

proposal is reasonably designed to (1) publicly disclose all relevant rules and material procedures concerning key aspects of NSCC's default rules and procedures, and (2) provide sufficient information to enable Members to identify and evaluate the risks by participating in NSCC.

Therefore, the Commission believes that NSCC's proposal is consistent with Rules 17Ad-22(e)(23)(i) and (ii) under the Act.<sup>48</sup>

### III. Conclusion

It is therefore noticed, pursuant to Section 806(e)(1)(I) of the Clearing Supervision Act,<sup>49</sup> that the Commission does not object to advance notice SR-NSCC-2017-806, as modified by Amendment No. 1, and that NSCC is authorized to implement the proposal as of the date of this notice or the date of an order by the Commission approving proposed rule change SR-NSCC-2017-018, as modified by Amendment No. 1, whichever is later.

By the Commission.

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

[FR Doc. 2018-18866 Filed 8-29-18; 8:45 am]

BILLING CODE 8011-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-83954; File No. SR-FICC-2017-805]

### Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of No Objection to an Advance Notice, as Modified by Amendment No. 1, To Adopt a Recovery & Wind-Down Plan and Related Rules

August 27, 2018.

On December 18, 2017, Fixed Income Clearing Corporation ("FICC") filed with the Securities and Exchange Commission ("Commission") advance notice SR-FICC-2017-805 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")<sup>1</sup> and Rule 19b-4(n)(1)(i) under the Securities Exchange Act of 1934 ("Act")<sup>2</sup> to adopt a recovery and wind-down plan ("R&W Plan") and related rules.<sup>3</sup> The advance notice was

published for comment in the **Federal Register** on January 30, 2018.<sup>4</sup> In that publication, the Commission also extended the review period of the advance notice for an additional 60 days, pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act.<sup>5</sup> On April 10, 2018, the Commission required additional information from FICC pursuant to Section 806(e)(1)(D) of the Clearing Supervision Act,<sup>6</sup> which tolled the Commission's period of review of the advance notice until 60 days from the date the information required by the Commission was received by the Commission.<sup>7</sup> On June 28, 2018, FICC

of the Act and Rule 19b-4 thereunder ("Proposed Rule Change"). 15 U.S.C. 78s(b)(1) and 17 CFR 240.19b-4, respectively. The Proposed Rule Change was published in the **Federal Register** on January 8, 2018. Securities Exchange Act Release No. 82431 (January 2, 2018), 83 FR 871 (January 8, 2018) (SR-FICC-2017-021). 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. 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). On March 20, 2018, the Commission instituted proceedings to determine whether to approve or disapprove the Proposed Rule Change. Securities Exchange Act Release No. 82913 (March 20, 2018), 83 FR 12997 (March 26, 2018) (SR-FICC-2017-021). 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. Securities Exchange Act Release No. 83509 (June 25, 2018), 83 FR 30785 (June 29, 2018) (SR-DTC-2017-021, SR-FICC-2017-021, SR-NSCC-2017-017). On June 28, 2018, FICC filed Amendment No. 1 to the Proposed Rule Change. Securities Exchange Act Release No. 83630 (July 13, 2018), 83 FR 34213 (July 19, 2018) (SR-FICC-2017-021). FICC submitted a courtesy copy of Amendment No. 1 to the Proposed Rule Change through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the Proposed Rule Change has been publicly available on the Commission's website at <https://www.sec.gov/rules/sro/ficc.htm> since June 29, 2018. The Commission did not receive any comments. The proposal, as set forth in both the advance notice and the Proposed Rule Change, each as modified by Amendments No. 1, shall not take effect until all required regulatory actions are completed.

<sup>4</sup> Securities Exchange Act Release No. 82580 (January 24, 2018), 83 FR 4341 (January 30, 2018) (SR-FICC-2017-805) ("Notice").

<sup>5</sup> Pursuant to Section 806(e)(1)(H) of the Clearing Supervision Act, the Commission may extend the review period of an advance notice for an additional 60 days, if the changes proposed in the advance notice raise novel or complex issues, subject to the Commission providing the clearing agency with prompt written notice of the extension. 12 U.S.C. 5465(e)(1)(H). The Commission found that the advance notice raised novel and complex issues and, accordingly, extended the review period of the advance notice for an additional 60 days until April 17, 2018. See Notice, *supra* note 4.

<sup>6</sup> 12 U.S.C. 5465(e)(1)(D).

<sup>7</sup> See 12 U.S.C. 5465(e)(1)(E)(ii) and (G)(ii); 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>.

filed Amendment No. 1 to the advance notice to amend and replace in its entirety the advance notice as originally filed on December 18, 2017.<sup>8</sup> On July 6, 2018, the Commission received a response to its request for additional information in consideration of the advance notice, which, in turn, added a further 60-days to the review period pursuant to Section 806(e)(1)(E) and (G) of the Clearing Supervision Act.<sup>9</sup> The Commission did not receive any comments. This publication serves as notice that the Commission does not object to the proposed changes set forth in the advance notice, as modified by Amendment No. 1 (hereinafter, "Advance Notice").

### I. Description of the Advance Notice

In the Advance Notice, FICC proposes to (1) adopt an R&W Plan; (2) amend FICC's Government Securities Division ("GSD") Rulebook ("GSD Rules") to (a) adopt Rule 22D (Wind-down of the Corporation) and Rule 50 (Market Disruption and Force Majeure), and (b) make conforming changes to Rule 3A (Sponsoring Members and Sponsored Members), Rule 3B (Centrally Cleared Institutional Triparty Service) and Rule 13 (Funds-Only Settlement) related to the adoption of these proposed rules to the GSD Rules; (3) amend FICC's Mortgage-Backed Securities Division ("MBSD," and, together with GSD, the "Divisions") Clearing Rules ("MBSD Rules") in order to (a) adopt Rule 17B (Wind-down of the Corporation) and Rule 40 (Market Disruption and Force Majeure); and (b) make conforming changes to Rule 3A (Cash Settlement Bank Members) related to the adoption of these proposed rules to the MBSD Rules; and (4) amend Rule 1 of the Electronic Pool Netting ("EPN") Rules of MBSD ("EPN Rules") to provide that EPN Users, as defined therein, are bound by proposed Rule 17B (Wind-down of the Corporation) and proposed Rule 40 (Market Disruption and Force Majeure) to be adopted to the MBSD Rules.<sup>10</sup> Each of the proposed rules is

<sup>8</sup> Securities Exchange Act Release No. 83744 (July 31, 2018), 83 FR 38413 (August 6, 2018) (SR-FICC-2017-805). FICC submitted a courtesy copy of Amendment No. 1 to the advance notice through the Commission's electronic public comment letter mechanism. Accordingly, Amendment No. 1 to the advance notice has been publicly available on the Commission's website at <https://www.sec.gov/rules/sro/ficc-an.htm> since June 29, 2018.

<sup>9</sup> 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>.

<sup>10</sup> The GSD Rules and the MBSD Rules are referred to collectively herein as the "Rules."

Continued

<sup>48</sup> 17 CFR 240.17Ad-22(e)(23)(i) and (ii).

<sup>49</sup> 12 U.S.C. 5465(e)(1)(I).

<sup>1</sup> 12 U.S.C. 5465(e)(1).

<sup>2</sup> 17 CFR 240.19b-4(n)(1)(i).

<sup>3</sup> On December 18, 2017, FICC filed the advance notice as proposed rule change SR-FICC-2017-021 with the Commission pursuant to Section 19(b)(1)

referred to herein as a “Proposed Rule,” and are collectively referred to as the “Proposed Rules.”

FICC states that the R&W Plan would be used by the Board of Directors of FICC (“Board”) and FICC’s management in the event FICC encounters scenarios that could potentially prevent it from being able to provide its critical services as a going concern.

FICC states that the Proposed Rules are designed to (1) facilitate the implementation of the R&W Plan when necessary and, in particular, allow FICC to effectuate its strategy for winding down and transferring its business; (2) provide Members and Limited Members with transparency around critical provisions of the R&W Plan that relate to their rights, responsibilities and obligations;<sup>11</sup> and (3) provide FICC with the legal basis to implement those provisions of the R&W Plan when necessary.

