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SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-76887; File No. SR-DTC-2015-011)

January 13, 2016

Self-Regulatory Organizations; The Depository Trust Company; Order Approving Proposed Rule Change Regarding the Acknowledgment of End-of-Day Net-Net Settlement Balances by Settling Banks

On November 16, 2015, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") proposed rule change SR-DTC-2015-011 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] and Rule 19b-4 thereunder,[2] to amend DTC's Settlement Service Guide ("Guide")[3] in order to establish a new practice whereby any Settling Bank[4] that (i) fails to affirmatively acknowledge its end-of-day net-net settlement balance,[5] or (ii) does not notify DTC of its refusal to settle on behalf of a Participant or Participants for which it is the designated Settling Bank will be deemed to have acknowledged its end-of-day net-net settlement balance and to make related technical changes and corrections to the Rules, as more fully described below. The proposed rule change was published for comment in the Federal

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 Available at http://www.dtcc.com/~/media/Files/Downloads/legal/service-guides/Settlement.pdf for an overview of the end-of-day net settlement process.

4 A "Settling Bank" is a DTC participant ("Participant") that is a bank and that settles for itself and may settle for other Participants, including other bank Participants.

5 The end-of-day net-net figure is the net of all Participants' net balances after cross-endorsement with the National Securities Clearing Corporation for which a Settling Bank settles, including its own accounts.

Register on November 30, 2015.[6] The Commission did not receive any comment letters on the proposed rule change. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

I. Description of the Proposed Rule Change

The following is a description of the proposed rule change, as provided by DTC:

Background. The DTC[7] end-of-day net settlement structure depends upon the use of Settling Banks.[8] Each Participant must designate a Settling Bank to settle on its behalf. Any Participant that is a bank may settle for itself.[9] Today, a Settling Bank that settles for other Participants must acknowledge its end-of-day net-net settlement balance for the group of Participants for which it settles, or notify DTC if it refuses to settle for any Participant for which it is the designated Settling Bank, by the later of 4:15 p.m. and the time that is 30 minutes after the Settling Bank end-of-day net-net settlement balances are first made available by DTC ("Acknowledgment Cutoff Time").[10]

If a Settling Bank notifies DTC that it refuses to settle for a Participant, DTC would recalculate the Settling Bank's net-net settlement balance by excluding the net

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6 See Securities Exchange Act Release No. 76510 (November 23, 2015), 80 FR 74819 (November 30, 2015) (SR-DTC-2015-011).

7 Terms not otherwise defined herein have the meaning set forth in the DTC Rules (the "Rules"), available at http://www.dtcc.com/legal/rules-and-procedures.aspx.

8 See the Guide, supra note 3, pp. 17–18.

9 See Rule 9(B), supra note 7.

10 Currently, a Settling Bank that settles only for itself may opt out of the requirement to acknowledge its balance, but it cannot refuse to settle for itself.

settlement balance of the Participant for which the Settling Bank refused to settle.[11] DTC would then provide the Settling Bank with its adjusted net-net settlement balance ("Post-Refusal Adjusted Balance"). The Settling Bank may not refuse to settle for any other Participant on that day and must immediately respond to DTC to acknowledge its Post-Refusal Adjusted Balance.

After the Acknowledgment Cutoff Time and any adjustments, DTC will prepare and submit to the National Settlement Service ("NSS") provided by the Federal Reserve Banks (individually and collectively, the "Fed") a file ("NSS File") reflecting the net debits or credits from and to all Settling Banks. NSS will process a debit or credit of each Settling Bank's Fed account ("Fed Account"), as applicable.[12]

Today, failure of a Settling Bank to timely respond to DTC after posting of final settlement figures creates uncertainty with respect to timely completion of settlement at DTC. The proposed rule change will address this issue as discussed below.

<u>Proposal</u>. To promote settlement certainty, DTC has proposed to treat a Settling Bank that fails to timely provide its affirmative acknowledgement of its end-of-day net-net settlement balance or notify DTC of its refusal to settle for one or more Participants for which it is the designated Settling Bank, as having been deemed to acknowledge its end-of-day net-net settlement balance.

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11 Any Participant for which its designated Settling Bank has refused to settle on its behalf remains obligated to DTC for the payment of any net debit balance and must make another arrangement to timely pay that amount by Fedwire.

12 The Guide currently provides that if NSS is unavailable then, if instructed by DTC, Settling Banks in a net-net debit balance must remit payments to DTC via Fedwire by the later of 5:00 p.m. or 1 hour after net settlement balances are first made available. This provision will be clarified to note an operational detail that all such payments must be remitted prior to the close of Fedwire.

