facilities.<sup>22</sup> By expressly reflecting in the Rules what is already FICC's current practice associated with its request for additional reporting of a GSD Member's or MBSD Member's financial or operational conditions to state that such request may include information regarding the businesses and operations of the member, as well as its risk management practices with respect to services of FICC utilized by the member for another Person, this proposed rule change would help enable FICC to have rule provisions that are reasonably designed to identify, monitor and manage the material risks to FICC arising from tiered participation arrangements consistent with Rule 17Ad-22(e)(19).

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

FICC does not believe that the proposed rule change to (i) enable the CRRM to generate credit ratings for foreign bank or trust company members, (ii) incorporate qualitative factors into the CRRM and (iii) shift to an absolute scoring approach would impose any burden on competition that is not necessary or appropriate in furtherance of the Act.<sup>23</sup> These proposed

<sup>19</sup> 17 CFR 240.17Ad-22(e)(3)(i). The Commission adopted amendments to Rule 17Ad-22, including the addition of new subsection 17Ad-22(e), on September 28, 2016. See Securities Exchange Act Release No. 78961 (September 28, 2016), 81 FR 70786 (October 13, 2016) (S7-03-14). FICC is a "covered clearing agency" as defined by the new Rule 17Ad-22(a)(5) and must comply with new subsection (e) of Rule 17Ad-22 by April 11, 2017. *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> 17 CFR 240.17Ad-22(e)(19). *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> 15 U.S.C. 78q-1(b)(3)(I).

<sup>18</sup> 15 U.S.C. 78q-1(b)(3)(F).

enhancements to the CRRM would improve FICC's member credit risk evaluation process by (1) expanding the CRRM's credit rating capability and thereby providing more comprehensive credit risk coverage of FICC membership, (2) enabling the CRRM to generate more consistent and comprehensive credit ratings for members and thereby reducing the need and frequency for manual downgrades and (3) enabling the CRRM to generate credit ratings for members that are more reflective of the members' default risk. However, FICC recognizes that any change to its member credit risk evaluation process, such as the proposed rule change, may impose a burden on competition in terms of potential impact on members' credit ratings and their Clearing Fund deposits. Nevertheless, FICC believes that any burden on competition derived from the proposed rule change would be necessary and appropriate in furtherance of the Act because the proposed enhancements to the CRRM would help improve FICC's membership monitoring process and thus better enable FICC to safeguard the securities and funds which are in its custody or control or for which it is responsible. Furthermore, the proposed enhancements to the CRRM would also assist FICC in identifying, measuring, monitoring and managing risks that arise in or are born by FICC. As such, FICC does not believe the proposed enhancements to the CRRM would impose any burden on competition that is not necessary or appropriate in furtherance of the Act.

FICC does not believe that the proposed rule changes to (1) GSD Rule 1 (Definitions of Credit Risk Rating Matrix and Watch List), GSD Rule 3 (Sections 7 and 12), GSD Rules 5, 11 and 18 and (2) MBSD Rule 1 (Definitions of Credit Risk Rating Matrix and Watch List) and MBSD Rule 3 (Sections 6 and 11) that are unrelated to the proposed CRRM enhancements would have any impact on competition because each of such proposed rule changes is designed to provide additional specificity, clarity and transparency in the Rules regarding FICC's current ongoing membership monitoring process by expressly providing in the Rules FICC's current practices with respect to such process. As such, these proposed rule changes would not impact FICC members or impose any burden 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. Date of Effectiveness of the Proposed Rule Change, and Timing for Commission Action**

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

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

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

**IV. Solicitation of Comments**

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

*Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FICC-2017-006 on the subject line.

*Paper Comments*

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

All submissions should refer to File Number SR-FICC-2017-006. 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 Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the

Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site 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 Web site (<http://dtcc.com/legal/sec-rule-filings.aspx>). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FICC-2017-006 and should be submitted on or before May 2, 2017.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>24</sup>

**Eduardo A. Aleman,**  
*Assistant Secretary.*

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**SECURITIES AND EXCHANGE COMMISSION**

**Proposed Collection; Comment Request**

*Upon Written Request, Copies Available From:* Securities and Exchange Commission, Office of FOIA Services, 100 F Street NE., Washington, DC 20549-2736

*Extension:*

Rule 15c2-11, SEC File No. 270-196, OMB Control No. 3235-0202

Notice is hereby given that, pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*) ("PRA"), the Securities and Exchange Commission ("Commission") is soliciting comments on the existing collection of information provided for in Rule 15c2-11, (17 CFR 240.15c2-11), under the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*) ("Exchange Act"). The Commission plans to submit this existing collection of information to the Office of Management and Budget ("OMB") for extension and approval.

Rule 15c2-11 under the Securities Exchange Act regulates the initiation or resumption of quotations in a quotation

<sup>24</sup> 17 CFR 200.30-3(a)(12).