#### A. FICC R&W Plan

The R&W Plan would be structured to provide a roadmap, define the strategy, and identify the tools available to FICC to either (i) recover, in the event it experiences losses that exceed its prefunded resources (such strategies and tools referred to herein as the “Recovery Plan”) or (ii) wind-down its business in a manner designed to permit the continuation of its critical services in the event that such recovery efforts are not successful (such strategies and tools referred to herein as the “Wind-down Plan”). The R&W Plan would identify (i) the recovery tools available to FICC to address the risks of (a) uncovered losses or liquidity shortfalls resulting from the default of one or more Members, and (b) losses arising from non-default events, such as damage to its physical assets, a cyber-attack, or custody and investment losses, and (ii) the strategy for implementation of such tools. The R&W Plan would also establish the strategy and framework for the orderly wind-down of FICC and the transfer of its business in the remote event the implementation of the available recovery tools does not successfully return FICC to financial viability.

As discussed in greater detail below, the R&W Plan would provide, among other matters, (i) an overview of the

Capitalized terms not defined herein are defined in the Rules.

<sup>11</sup> References herein to “Members” refer to GSD Netting Members and MBSB Clearing Members. References herein to “Limited Members” refer to participants of GSD or MBSB other than GSD Netting Members and MBSB Clearing Members, including, for example, GSD Comparison-Only Members, GSD Sponsored Members, GSD CCIT Members, and MBSB EPN Users.

business of FICC and its parent, The Depository Trust & Clearing Corporation (“DTCC”);<sup>12</sup> (ii) an analysis of FICC’s intercompany arrangements and an existing link to another financial market infrastructure (“FMI”); (iii) a description of FICC’s services, and the criteria used to determine which services are considered critical; (iv) a description of the FICC and DTCC governance structure; (v) a description of the governance around the overall recovery and wind-down program; (vi) a discussion of tools available to FICC to mitigate credit/market<sup>13</sup> risks and liquidity risks, including recovery indicators and triggers, and the governance around management of a stress event along a Crisis Continuum timeline; (vii) a discussion of potential non-default losses and the resources available to FICC to address such losses, including recovery triggers and tools to mitigate such losses; (viii) an analysis of the recovery tools’ characteristics, including how they are designed to be comprehensive, effective, and transparent, how the tools provide incentives to Members to, among other things, control and monitor the risks they may present to FICC, and how FICC seeks to minimize the negative consequences of executing its recovery tools; and (ix) the framework and approach for the orderly wind-down and transfer of FICC’s business, including an estimate of the time and costs to effect a recovery or orderly wind-down of FICC.

Certain recovery tools that would be identified in the R&W Plan are based in the Rules (including the Proposed Rules); therefore, descriptions of those tools in the R&W Plan would include descriptions of, and reference to, the applicable Rules and any related internal policies and procedures. Other recovery tools that would be identified in the R&W Plan are based in contractual arrangements to which FICC is a party, including, for example, existing committed or pre-arranged liquidity arrangements. Further, the R&W Plan would state that FICC may develop further supporting internal

<sup>12</sup> DTCC is a user-owned and user-governed holding company and is the parent company of FICC and its affiliates, The Depository Trust Company (“DTC”) and National Securities Clearing Corporation (“NSCC”, and, together with FICC and DTC, the “Clearing Agencies”). The R&W Plan would describe how corporate support services are provided to FICC from DTCC and DTCC’s other subsidiaries through intercompany agreements under a shared services model.

<sup>13</sup> FICC states that it uses the term “credit/market” risks in the R&W Plan because FICC monitors its credit exposure to its Members by managing the market risks of each Member’s unsettled portfolio through the collection of each Division’s Clearing Fund. See *infra* note 23.

guidelines and materials that may provide operational support for matters described in the R&W Plan, and that such documents would be supplemental and subordinate to the R&W Plan.

FICC states that many of the tools available to FICC that would be described in the R&W Plan are FICC’s existing, business-as-usual risk management and Member default management tools, which would continue to be applied in scenarios of increasing stress. In addition to these existing, business-as-usual tools, the R&W Plan would describe FICC’s other principal recovery tools, which include, for example, (i) identifying, monitoring and managing general business risk and holding sufficient liquid net assets funded by equity (“LNA”) to cover potential general business losses pursuant to the Clearing Agency Policy on Capital Requirements (“Capital Policy”),<sup>14</sup> (ii) maintaining the Clearing Agency Capital Replenishment Plan (“Replenishment Plan”) as a viable plan for the replenishment of capital should FICC’s equity fall close to or below the amount being held pursuant to the Capital Policy,<sup>15</sup> and (iii) the process for the allocation of losses among Members, as provided in GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSB Rule 4 (Clearing Fund and Loss Allocation).<sup>16</sup> The R&W Plan would provide governance around the selection and implementation of the recovery tool or tools most relevant to mitigate a stress scenario and any applicable loss or liquidity shortfall.

The development of the R&W Plan is facilitated by the Office of Recovery & Resolution Planning (“R&R Team”) of DTCC.<sup>17</sup> The R&R Team reports to the DTCC Management Committee (“Management Committee”) and is responsible for maintaining the R&W Plan and for the development and ongoing maintenance of the overall recovery and wind-down planning process. The Board, or such committees as may be delegated authority by the Board from time to time pursuant to its charter, would review and approve the R&W Plan biennially, and would also review and approve any changes that

<sup>14</sup> See Securities Exchange Act Release No. 81105 (July 7, 2017), 82 FR 32399 (July 13, 2017) (SR-DTC-2017-003, SR-FICC-2017-007, SR-NSCC-2017-004).

<sup>15</sup> See *id.*

<sup>16</sup> See *supra* note 10.

<sup>17</sup> DTCC operates on a shared services model with respect to FICC and its other subsidiaries. Most corporate functions are established and managed on an enterprise-wide basis pursuant to intercompany agreements under which it is generally DTCC that provides a relevant service to a subsidiary, including FICC.

are proposed to the R&W Plan outside of the biennial review.

As discussed in greater detail below, the Proposed Rules would define the procedures that may be employed in the event of FICC's wind-down and would provide for FICC's authority to take certain actions on the occurrence of a Market Disruption Event, as defined therein. FICC states that the Proposed Rules are designed to provide Members and Limited Members with transparency and certainty with respect to these matters. FICC also states that the Proposed Rules are designed to facilitate the implementation of the R&W Plan, particularly FICC's strategy for winding down and transferring its business, and are designed to provide FICC with the legal basis to implement those aspects of the R&W Plan.

#### 1. Business Overview, Critical Services, and Governance

The introduction to the R&W Plan would identify the document's purpose and its regulatory background, and would outline a summary of the R&W Plan. The stated purpose of the R&W Plan is that it is to be used by the Board and FICC management in the event FICC encounters scenarios that could potentially prevent it from being able to provide its critical services as a going concern.

The R&W Plan would describe DTCC's business profile, provide a summary of the services of FICC as offered by each of the Divisions, and identify the intercompany arrangements and links between FICC and other entities, most notably a link between GSD and Chicago Mercantile Exchange Inc. ("CME"), which is also an FMI. FICC states that the overview section would provide a context for the R&W Plan by describing FICC's business, organizational structure and critical links to other entities. FICC also states that by providing this context, this section would facilitate the analysis of the potential impact of utilizing the recovery tools set forth in later sections of the Recovery Plan, and the analysis of the factors that would be addressed in implementing the Wind-down Plan.

The R&W Plan would provide a description of the critical contractual and operational arrangements between FICC and other legal entities, including the cross-margining agreement between GSD and CME, which is also an FMI.<sup>18</sup> FICC states that this section of the R&W Plan, which identifies and briefly

describes FICC's established links, is designed to provide a mapping of critical connections and dependencies that may need to be relied on or otherwise addressed in connection with the implementation of either the Recovery Plan or the Wind-down Plan.

