

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48089; File No. SR-DTC-2002-06]

### Self-Regulatory Organizations; The Depository Trust Company; Order Approving a Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval of Amendments to a Proposed Rule Change Relating to the Use of the Federal Reserve Banks' Net Settlement System by Settling Banks

June 25, 2003.

#### I. Introduction

On May 7, 2002, The Depository Trust Company filed with the Securities and Exchange Commission ("Commission") a proposed rule change File No. SR-DTC-2002-06 pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposal was published in the **Federal Register** on June 11, 2002.<sup>2</sup> DTC amended the proposal on April 8, 2003,<sup>3</sup> and June 5, 2003.<sup>4</sup> Two comment letters were received.<sup>5</sup> For the reasons discussed below, the Commission is granting accelerated approval of the proposed rule change.<sup>6</sup>

#### II. Description

The Federal Reserve Banks' ("FRBs") Net Settlement Service ("NSS") is an automated mechanism for submitting settlement files to the FRBs and is used by entities in private clearing arrangements that provide for the exchange and settlement of transactions on a net basis. In February 2001, DTC adopted NSS as an alternative method for its participants' settling banks to

satisfy their end-of-day net-net debits at DTC.<sup>7</sup> Under the NSS process, DTC submits an instruction to a FRB on behalf of the settling bank to have the account of the settling bank charged for their DTC end-of-day net-net debit balance. Use of the NSS eliminates the need for a settling bank to initiate a wire to DTC's FRB account in satisfaction of the settling bank's net-net debit balance at DTC. As originally adopted, use of NSS was on a voluntary basis. Currently 43 of the 79 DTC settling banks are using NSS.

Under the rule change, DTC will require all settling banks to use NSS.<sup>8</sup> Settling banks using NSS will be governed by DTC's procedures, including the End-of-Day Settlement Process section of DTC's Settlement Service Guide.<sup>9</sup> Fees connected with the End-of-Day Settlement Process remain unchanged.

Prior to using NSS, settling banks will be required to sign a Settler Agreement with an FRB which incorporates a requirement that the settling bank agrees to the terms of the Fed's Operating Circular No. 12.<sup>10</sup> The signed Settler Agreement must be on the settling bank's letterhead, must be signed by an authorized signer recognized by the FRB, and must be submitted to a FRB through DTC.

Under Section 6.4 of Operating Circular No. 12, the settlement agent (in this case, DTC) has certain responsibilities regarding the allocation among settling banks using NSS of a claim for indemnity by a FRB. In making such an allocation, DTC will apply the same loss allocation procedures found in Section 4 and 9 of DTC's Rules as it would with respect to losses included in DTC's settlement system.

DTC will send a "pre-advice" to each settling bank, notifying the settling bank that DTC is about to send its NSS transmission to the FRB. Each settling bank will be required to acknowledge its net-net debit balance at the end of the

day; however, any settling bank that only settles for its own account may elect to not acknowledge its net debit balance at the end of the day.<sup>11</sup> This option will not be made available to settling banks that settle for others because the acknowledgement process includes the option to refuse to pay for a participant for whom the settling bank provides settlement services. Settling banks that settle for others will also be required to acknowledge their net-net credit balances. DTC will not send a settling bank's net-net debit balance to a FRB for collection until the settling bank has acknowledged its balance.

#### III. Comment Letters

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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Comments may also be submitted electronically at the following e-mail address: [rule-comments@sec.gov](mailto:rule-comments@sec.gov). All comment letters should refer to File No. SR-DTC-2002-06. This file number should be included on the subject line if e-mail is used. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section, 450 Fifth Street, NW., Washington, DC 20549. Electronically submitted comment letters also will be posted on the Commission's web site (<http://www.sec.gov>).<sup>12</sup> Copies of such filing also will be available for inspection and copying at the principal office of the DTC. All submissions

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

<sup>2</sup> Securities Exchange Act Release No. 46028, (June 4, 2002), 67 FR 40035 (June 11, 2002).

<sup>3</sup> The April 8, 2003, amendment deleted the words "attempt to" from the sentence in the filing (the sixth paragraph of section 3 of the filing) that indicated DTC would apply the same loss allocation procedures found in DTC's rules as it would with respect to losses incurred in DTC's settlement system.

<sup>4</sup> The June 5, 2003, amendment added two provisions to the filing. The first provision allowed settling banks to opt out of NSS for one business day under certain circumstances. (See note 8.) The second provision provided that DTC would send a notification prior to DTC's NSS transmission to its account at the FRB.

<sup>5</sup> Letters from Neil T. Henderson, Senior Vice President, JP MorganChase (July 1, 2002); Daniel L. Goelzer, Counsel for the Association, The Association of Global Custodians (July 2, 2002). The commenters have indicated that they no longer object to the Commission approving DTC's amended filing.

<sup>6</sup> A copy of the text of DTC's proposed rule change, the amendments, and the attached exhibits are available at the Commission's Public Reference Section or through DTC.

<sup>7</sup> Exchange Act Release No. 44176 (April 11, 2001), 66 FR 19821 (April 17, 2001) [File No. SR-DTC-2001-02]. See also Important Notice to Participants Nos. 0842 (November 20, 2000) and 2728 (May 2, 2002) and DTC's memorandum (April 14, 2000), all of which are included as part of DTC's filing.