DTC has proposed to modify the Guide to provide that a Settling Bank that (i) fails to affirmatively acknowledge its end-of-day net-net settlement balance, or (ii) does not notify DTC of its refusal to settle on behalf of a Participant or Participants for which it is the designated Settling Bank, by the Acknowledgement Cutoff Time, will be deemed to have acknowledged its end-of-day net-net settlement balance.[13] The Settling Bank's balance will then, in the ordinary course of settlement processing, be debited from or credited to its Fed Account through the NSS process. Likewise, DTC has proposed that the Guide provide that a Settling Bank that fails to acknowledge immediately upon receipt its Post-Refusal Adjusted Balance, if any, will be deemed to have acknowledged its Post-Refusal Adjusted Balance and the Post-Refusal Adjusted Balance will then, in the ordinary course of settlement processing, be debited from or credited to its designated Fed Account through the NSS process.

DTC will continue to maintain flexibility and allow for a Settling Bank to request extra time if the Settling Bank has a reason that it cannot affirmatively acknowledge or refuse its net-net settlement balance so long as the Settling Bank notifies DTC accordingly at or before the Acknowledgement Cutoff Time, or, in the case of a Post-Refusal Adjusted Balance, it notifies DTC immediately where it is unable to affirmatively acknowledge its Post-Refusal Adjusted Balance. In this regard, the Guide will be updated to clarify that the Settling Bank is required to notify DTC of its request for extra time via a dedicated DTC Settlement phone "hotline" prior to the

[13] DTC will provide reminders to Settling Banks when they have not affirmatively acknowledged their settlement balance. Notwithstanding delivery of reminders, once a Settling Bank is deemed to have acknowledged its balance, it may not notify DTC of a refusal to settle for a Participant for which it is the designated Settling Bank.

Acknowledgment Cutoff Time. In the event that DTC provides the Settling Bank with a Post-Refusal Adjusted Balance, the Settling Bank will be required to notify DTC of its request for extra time immediately via the hotline. Any Settling Bank that timely complies with this notification requirement will not be deemed to have acknowledged its net-net Settlement Balance or its Post-Refusal Adjusted Balance.[14]

If, after the initial release of final settlement figures, a Settling Bank's net-net settlement balance is adjusted for any reason, other than as a result of the Settling Bank's refusal to settle, then the Acknowledgment Cutoff Time for that Settling Bank will be extended to 30 minutes after DTC advises the Settling Bank of the adjusted net-net settlement balance.

DTC will attempt to contact the Settling Bank if DTC does not receive a response in the form of (i) an acknowledgment or refusal prior to the Acknowledgment Cutoff Time, (ii) an immediate acknowledgment of a Post-Refusal Adjusted Balance, or (iii) a notification from the Settling Bank that it cannot acknowledge or refuse, as described in the preceding paragraph.[15] If DTC is able to contact the Settling Bank and the Settling Bank notifies DTC that it cannot, at that time, acknowledge or refuse its net-net settlement balance, or Post-Refusal Adjusted Balance, as applicable, then the Settling Bank will not be deemed to have acknowledged its net-net settlement balance. However, if the Settling Bank cannot be reached, the Settling Bank will be deemed to have

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14 If the problem is due to a connectivity issue with DTC, DTC may then direct the Settling Bank to submit its acknowledgement/refusal instruction via e-mail or as otherwise specified by DTC at that time.

15 DTC uses the most recent contact information provided by the Settling Bank to its DTC Relationship Manager for this purpose.

acknowledged its net-net settlement balance or Post-Refusal Adjusted Balance, as applicable.

DTC will update the Guide to clarify that each Settling Bank must ensure that it maintains accurate contact details with DTC so that DTC may contact the Settling Bank regarding settlement issues. Settling Banks must update any contact details by contacting their DTC Relationship Manager.

The Fed's cutoff for NSS processing, unless extended, is 5:30 p.m. In order to facilitate timely processing of the NSS File, DTC will maintain discretion to exclude a Settling Bank's balance from the NSS File if the Settling Bank (i) (A) does not acknowledge its net-net settlement balance by the Acknowledgment Cutoff Time, or (B) does not immediately acknowledge its Post-Refusal Adjusted Balance; and (ii) is not deemed to have acknowledged its net-net settlement balance or Post-Refusal Adjusted Balance because it has notified DTC that it is unable to affirmatively acknowledge its net-net settlement balance or to refuse to settle on behalf of a Participant. If DTC proceeds to process the NSS File excluding the Settling Bank's debit balance, then the Settling Bank must pay the debit balance via Fedwire. If DTC proceeds to process the NSS File excluding the Settling Bank's credit balance, then DTC will pay the credit balance via Fedwire after the Settling Bank acknowledges its settlement balance.

The text of the Guide will also state that a Settling Bank which settles on behalf of others that timely notifies DTC that it cannot acknowledge or refuse its end-of-day net-net settlement balance will not be assessed a flat fee for failure to acknowledge or notify DTC of its refusal to settle. However, such a Settling Bank will be charged interest with respect to any borrowing DTC is required to make to complete settlement that day for any Participant that the Settling Bank settles on behalf of, if the Settling Bank has not timely refused to settle for that Participant.