The R&W Plan would define the criteria for classifying certain of FICC's services as "critical," and would identify those critical services and the rationale for their classification. This section of the R&W Plan would provide an analysis of the potential systemic impact from a service disruption, which FICC states is important for evaluating how the recovery tools and the wind-down strategy would facilitate and provide for the continuation of FICC's critical services to the markets it serves. The criteria that would be used to identify an FICC service or function as critical would include (1) whether there is a lack of alternative providers or products; (2) whether failure of the service could impact FICC's ability to perform its central counterparty services through either Division; (3) whether failure of the service could impact FICC's ability to perform its multilateral netting services through either Division and, therefore, could impact the volume of transactions; (4) whether failure of the service could impact FICC's ability to perform its book-entry delivery and settlement services through either Division and, as such, could impact transaction costs; (5) whether failure of the service could impact FICC's ability to perform its cash payment processing services through either Division and, as such, could impact the flow of liquidity in the U.S. financial markets; and (6) whether the service is interconnected with other participants and processes within the U.S. financial system, for example, with other FMIs, settlement banks, and broker-dealers. The R&W Plan would then list each of those services, functions or activities that FICC has identified as "critical" based on the applicability of these six criteria. The R&W Plan would also include a non-exhaustive list of FICC services that are not deemed critical.

FICC states that the evaluation of which services provided by FICC are deemed critical is important for purposes of determining how the R&W Plan would facilitate the continuity of those services. While FICC's Wind-down Plan would provide for the transfer of all critical services to a transferee in the event FICC's wind-down is implemented, it would anticipate that any non-critical services that are ancillary and beneficial to a critical service, or that otherwise have substantial user demand from the

continuing membership, would also be transferred.

The R&W Plan would describe the governance structure of both DTCC and FICC. This section of the R&W Plan would identify the ownership and governance model of these entities at both the Board and management levels. The R&W Plan would state that the stages of escalation required to manage recovery under the Recovery Plan or to invoke FICC's wind-down under the Wind-down Plan would range from relevant business line managers up to the Board through FICC's governance structure. The R&W Plan would then identify the parties responsible for certain activities under both the Recovery Plan and the Wind-down Plan, and would describe their respective roles. The R&W Plan would identify the Risk Committee of the Board ("Board Risk Committee") as being responsible for oversight of risk management activities at FICC, which include focusing on both oversight of risk management systems and processes designed to identify and manage various risks faced by FICC as well as oversight of FICC's efforts to mitigate systemic risks that could impact those markets and the broader financial system.<sup>19</sup> The R&W Plan would identify the DTCC Management Risk Committee ("Management Risk Committee") as primarily responsible for general, day-to-day risk management through delegated authority from the Board Risk Committee. The R&W Plan would state that the Management Risk Committee has delegated specific day-to-day risk management, including management of risks addressed through margining systems and related activities, to the DTCC Group Chief Risk Office ("GCRO"), which works with staff within the DTCC Financial Risk Management group. Finally, the R&W Plan would describe the role of the Management Committee, which provides overall direction for all aspects of FICC's business, technology, and operations and the functional areas that support these activities.

The R&W Plan would describe the governance of recovery efforts in response to both default losses and non-default losses under the Recovery Plan, identifying the groups responsible for those recovery efforts. Specifically, the R&W Plan would state that the Management Risk Committee provides oversight of actions relating to the default of a Member, which would be

<sup>18</sup> Available at [http://www.dtcc.com/-/media/Files/Downloads/legal/rules/ficc\\_cme\\_crossmargin\\_agreement.pdf](http://www.dtcc.com/-/media/Files/Downloads/legal/rules/ficc_cme_crossmargin_agreement.pdf). See also GSD Rule 43 (Cross-Margining Arrangements), *supra* note 10.

<sup>19</sup> The DTCC, DTC, NSCC, FICC Risk Committee Charter is available at <http://www.dtcc.com/-/media/Files/Downloads/legal/policy-and-compliance/DTCC-BOD-Risk-Committee-Charter.pdf>.

reported and escalated to it through the GCRO, and the Management Committee provides oversight of actions relating to non-default events that could result in a loss, which would be reported and escalated to it from the DTCC Chief Financial Officer (“CFO”) and the DTCC Treasury group that reports to the CFO, and from other relevant subject matter experts based on the nature and circumstances of the non-default event.<sup>20</sup> More generally, the R&W Plan would state that the type of loss and the nature and circumstances of the events that lead to the loss would dictate the components of governance to address that loss, including the escalation path to authorize those actions. Both the Recovery Plan and the Wind-down Plan would describe the governance of escalations, decisions, and actions under each of those plans.

Finally, the R&W Plan would describe the role of the R&R Team in managing the overall recovery and wind-down program and plans for each of the Clearing Agencies.

## 2. FICC Recovery Plan

FICC states that the Recovery Plan is intended to be a roadmap of those actions that FICC may employ across both Divisions to monitor and, as needed, stabilize its financial condition. FICC also states that as each event that could lead to a financial loss could be unique in its circumstances, FICC proposes that the Recovery Plan would not be prescriptive and would permit FICC to maintain flexibility in its use of identified tools and in the sequence in which such tools are used, subject to any conditions in the Rules or the contractual arrangement on which such tool is based. FICC’s Recovery Plan would consist of (1) a description of the risk management surveillance, tools, and governance that FICC would employ across evolving stress scenarios that it may face as it transitions through a Crisis Continuum, described below; (2) a description of FICC’s risk of losses that may result from non-default events, and the financial resources and recovery tools available to FICC to manage those risks and any resulting losses; and (3) an evaluation of the characteristics of the recovery tools that may be used in response to either default losses or non-

default losses. In all cases, FICC states that it would act in accordance with the Rules, within the governance structure described in the R&W Plan, and in accordance with applicable regulatory oversight to address each situation to best protect FICC, the Members, and the markets in which it operates.

### (i) Managing Member Default Losses and Liquidity Needs Through the Crisis Continuum

The Recovery Plan would describe the risk management surveillance, tools, and governance that FICC may employ across an increasing stress environment, which is referred to as the Crisis Continuum. This description would identify those tools that can be employed to mitigate losses, and mitigate or minimize liquidity needs, as the market environment becomes increasingly stressed. The phases of the Crisis Continuum would include (1) a stable market phase, (2) a stress market phase, (3) a phase commencing with FICC’s decision to cease to act for a Member or Affiliated Family of Members<sup>21</sup> (referred to in the R&W Plan as the “Member default phase”), and (4) a recovery phase. In the R&W Plan, the term “cease to act” and the actions that lead to such decision are used within the context of each Division’s Rules, in particular Rules 21 and 22 of the GSD Rules and Rules 14 and 16 of the MBSD Rules.<sup>22</sup> Further, the R&W Plan would, for purposes of the R&W Plan, use the following terms: (1) “Member default” to refer to the event or events that precipitate FICC ceasing to act for a Member or an Affiliated Family; (2) “Defaulting Member” to refer to a Member for which FICC has ceased to act; and (3) “Member Default Losses” to refer to losses that arise out of or relate to the Member default (including any losses that arise from liquidation of that Member’s portfolio), and to distinguish such losses from those that arise out of the business or other events not related to a Member default, which are separately addressed in the R&W Plan.

FICC states that the Recovery Plan would provide context to its roadmap through this Crisis Continuum by describing FICC’s ongoing management of credit, market and liquidity risk across the Divisions, and its existing process for measuring and reporting its risks as they align with established

thresholds for its tolerance of those risks. FICC also states that the Recovery Plan would discuss the management of credit/market risk and liquidity exposures together because the tools that address these risks can be deployed either separately or in a coordinated approach in order to address both exposures. FICC states that it manages these risk exposures collectively to limit their overall impact on FICC and the memberships of the Divisions. FICC states that as part of its market risk management strategy, FICC manages its credit exposure to Members by determining the appropriate required deposits to the GSD and MBSD Clearing Fund and monitoring its sufficiency, as provided for in the applicable Rules.<sup>23</sup> FICC states that it manages its liquidity risks with an objective of maintaining sufficient resources to be able to fulfill obligations that have been guaranteed by FICC in the event of a Member default that presents the largest aggregate liquidity exposure to FICC over the settlement cycle.<sup>24</sup>

The Recovery Plan would outline the metrics and indicators that FICC has developed to evaluate a stress situation against established risk tolerance thresholds. Each risk mitigation tool identified in the Recovery Plan would include a description of the escalation thresholds that allow for effective and timely reporting to the appropriate internal management staff and committees, or to the Board. FICC states that the Recovery Plan is designed to make clear that these tools and escalation protocols would be calibrated across each phase of the Crisis Continuum. The Recovery Plan would also establish that FICC would retain the

<sup>23</sup> See GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation), *supra* note 10. FICC states that because GSD and MBSD do not maintain a guaranty fund separate and apart from the Clearing Fund they collect from Members, FICC monitors its credit exposure to its Members by managing the market risks of each Member’s unsettled portfolio through the collection of each Division’s Clearing Fund. The aggregate of all Members’ Required Clearing Fund deposits to each of GSD or MBSD comprises that Division’s Clearing Fund that represents FICC’s prefunded resources to address uncovered loss exposures as provided in GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation). Therefore, FICC states that its market risk management strategy for both Divisions is designed to comply with Rule 17Ad-22(e)(4) under the Act, where these risks are referred to as “credit risks.” See 17 CFR 240.17Ad-22(e)(4).