<sup>8</sup> In extenuating circumstances when a settling bank would prefer to opt out of NSS for one business day and to send its wire directly to DTC's account at the FRB in settlement of its net-net debit balance, DTC will exclude that settling bank's debit amount from the NSS transmission that would ordinarily be forwarded to the FRB.

<sup>9</sup> The revised version of the End-of-Day Settlement Process section of the Settlement Service Guide is included as part of DTC's filing.

<sup>10</sup> The Settler Agreement and Operating Circular No. 12 are attached as part of DTC's filing.

<sup>11</sup> Settling banks electing not to acknowledge their debit balance will be required to sign the NSS Settling Bank Acknowledgement Option Form. The form is included as part of DTC's filing. In addition, DTC has made changes to its Settling Bank Failure to Settling Procedures to reflect that certain settling banks may opt out of the acknowledgement requirements. Exchange Act Release No. 41879 (September 15, 1999), 64 FR 51360 (September 22, 1999) [File No. SR-DTC-99-15].

<sup>12</sup> We do not edit personal, identifying information such as names, or e-mail addresses, from electronic submissions. Submit only information you wish to make publicly available.

should refer to File No. SR-DTC-2002-06 and should be submitted by July 28, 2003.

#### IV. Discussion

Section 17A(b)(3)(F) requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible.<sup>13</sup> The rule change should allow DTC to reduce settlement risk and improve its safeguarding of securities and funds by reducing the risk that the completion of settlement will be delayed because a settling bank is late or is unable to wire funds to DTC in settlement of its obligations.

The Commission finds good cause for approving the proposed rule change prior to the thirtieth day after the date of publication of notice of filing. Participants and their settling banks have been on notice for over a year that DTC intended to require the use of NSS, and some have been working with DTC during this time to address procedural or operational issues they had with the DTC proposal. Now that those issues have been resolved by DTC's amendments to the proposed rule change, accelerated approval will allow DTC to implement the requirement to use NSS as soon as possible, which in turn will allow DTC to improve its risk reduction efforts.

#### V. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular with the requirements of section 17A(b)(3)(F) of the Act and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to section 19(b)(2) of the Act, that the proposed rule change (File No. SR-DTC-2002-06) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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### SECURITIES AND EXCHANGE COMMISSION

**[Release No. 34-48110; File No. SR-NASD-2003-97]**

#### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 by the National Association of Securities Dealers, Inc. Relating to Extension on a Pilot Basis of NASD Rule 7010(k) Relating to Fees for the Trade Reporting and Compliance Engine (TRACE)**

June 30, 2003.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 17, 2003, the National Association of Securities Dealers, Inc. ("NASD"), filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. NASD filed an amendment to the proposed rule change on June 27, 2003.<sup>3</sup> NASD has designated the proposed rule change as "establishing or changing a due, fee,

or other charge" under section 19(b)(3)(A)(ii) of the Act<sup>4</sup> and Rule 19b-4(f)(2) thereunder,<sup>5</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

NASD is proposing to amend NASD Rule 7010(k) relating to fees for the Trade Reporting and Compliance Engine ("TRACE") prior to the expiration of the pilot program for fees on June 30, 2003. NASD is proposing to extend the pilot program for TRACE fees to January 31, 2004. NASD is not proposing any revisions to the current fee structure for TRACE as part of this rule filing. Therefore, as a result of the proposed rule change, the current fee structure would remain in effect to January 31, 2004. Below is the text of the proposed rule change. Proposed new language is italicized; proposed deletions are in brackets.

\* \* \* \* \*

#### **7010. System Services**

(a) through (j) No Change.

(k) Trade Reporting and Compliance Engine (TRACE)

(Rule 7010(k) shall expire on [June 30, 2003] *January 31, 2004*, unless amended, extended, or permanently adopted by NASD pursuant to SEC approval at or before such date).

The following charges shall be paid by participants for the use of the Trade Reporting and Compliance Engine ("TRACE"):

System fees	Transaction reporting fees	Market data fees
From 07/01/02 to 12/31/02: Web Browser Access: \$85/month for 1 user ID; \$75/month for 2-9 user IDs; \$70/month for 2-10+ user, IDs, except If less than 25 trades per month, in October, November, or December 2002-\$25/month per user ID	From 07/01/02 to 12/31/02: Trades up to and including \$200,000 par value—\$0.50/trade; Trades between \$201,000 and \$999,999 par value—\$0.0025 times the number of bonds traded/trade; Trades of \$1,000,000 par value or more— \$2.50/trade	BTDS Professional Display—\$60/month per terminal, except For a period of one calendar month to be an- nounced: Waiver of fee (\$0)

<sup>13</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> See letter from Kosha K. Dalal, Assistant General Counsel, NASD, to Katherine A. England, Assistant Director, Division of Market Regulation, SEC, dated June 27, 2003 (Amendment No. 1). In Amendment No. 1, NASD moved the placement of a footnote

marked for deletion in the rule filing to clarify that the footnote was part of the actual rule text and not simply a footnote to the rule filing.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>5</sup> 17 CFR 240.19b-4(f)(2).