Additionally, DTC will revise the Guide to:

(i) clarify that it is DTC's Settlement Operations group that controls and coordinates the settling of Participant and Settling Bank accounts on DTC's systems;

(ii) define the Federal Reserve Banks individually and collectively within the Guide's text as the "Fed" unless indicated otherwise;

(iii) clarify text for descriptive purposes, and consistent with the Rules, that Participants make formal arrangements for a Settling Bank to be designated as the Settling Bank to settle with DTC on the Participant's behalf;

(iv) clarify that certain online reports DTC provides Participants and Settling Banks through the processing day reflect "intraday" gross debits and credits, and net debit and credit balances;

(v) clarify that a Settling Bank's end-of-day net-net settlement balance includes the Settling Bank's own settlement obligations as a Participant if it settles for itself;

(vi) add text for the purpose of context, consistent with the Rules, that each Participant is obligated to settle timely with DTC and if its Settling Bank refuses to settle for it then it must make alternative arrangements to make payment to DTC via Fedwire;

(vii) add text for the purpose of context, consistent with the Rules, that a Participant that acts as its own Settling Bank may not refuse to settle for itself and that it will be in default if it does not fund its settlement obligation;

(viii) for clarity, change the heading to an existing example of how a Settling Bank's settlement balance is calculated from "Settlement Example" to "Example of the Calculation of a DTC Settling Bank's Net-Net Settlement Balance";

(ix) remove the provision from the Guide indicating that that a Settling Bank that settles only for itself will need to affirmatively opt out in order to not be required to affirmatively acknowledge its settlement balance, and add text simply stating that a Settling Bank that settles only for itself will not be required to acknowledge its settlement balance;

(x) clarify the interest charged to Participants for a failure to settle;

(xi) delete references to a Settling Bank's failure to timely settle its settlement balance from being referred to as a "failure to settle" and remove references to related procedures as being "failure-to-settle" procedures, as the terminology could be confused with an individual Participant's failure to meet its settlement obligation;

(xii) rewrite text in the Guide in light of the proposed changes, as applicable, including Addendum A of the Guide, to incorporate proposed changes, consolidate text, clarify text for readability and eliminate duplication;

(xiii) clarify certain Settling Bank and settlement processing timeframes;

(xiv) apply initial capitalization as appropriate for the terms "Participant" and "Settling Bank" where they are used as defined terms;

(xv) remove references to Participant Terminal System (PTS) functions, which are no longer used for DTC settlement processing; and

(xvi) insert the title of the Guide on the Guide's front page.

Implementation. The effective date of the proposed rule change will be announced via a DTC Important Notice.

II. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act[16] directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and rules and regulations thereunder applicable to such organization. The Commission believes the proposal is consistent with Section 17A(b)(3)(F) of the Act[17] and Rule 17Ad-22(d)(5),[18] as described in detail below.

Consistency with Section 17A(b)(3)(F) of the Act. Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions.[19] As

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16 15 U.S.C. 78s(b)(2)(C).

17 15 U.S.C. 78q-1(b)(3)(F).

18 17 CFR 240.17Ad-22(d)(5).

19 15 U.S.C. 78q-1(b)(3)(F).

described above, the change will reduce delays in the settlement process by allowing DTC to collect net debits and release net credits within scheduled timeframes despite the failure of a Settling Bank to affirmatively acknowledge its end-of-day net-net settlement balance or notify DTC of its refusal to settle for a Participant for which it is the designated Settling Bank on a timely basis. This requirement will reduce uncertainty and associated risks that may currently arise from Failure to Acknowledge, thus facilitating the prompt and accurate clearance and settlement of securities transactions.

Consistency with Rule 17Ad-22(d)(5). Rule 17Ad-22(d)(5) under the Act requires a clearing agency, such as DTC, to establish, implement, maintain and enforce written policies and procedures reasonably designed to employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks and require funds transfers to the clearing agency to be final when effected.[20] As described above, the change should reduce DTC's credit and liquidity risk by mitigating the risk that end-of-day net-net debit settlement balances would not be paid due to the failure of a Settling Bank to respond to DTC after posting of final settlement figures. The change also should create an arrangement that reduces delays in the settlement process by allowing DTC to collect net debits and release net credits within scheduled timeframes, which will limit the settlement risk to DTC. As such, the Commission believes that the proposal is consistent with Rule 17Ad-22(d)(5).[21]

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[20] 17 CFR 240.17Ad-22(d)(5).

[21] Id.

III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act[22] and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that proposed rule change SR-DTC-2015-011 be, and hereby is, APPROVED.[23]

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[24]

Robert W. Errett
Deputy Secretary

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22 15 U.S.C. 78q-1.

23 In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

24 17 CFR 200.30-3(a)(12).

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