<sup>24</sup> FICC’s liquidity risk management strategy, including the manner in which FICC utilizes its liquidity tools, is described in the Clearing Agency Liquidity Risk Management Framework. See Securities Exchange Act Release No. 82377 (December 21, 2017), 82 FR 61617 (December 28, 2017) (SR-DTC-2017-004, SR-FICC-2017-008, SR-NSCC-2017-005).

<sup>20</sup> The R&W Plan would state that these groups would be involved to address how to mitigate the financial impact of non-default losses, and in recommending mitigating actions, the Management Committee would consider information and recommendations from relevant subject matter experts based on the nature and circumstances of the non-default event. Any necessary operational response to these events, however, would be managed in accordance with applicable incident response/business continuity process.

<sup>21</sup> The R&W Plan would define an “Affiliated Family” of Members as a number of affiliated entities that are all Members of either GSD or MBSD.

<sup>22</sup> See GSD Rules 21 (Restrictions on Access to Services) and 22 (Insolvency of a Member), and MBSD Rules 14 (Restrictions on Access to Services) and 16 (Insolvency of a Member), *supra* note 10.

flexibility to deploy such tools either separately or in a coordinated approach, and to use other alternatives to these actions and tools as necessitated by the circumstances of a particular Member default in accordance with the applicable Rules. Therefore, FICC states that the Recovery Plan would both provide FICC with a roadmap to follow within each phase of the Crisis Continuum, and would permit it to adjust its risk management measures to address the unique circumstances of each event.

The Recovery Plan would describe the conditions that mark each phase of the Crisis Continuum, and would identify actions that FICC could take as it transitions through each phase in order to both prevent losses from materializing through active risk management, and to restore the financial health of FICC during a period of stress.

The stable market phase of the Crisis Continuum would describe active risk management activities in the normal course of business. These activities would include (1) routine monitoring of margin adequacy through daily review of back testing and stress testing results that review the adequacy of the margin calculations for each of GSD and MBSD, and escalation of those results to internal and Board committees;<sup>25</sup> and (2) routine monitoring of liquidity adequacy through review of daily liquidity studies that measure sufficiency of available liquidity resources to meet cash settlement obligations of the Member that would generate the largest aggregate payment obligation.<sup>26</sup>

The Recovery Plan would describe some of the indicators of the stress market phase of the Crisis Continuum, which would include, for example, volatility in market prices of certain assets where there is increased uncertainty among market participants about the fundamental value of those assets. This phase would involve general market stresses, when no Member default would be imminent. Within the description of this phase, the Recovery Plan would provide that FICC may take targeted, routine risk management measures as necessary and as permitted by the Rules.

Within the Member default phase of the Crisis Continuum, the Recovery Plan

would provide a roadmap for the existing procedures that FICC would follow in the event of a Member default and any decision by FICC to cease to act for that Member.<sup>27</sup> The Recovery Plan would provide that the objectives of FICC's actions upon a Member or Affiliated Family default are to (1) minimize losses and market exposure of the affected Members and the applicable Division's non-Defaulting Members; and (2), to the extent practicable, minimize disturbances to the affected markets. The Recovery Plan would describe tools, actions, and related governance for both market risk monitoring and liquidity risk monitoring through this phase. Management of liquidity risk through this phase would involve ongoing monitoring of the adequacy of FICC's liquidity resources, and the Recovery Plan would identify certain actions FICC may deploy as it deems necessary to mitigate a potential liquidity shortfall. The Recovery Plan would state that, throughout this phase, relevant information would be escalated and reported to both internal management committees and the Board Risk Committee.

The Recovery Plan would also identify financial resources available to FICC, pursuant to the Rules, to address losses arising out of a Member default. Specifically, GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation) provides that losses remaining after application of the Defaulting Member's resources be satisfied first by applying a Corporate Contribution, and then, if necessary, by allocating remaining losses among the membership in accordance with GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation), as applicable.<sup>28</sup>

In order to provide for an effective and timely recovery, the Recovery Plan would describe the period of time that would occur near the end of the

Member default phase, during which FICC may experience stress events or observe early warning indicators that allow it to evaluate its options and prepare for the recovery phase (referred to in the R&W Plan as the Recovery Corridor). The Recovery Plan would then describe the recovery phase of the Crisis Continuum, which would begin on the date that FICC issues the first Loss Allocation Notice of the second loss allocation round with respect to a given Event Period.<sup>29</sup> The recovery phase would describe actions that FICC may take to avoid entering into a wind-down of its business.

FICC states that it expects that significant deterioration of liquidity resources would cause it to enter the Recovery Corridor. Therefore, the R&W Plan would describe the actions FICC may take at this stage aimed at replenishing those resources. Throughout the Recovery Corridor, FICC would monitor the adequacy of the Divisions' respective resources and the expected timing of replenishment of those resources, and would do so through the monitoring of certain corridor indicator metrics.

FICC states that the majority of the corridor indicators, as identified in the Recovery Plan, relate directly to conditions that may require either Division to adjust its strategy for hedging and liquidating a Defaulting Member's portfolio, and any such changes would include an assessment of the status of the corridor indicators. For each corridor indicator, the Recovery Plan would identify (1) measures of the indicator, (2) evaluations of the status of the indicator, (3) metrics for determining the status of the deterioration or improvement of the indicator, and (4) "Corridor Actions," which are steps that may be taken to

<sup>29</sup> As provided for in GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation), the "Event Period" is ten Business Days beginning on (i) with respect to a Member default, the day on which FICC notifies Members that it has ceased to act for a Member under the Rules, or (ii) with respect to a non-default loss, the day that FICC notifies Members of the determination by the Board that there is a non-default loss event. The proposed GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation) define a "round" as a series of loss allocations relating to an Event Period, and provides that the first Loss Allocation Notice in a first, second, or subsequent round shall expressly state that such notice reflects the beginning of a first, second, or subsequent round. The maximum allocable loss amount of a round is equal to the sum of the Loss Allocation Caps of those Members included in the round. See GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation), *supra* note 10.

<sup>25</sup> FICC's stress testing practices are described in the Clearing Agency Stress Testing Framework (Market Risk). See Securities Exchange Act Release No. 82638 (December 19, 2017), 82 FR 61082 (December 26, 2017) (SR-DTC-2017-005, SR-FICC-2017-009, SR-NSCC-2017-006).

<sup>26</sup> See *supra* note 24 (concerning FICC's liquidity risk management strategy).

<sup>27</sup> See GSD Rule 21 (Restrictions on Access to Services), GSD Rule 22A (Procedures for When the Corporation Ceases to Act), MBSD Rule 14 (Restrictions on Access to Services), and MBSD Rule 17 (Procedures for When the Corporation Ceases to Act), *supra* note 10.

<sup>28</sup> See *supra* note 10. GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation) define the amount FICC would contribute to address a loss resulting from either a Member default or a non-default event as the Corporate Contribution. This amount would be 50 percent of the General Business Risk Capital Requirement, which is calculated pursuant to the Capital Policy and, which FICC states is an amount sufficient to cover potential general business losses so that FICC can continue operations and services as a going concern if those losses materialize, in an effort to comply with Rule 17Ad-22(e)(15) under the Act. See *supra* note 14 (concerning the Capital Policy); 17 CFR 240.17Ad-22(e)(15).

improve the status of the indicator,<sup>30</sup> as well as management escalations required to authorize those steps. FICC states that because FICC has never experienced the default of multiple Members, it has not, historically, measured the deterioration or improvements metrics of the corridor indicators. Therefore, FICC states that these metrics were chosen based on the business judgment of FICC management.

The Recovery Plan would also describe the reporting and escalation of the status of the corridor indicators throughout the Recovery Corridor. Significant deterioration of a corridor indicator, as measured by the metrics set out in the Recovery Plan, would be escalated to the Board. FICC management would review the corridor indicators and the related metrics at least annually, and would modify these metrics as necessary in light of observations from simulations of Member defaults and other analyses. Any proposed modifications would be reviewed by the Management Risk Committee and the Board Risk Committee. The Recovery Plan would estimate that FICC may remain in the Recovery Corridor between one day and two weeks. FICC states that this estimate is based on historical data observed in past Member defaults, the results of simulations of Member defaults, and periodic liquidity analyses conducted by FICC. FICC states that the actual length of a Recovery Corridor would vary based on actual market conditions observed at the time, and FICC would expect the Recovery Corridor to be shorter in market conditions of increased stress.

The Recovery Plan would outline steps by which FICC may allocate its losses, which would occur when and in the order provided in GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation), as applicable.<sup>31</sup> The Recovery Plan would also identify tools that may be used to address foreseeable shortfalls of FICC's liquidity resources following a Member default, and would provide that these tools may be used as appropriate during the Crisis Continuum to address liquidity shortfalls if they arise. FICC states that the goal in managing FICC's qualified liquidity resources is to maximize

<sup>30</sup> The Corridor Actions that would be identified in the R&W Plan are designed to be indicative, but not prescriptive; therefore, if FICC needs to consider alternative actions due to the applicable facts and circumstances, the escalation of those alternative actions would follow the same escalation protocol identified in the R&W Plan for the Corridor Indicator to which the action relates.

<sup>31</sup> See *supra* note 10.

resource availability in an evolving stress situation, to maintain flexibility in the order and use of sources of liquidity, and to repay any third party lenders of liquidity in a timely manner. Additional voluntary or uncommitted tools to address potential liquidity shortfalls which may supplement FICC's other liquid resources described herein, would also be identified in the Recovery Plan. The Recovery Plan would state that, due to the extreme nature of a stress event that would cause FICC to consider the use of these liquidity tools, the availability and capacity of these liquidity tools, and the willingness of counterparties to lend, cannot be accurately predicted and are dependent on the circumstances of the applicable stress period, including market price volatility, actual or perceived disruptions in financial markets, the costs to FICC of utilizing these tools, and any potential impact on FICC's credit rating.

The Recovery Plan would state that FICC will have entered the recovery phase on the date that it issues the first Loss Allocation Notice of the second loss allocation round with respect to a given Event Period. The Recovery Plan would provide that, during the recovery phase, FICC would continue and, as needed, enhance, the monitoring and remedial actions already described in connection with previous phases of the Crisis Continuum, and would remain in the recovery phase until its financial resources are expected to be or are fully replenished, or until the Wind-down Plan is triggered.

The Recovery Plan would describe governance for the actions and tools that may be employed within each phase of the Crisis Continuum, which would be dictated by the facts and circumstances applicable to the situation being addressed. Such facts and circumstances would be measured by the various indicators and metrics applicable to that phase of the Crisis Continuum, and would follow the relevant escalation protocols that would be described in the Recovery Plan. The Recovery Plan would also describe the governance procedures around a decision to cease to act for a Member, pursuant to the applicable Division's Rules, and around the management and oversight of the subsequent liquidation of the Defaulting Member's portfolio. The Recovery Plan would state that, overall, FICC would retain flexibility in accordance with each Division's Rules, its governance structure, and its regulatory oversight, to address a particular situation in order to best protect FICC and the Members, and to meet the primary objectives, throughout

the Crisis Continuum, of minimizing losses and, where consistent and practicable, minimizing disturbance to affected markets.

(ii) Non-Default Losses

The Recovery Plan would outline how FICC may address losses that result from events other than a Member default. While these matters are addressed in greater detail in other documents, this section of the R&W Plan would provide a roadmap to those documents and an outline for FICC's approach to monitoring and managing losses that could result from a non-default event. The R&W Plan would first identify some of the risks FICC faces that could lead to these losses, which include, for example, (1) the business and profit/loss risks of unexpected declines in revenue or growth of expenses; (2) the operational risks of disruptions to systems or processes that could lead to large losses, including those resulting from, for example, a cyber-attack; and (3) custody or investment risks that could lead to financial losses. The Recovery Plan would describe FICC's overall strategy for the management of these risks, which includes a "three lines of defense" approach to risk management that allows for comprehensive management of risk across the organization.<sup>32</sup> The Recovery Plan would also describe FICC's approach to financial risk and capital management. The R&W Plan would identify key aspects of this approach, including, for example, an annual budget process, business line performance reviews with management, and regular review of capital requirements against LNA. These risk management strategies are collectively intended to allow FICC to effectively

<sup>32</sup> FICC states that the "three lines of defense" approach to risk management includes (1) a first line of defense comprised of the various business lines and functional units that support the products and services offered by FICC; (2) a second line of defense comprised of control functions that support FICC, including the risk management, legal and compliance areas; and (3) a third line of defense, which is performed by an internal audit group. The Clearing Agency Risk Management Framework includes a description of this "three lines of defense" approach to risk management, and addresses how FICC comprehensively manages various risks, including operational, general business, investment, custody, and other risks that arise in or are borne by it. Securities Exchange Act Release No. 81635 (September 15, 2017), 82 FR 44224 (September 21, 2017) (SR-DTC-2017-013, SR-FICC-2017-016, SR-NSCC-2017-012). The Clearing Agency Operational Risk Management Framework describes the manner in which FICC manages operational risks, as defined therein. Securities Exchange Act Release No. 81745 (September 28, 2017), 82 FR 46332 (October 4, 2017) (SR-DTC-2017-014, SR-FICC-2017-017, SR-NSCC-2017-013).

identify, monitor, and manage risks of non-default losses.

The R&W Plan would identify the two categories of financial resources FICC maintains to cover losses and expenses arising from non-default risks or events as (1) LNA, maintained, monitored, and managed pursuant to the Capital Policy, which include (a) amounts held in satisfaction of the General Business Risk Capital Requirement,<sup>33</sup> (b) the Corporate Contribution,<sup>34</sup> and (c) other amounts held in excess of FICC's capital requirements pursuant to the Capital Policy; and (2) resources available pursuant to the loss allocation provisions of GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation).<sup>35</sup>

The R&W Plan would address the process by which the CFO and the DTCC Treasury group would determine which available LNA resources are most appropriate to cover a loss that is caused by a non-default event. This determination involves an evaluation of a number of factors, including the current and expected size of the loss, the expected time horizon over when the loss or additional expenses would materialize, the current and projected available LNA, and the likelihood LNA could be successfully replenished pursuant to the Replenishment Plan, if triggered.<sup>36</sup> Finally the R&W Plan would discuss how FICC would apply its resources to address losses resulting from a non-default event, including the order of resources it would apply if the loss or liability exceeds FICC's excess LNA amounts, or is large relative thereto, and the Board has declared the event a Declared Non-Default Loss Event pursuant to GSD Rule 4 (Clearing Fund and Loss Allocation) and MBSD Rule 4 (Clearing Fund and Loss Allocation).<sup>37</sup>

The R&W Plan would also describe proposed GSD Rule 50 (Market Disruption and Force Majeure) and proposed MBSD Rule 40 (Market Disruption and Force Majeure), which FICC is proposing to adopt in the GSD Rule and MBSD Rules, respectively. FICC states that this Proposed Rule is designed to provide transparency around how FICC would address extraordinary events that may occur outside its control. Specifically, the Proposed Rule would define a Market Disruption Event and the governance

around a determination that such an event has occurred. The Proposed Rule would also describe FICC's authority to take actions during the pendency of a Market Disruption Event that it deems appropriate to address such an event and facilitate the continuation of its services, if practicable.

The R&W Plan would describe the interaction between the Proposed Rule and FICC's existing processes and procedures addressing business continuity management and disaster recovery (generally, the "BCM/DR procedures"). FICC states that the intent is to make clear that the Proposed Rule is designed to support those BCM/DR procedures and to address circumstances that may be exogenous to FICC and not necessarily addressed by the BCM/DR procedures. Finally, the R&W Plan would describe that, because the operation of the Proposed Rule is specific to each applicable Market Disruption Event, the Proposed Rule does not define a time limit on its application. However, the R&W Plan would note that actions authorized by the Proposed Rule would be limited to the pendency of the applicable Market Disruption Event, as made clear in the Proposed Rule. FICC states that, overall, the Proposed Rule is designed to mitigate risks caused by Market Disruption Events and, thereby, minimize the risk of financial loss that may result from such events.

### (iii) Recovery Tool Characteristics

The Recovery Plan would describe FICC's evaluation of the tools identified within the Recovery Plan, and its rationale for concluding that such tools are comprehensive, effective, and transparent, and that such tools provide incentives to Members and minimize negative impact on Members and the financial system.

### 3. FICC Wind-Down Plan

The Wind-down Plan would provide the framework and strategy for the orderly wind-down of FICC if the use of the recovery tools described in the Recovery Plan do not successfully return FICC to financial viability. FICC states that while such event is extremely unlikely, given the comprehensive nature of the recovery tools, FICC is proposing a wind-down strategy that provides for (1) the transfer of FICC's business, assets, and memberships of both Divisions to another legal entity, (2) such transfer being effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code,<sup>38</sup> and (3) after effectuating this

transfer, FICC liquidating any remaining assets in an orderly manner in bankruptcy proceedings. FICC states that the proposed transfer approach to a wind-down would meet its objectives of (1) assuring that FICC's critical services will be available to the market as long as there are Members in good standing, and (2) minimizing disruption to the operations of Members and financial markets generally that might be caused by FICC's failure.

In describing the transfer approach to FICC's Wind-down Plan, the R&W Plan would identify the factors that FICC considered in developing this approach, including the fact that FICC does not own material assets that are unrelated to its clearance and settlement activities. Therefore, FICC states that a business reorganization or "bail-in" of debt approach would be unlikely to mitigate significant losses. Additionally, FICC states that the proposed approach was developed in consideration of its critical and unique position in the U.S. markets, which precludes any approach that would cause FICC's critical services to no longer be available.

First, the Wind-down Plan would describe the potential scenarios that could lead to the wind-down of FICC, and the likelihood of such scenarios. The Wind-down Plan would identify the time period leading up to a decision to wind-down FICC as the Runway Period. FICC states that this period would follow the implementation of any recovery tools, as it may take a period of time, depending on the severity of the market stress at that time, for these tools to be effective or for FICC to realize a loss sufficient to cause it to be unable to effectuate settlements and repay its obligations.<sup>39</sup> The Wind-down Plan would identify some of the indicators that it has entered this Runway Period.

The trigger for implementing the Wind-down Plan would be a determination by the Board that recovery efforts have not been, or are unlikely to be, successful in returning FICC to viability as a going concern. As described in the R&W Plan, FICC states that this is an appropriate trigger because it is both broad and flexible enough to cover a variety of scenarios, and would align incentives of FICC and the Members to avoid actions that might undermine FICC's recovery efforts. Additionally, FICC states that this

<sup>39</sup>The Wind-down Plan would state that, given FICC's position as a user-governed financial market utility, it is possible that Members might voluntarily elect to provide additional support during the recovery phase leading up to a potential trigger of the Wind-down Plan, but would also be designed to make clear that FICC cannot predict the willingness of Members to do so.

<sup>33</sup> See *supra* note 28.

<sup>34</sup> See *supra* note 28.

<sup>35</sup> See *supra* note 10.

<sup>36</sup> See *supra* note 14 (concerning the Capital Policy).

<sup>37</sup> See *supra* note 10.

<sup>38</sup> 11 U.S.C. 101 *et seq.*



approach takes into account the characteristics of FICC's recovery tools and enables the Board to consider (1) the presence of indicators of a successful or unsuccessful recovery, and (2) potential for knock-on effects of continued iterative application of FICC's recovery tools.

The Wind-down Plan would describe the general objectives of the transfer strategy, and would address assumptions regarding the transfer of FICC's critical services, business, assets, and membership, and the assignment of GSD's link with another FMI, to another legal entity that is legally, financially, and operationally able to provide FICC's critical services to entities that wish to continue their membership following the transfer ("Transferee"). The Wind-down Plan would provide that the Transferee would be either (1) a third party legal entity, which may be an existing or newly established legal entity or a bridge entity formed to operate the business on an interim basis to enable the business to be transferred subsequently ("Third Party Transferee"); or (2) an existing, debt-free failover legal entity established ex-ante by DTCC ("Failover Transferee") to be used as an alternative Transferee in the event that no viable or preferable Third Party Transferee timely commits to acquire FICC's business. FICC would seek to identify the proposed Transferee, and negotiate and enter into transfer arrangements during the Runway Period and prior to making any filings under Chapter 11 of the U.S. Bankruptcy Code.<sup>40</sup> The Wind-down Plan would anticipate that the transfer to the Transferee be effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code, and pursuant to a bankruptcy court order under Section 363 of the Bankruptcy Code, with the intent that the transfer be free and clear of claims against, and interests in, FICC, except to the extent expressly provided in the court's order.<sup>41</sup>

FICC states that in order to effect a timely transfer of its services and minimize the market and operational disruption of such transfer, FICC would expect to transfer all of its critical services and any non-critical services that are ancillary and beneficial to a critical service, or that otherwise have substantial user demand from the continuing membership. Following the transfer, the Wind-down Plan would anticipate that the Transferee and its continuing membership would determine whether to continue to

provide any transferred non-critical service on an ongoing basis, or terminate the non-critical service following some transition period. FICC's Wind-down Plan would anticipate that the Transferee would enter into a transition services agreement with DTCC so that DTCC would continue to provide the shared services it currently provides to FICC, including staffing, infrastructure and operational support. The Wind-down Plan would also anticipate the assignment of FICC's link arrangements, including its arrangements with clearing banks and GSD's cross-margining arrangement with CME, described above, to the Transferee.<sup>42</sup> The Wind-down Plan would provide that Members' open positions existing prior to the effective time of the transfer would be addressed by the provisions of the proposed Wind-down Rule, as defined and described below, and the existing GSD Rule 22B (Corporation Default) and MBSD Rule 17 (Corporation Default) (collectively, "Corporation Default Rule"), as applicable, and that the Transferee would not acquire any pending or open transactions with the transfer of the business.<sup>43</sup> The Wind-down Plan would anticipate that the Transferee would accept transactions for processing with a trade date from and after the effective time of the transfer.

The Wind-down Plan would provide that, following the effectiveness of the transfer to the Transferee, the wind-down of FICC would involve addressing any residual claims against FICC through the bankruptcy process and liquidating the legal entity. The Wind-down Plan does not contemplate FICC continuing to provide services in any capacity following the transfer time, and any services not transferred would be terminated.

The Wind-down Plan would also identify the key dependencies for the effectiveness of the transfer, which include regulatory approvals that would permit the Transferee to be legally qualified to provide the transferred services from and after the transfer, and approval by the applicable bankruptcy

court of, among other things, the proposed sale, assignments, and transfers to the Transferee.

The Wind-down Plan would address governance matters related to the execution of the transfer of FICC's business and its wind-down. The Wind-down Plan would address the duties of the Board to execute the wind-down of FICC in conformity with (1) the Rules, (2) the Board's fiduciary duties, which mandate that it exercise reasonable business judgment in performing these duties, and (3) FICC's regulatory obligations under the Act as a registered clearing agency. The Wind-down Plan would also identify certain factors the Board may consider in making these decisions, which would include, for example, whether FICC could safely stabilize the business and protect its value without seeking bankruptcy protection, and FICC's ability to continue to meet its regulatory requirements.

The Wind-down Plan would describe (1) actions FICC or DTCC may take to prepare for wind-down in the period before FICC experiences any financial distress, (2) actions FICC would take both during the recovery phase and the Runway Period to prepare for the execution of the Wind-down Plan, and (3) actions FICC would take upon commencement of bankruptcy proceedings to effectuate the Wind-down Plan.

Finally, the Wind-down Plan would include an analysis of the estimated time and costs to effectuate the R&W Plan, and would provide that this estimate be reviewed and approved by the Board annually. In order to estimate the length of time it might take to achieve a recovery or orderly wind-down of FICC's critical operations, as contemplated by the R&W Plan, the Wind-down Plan would include an analysis of the possible sequencing and length of time it might take to complete an orderly wind-down and transfer of critical operations, as described in earlier sections of the R&W Plan. The Wind-down Plan would also include in this analysis consideration of other factors, including the time it might take to complete any further attempts at recovery under the Recovery Plan. The Wind-down Plan would then multiply this estimated length of time by FICC's average monthly operating expenses, including adjustments to account for changes to FICC's profit and expense profile during these circumstances, over the previous twelve months to determine the amount of LNA that it should hold to achieve a recovery or orderly wind-down of FICC's critical operations. The estimated wind-down

<sup>42</sup> The proposed transfer arrangements outlined in the Wind-down Plan do not contemplate the transfer of any credit or funding agreements, which are generally not assignable by FICC. However, to the extent the Transferee adopts rules substantially identical to those FICC has in effect prior to the transfer, FICC states that it would have the benefit of any rules-based liquidity funding. The Wind-down Plan contemplates that neither of the Divisions' respective Clearing Funds would be transferred to the Transferee, as they are not held in a bankruptcy remote manner and they are the primary prefunded liquidity resource to be accessed in the recovery phase.

<sup>43</sup> See *supra* note 10.

<sup>40</sup> See 11 U.S.C. 101 *et seq.*

<sup>41</sup> See 11 U.S.C. 363.



costs would constitute the Recovery/Wind-down Capital Requirement under the Capital Policy.<sup>44</sup> Under that policy, the General Business Risk Capital Requirement is calculated as the greatest of three estimated amounts, one of which is this Recovery/Wind-down Capital Requirement.<sup>45</sup>

FICC states that the R&W Plan is designed as a roadmap, and the types of actions that may be taken both leading up to and in connection with implementation of the Wind-down Plan would be primarily addressed in other supporting documentation referred to therein.

The Wind-down Plan would address proposed GSD Rule 22D and MBSD Rule 17B (Wind-down of the Corporation), which would be adopted to facilitate the implementation of the Wind-down Plan, as discussed below.

### B. Proposed Rules

In connection with the adoption of the R&W Plan, FICC proposes to adopt the Proposed Rules, each of which is described below. FICC states that the Proposed Rules are designed to facilitate the execution of the R&W Plan and are designed to provide Members and Limited Members with transparency as to critical aspects of the R&W Plan, particularly as they relate to the rights and responsibilities of both FICC and Members. FICC also states that the Proposed Rules are designed to provide a legal basis to these aspects of the R&W Plan.

#### 1. GSD Rule 22D and MBSD Rule 17B (Wind-Down of the Corporation)

FICC states that the proposed GSD Rule 22D and MBSD Rule 17B (collectively, "Wind-down Rule") are designed to facilitate the execution of the Wind-down Plan. The Wind-down Rule would include a proposed set of defined terms that would be applicable only to the provisions of this Proposed Rule. FICC states that the Wind-down Rule is designed to make clear that a wind-down of FICC's business would occur (1) after a decision is made by the Board, and (2) in connection with the transfer of FICC's services to a Transferee, as described therein. Because GSD and MBSD are both divisions of FICC, the individual Wind-down Rules are designed to work together. A decision by the Board to initiate the Wind-down Plan would be pursuant to, and trigger the provisions of, the Wind-down Rule of each Division simultaneously. FICC states that, generally, the proposed Wind-

down Rule is designed to create clear mechanisms for the transfer of Eligible Members, Eligible Limited Members, and Settling Banks (as these terms would be defined in the Wind-down Rule), and FICC's business in order to provide for continued access to critical services and to minimize disruption to the markets in the event the Wind-down Plan is initiated.

#### (i) Wind-Down Trigger

First, FICC states that the Proposed Rule is designed to make clear that the Board is responsible for initiating the Wind-down Plan, and would identify the criteria the Board would consider when making this determination. As provided for in the Wind-down Plan and in the proposed Wind-down Rule, the Board would initiate the Wind-down Plan if, in the exercise of its business judgment and subject to its fiduciary duties, it has determined that the execution of the Recovery Plan has not or is not likely to restore FICC to viability as a going concern, and the implementation of the Wind-down Plan, including the transfer of FICC's business, is in the best interests of FICC, Members and Limited Members of both Divisions, its shareholders and creditors, and the U.S. financial markets.

#### (ii) Identification of Critical Services; Designation of Dates and Times for Specific Actions

The Proposed Rule would provide that, upon making a determination to initiate the Wind-down Plan, the Board would identify the critical and non-critical services that would be transferred to the Transferee at the Transfer Time (as defined below and in the Proposed Rule), as well as any non-critical services that would not be transferred to the Transferee. The proposed Wind-down Rule would also establish that any services transferred to the Transferee will only be provided by the Transferee as of the Transfer Time, and that any non-critical services that are not transferred to the Transferee would be terminated at the Transfer Time. The Proposed Rule would also provide that the Board would establish (1) an effective time for the transfer of FICC's business to a Transferee ("Transfer Time"), (2) the last day that transactions may be submitted to either Division for processing ("Last Transaction Acceptance Date"), and (3) the last day that transactions submitted to either Division will be settled ("Last Settlement Date").

#### (iii) Treatment of Pending Transactions

The Wind-down Rule would authorize the Board to provide for the settlement of pending transactions of either Division prior to the Transfer Time, so long as the applicable Division's Corporation Default Rule has not been triggered. The Board would also have the ability to allow Members to only submit trades to the applicable Division that would effectively offset pending positions or provide that transactions will be processed in accordance with special or exception processing procedures. FICC states that the Proposed Rule is designed to enable these actions in order to facilitate settlement of pending transactions of the applicable Division and reduce claims against FICC that would have to be satisfied after the transfer has been effected. If none of these actions are deemed practicable (or if the applicable Division's Corporation Default Rule has been triggered with respect to a Division), then the provisions of the proposed Corporation Default Rule would apply to the treatment of open, pending transactions of such Division.

FICC states that the Proposed Rule is designed to make clear, however, that neither Division would accept any transactions for processing after the Last Transaction Acceptance Date or which are designated to settle after the Last Settlement Date for such Division. Any transactions to be processed and/or settled after the Transfer Time would be required to be submitted to the Transferee, and would not be FICC's responsibility.

#### (iv) Notice Provisions

The proposed Wind-down Rule would provide that, upon a decision to implement the Wind-down Plan, FICC would provide its Members and Limited Members and its regulators with a notice that includes material information relating to the Wind-down Plan and the anticipated transfer of the membership of both Divisions and business, including, for example, (1) a brief statement of the reasons for the decision to implement the Wind-down Plan; (2) identification of the Transferee and information regarding the transaction by which the transfer of FICC's business would be effected; (3) the Transfer Time, Last Transaction Acceptance Date, and Last Settlement Date; and (4) identification of Eligible Members and Eligible Limited Members, and the critical and non-critical services that would be transferred to the Transferee at the Transfer Time, as well as those Non-Eligible Members and Non-Eligible Limited Members (as

<sup>44</sup> See *supra* note 14.

<sup>45</sup> See *supra* note 14.

defined in the Proposed Rule), and any non-critical services that would not be included in the transfer. FICC would also make available the rules and procedures and membership agreements of the Transferee.

(v) Transfer of Membership

The proposed Wind-down Rule would address the expected transfer of both Divisions' membership to the Transferee, which FICC would seek to effectuate by entering into an arrangement with a Failover Transferee, or by using commercially reasonable efforts to enter into such an arrangement with a Third Party Transferee. Therefore, the Wind-down Rule would provide Members, Limited Members and Settling Banks with notice that, in connection with the implementation of the Wind-down Plan and with no further action required by any party, (1) their membership with the applicable Division would transfer to the Transferee, (2) they would become party to a membership agreement with such Transferee, and (3) they would have all of the rights and be subject to all of the obligations applicable to their membership status under the rules of the Transferee. These provisions would not apply to any Member or Limited Member that is either in default of an obligation to FICC or has provided notice of its election to withdraw its membership from the applicable Division. Further, FICC states that the proposed Wind-down Rule is designed to make clear that it would not prohibit (1) Members and Limited Members that are not transferred by operation of the Wind-down Rule from applying for membership with the Transferee, or (2) Members, Limited Members, and Settling Banks that would be transferred to the Transferee from withdrawing from membership with the Transferee.<sup>46</sup>

(vi) Comparability Period

FICC states that the proposed automatic mechanism for the transfer of both Divisions' memberships is intended to provide the membership with continuous access to critical services in the event of FICC's wind-down, and to facilitate the continued prompt and accurate clearance and settlement of securities transactions. The proposed Wind-down Rule would provide that FICC would enter into arrangements with a Failover

Transferee, or would use commercially reasonable efforts to enter into arrangements with a Third Party Transferee, providing that, in either case, with respect to the critical services and any non-critical services that are transferred from FICC to the Transferee, for at least a period of time to be agreed upon ("Comparability Period"), the business transferred from FICC to the Transferee would be operated in a manner that is comparable to the manner in which the business was previously operated by FICC. Specifically, the proposed Wind-down Rule would provide that: (1) The rules of the Transferee and terms of membership agreements would be comparable in substance and effect to the analogous Rules and membership agreements of FICC; (2) the rights and obligations of any Members, Limited Members and Settling Banks that are transferred to the Transferee would be comparable in substance and effect to their rights and obligations as to FICC; and (3) the Transferee would operate the transferred business and provide any services that are transferred in a comparable manner to which such services were provided by FICC. FICC states that the purpose of these provisions and the intended effect of the proposed Wind-down Rule is to facilitate a smooth transition of FICC's business to a Transferee and to provide that, for at least the Comparability Period, the Transferee (1) would operate the transferred business in a manner that is comparable in substance and effect to the manner in which the business was operated by FICC, and (2) would not require sudden and disruptive changes in the systems, operations and business practices of the new members of the Transferee.

(vii) Subordination of Claims Provisions and Miscellaneous Matters

The proposed Wind-down Rule would include a provision addressing the subordination of unsecured claims against FICC of its Members and Limited Members who fail to participate in FICC's recovery efforts (*i.e.*, firms delinquent in their obligations to FICC or elect to retire from FICC in order to minimize their obligations with respect to the allocation of losses, pursuant to the Rules). FICC states that this provision is designed to incentivize Members to participate in FICC's recovery efforts.<sup>47</sup>

The proposed Wind-down Rule would address other ex-ante matters, including provisions providing that its Members, Limited Members and Settling Banks (1) will assist and cooperate with FICC to effectuate the transfer of FICC's business to a Transferee, (2) consent to the provisions of the rule, and (3) grant FICC power of attorney to execute and deliver on their behalf documents and instruments that may be requested by the Transferee. Finally, the Proposed Rule would include a limitation of liability for any actions taken or omitted to be taken by FICC pursuant to the Proposed Rule.

FICC states that the purpose of the limitation of liability is to facilitate and protect FICC's ability to act expeditiously in response to extraordinary events. Such limitation of liability would be available only following triggering of the Wind-down Plan. In addition, and as a separate matter, FICC states that the limitation of liability provides Members with transparency for the unlikely situation when those extraordinary events could occur, as well as supporting the legal framework within which FICC would take such actions. FICC states that these provisions, collectively, are designed to enable FICC to take such acts as the Board determines necessary to effectuate an orderly transfer and wind-down of its business should recovery efforts prove unsuccessful.

2. GSD Rule 50 and MBSD Rule 40 (Market Disruption and Force Majeure)

The proposed GSD Rule 50 and MBSD Rule 40 (Market Disruption and Force Majeure) (collectively, "Force Majeure Rule") would address FICC's authority to take certain actions upon the occurrence, and during the pendency, of a Market Disruption Event, as defined therein. FICC states that because GSD and MBSD are both divisions of FICC, the individual Force Majeure Rules are designed to work together. A decision by the Board or management of FICC that a Market Disruption Event has occurred in accordance with the Force Majeure Rule would trigger the provisions of the Force Majeure Rule of each Division simultaneously. The Proposed Rule is designed to clarify FICC's ability to take actions to address extraordinary events outside of the control of FICC and of the memberships of the Divisions, and to mitigate the effect of such events by facilitating the continuity of services (or, if deemed

<sup>46</sup> The Members and Limited Members whose membership is transferred to the Transferee pursuant to the proposed Wind-down Rule would submit transactions to be processed and settled subject to the rules and procedures of the Transferee, including any applicable margin charges or other financial obligations.

<sup>47</sup> Nothing in the proposed Wind-down Rule would seek to prevent a Member, Limited Member or Settling Bank that retired its membership at either of the Divisions from applying for membership with the Transferee. Once its FICC membership is terminated, however, such firm

would not be able to benefit from the membership assignment that would be effected by this proposed Wind-down Rule, and it would have to apply for membership directly with the Transferee, subject to its membership application and review process.

necessary, the temporary suspension of services). To that end, under the proposed Force Majeure Rule, FICC would be entitled, during the pendency of a Market Disruption Event, to (1) suspend the provision of any or all services, and (2) take, or refrain from taking, or require its Members and Limited Members to take, or refrain from taking, any actions it considers appropriate to address, alleviate, or mitigate the event and facilitate the continuation of FICC's services as may be practicable.

The proposed Force Majeure Rule would identify the events or circumstances that would be considered a Market Disruption Event. The proposed Force Majeure Rule would define the governance procedures for how FICC would determine whether, and how, to implement the provisions of the rule. A determination that a Market Disruption Event has occurred would generally be made by the Board, but the Proposed Rule would provide for limited, interim delegation of authority to a specified officer or management committee if the Board would not be able to take timely action. In the event such delegated authority is exercised, the proposed Force Majeure Rule would require that the Board be convened as promptly as practicable, no later than five Business Days after such determination has been made, to ratify, modify, or rescind the action. The proposed Force Majeure Rule would also provide for prompt notification to the Commission, and advance consultation with Commission staff, when practicable, including notification when an event is no longer continuing and the relevant actions are terminated. The Proposed Rule would require Members and Limited Members to notify FICC immediately upon becoming aware of a Market Disruption Event, and, likewise, would require FICC to notify Members and Limited Members if it has triggered the Proposed Rule and of actions taken or intended to be taken thereunder.

Finally, the Proposed Rule would address other related matters, including a limitation of liability for any failure or delay in performance, in whole or in part, arising out of the Market Disruption Event. FICC states that the purpose of the limitation of liability would be similar to the purpose of the analogous provision in the proposed Wind-down Rule, which is to facilitate and protect FICC's ability to act expeditiously in response to extraordinary events.

### 3. Proposed Changes to GSD Rules, MBSD Rules, and EPN Rules

In order to incorporate the Proposed Rules into the Rules and the EPN Rules, FICC proposes to amend (1) GSD Rule 3A (Sponsoring Members and Sponsored Members), GSD Rule 3B (Centrally Cleared Institutional Triparty Service), and GSD Rule 13 (Funds-Only Settlement); (2) MBSD Rule 3A (Cash Settlement Bank Members); and (3) EPN Rule 1 (Definitions). FICC states that these proposed changes are designed to clarify that certain types of Limited Members, as identified in those rules, would be subject to the Proposed Rules.

## II. Discussion and Commission Findings

Although the Clearing Supervision Act does not specify a standard of review for an advance notice, its stated purpose is instructive: To mitigate systemic risk in the financial system and promote financial stability by, among other things, promoting uniform risk management standards for systemically important financial market utilities and strengthening the liquidity of systemically important financial market utilities.<sup>48</sup>

Section 805(a)(2) of the Clearing Supervision Act<sup>49</sup> authorizes the Commission to prescribe risk management standards for the payment, clearing and settlement activities of designated clearing entities engaged in designated activities for which the Commission is the supervisory agency. Section 805(b) of the Clearing Supervision Act<sup>50</sup> provides the following objectives and principles for the Commission's risk management standards prescribed under Section 805(a):

- To promote robust risk management;
- to promote safety and soundness;
- to reduce systemic risks; and
- to support the stability of the broader financial system.

The Commission has adopted risk management standards under Section 805(a)(2) of the Clearing Supervision Act<sup>51</sup> and Section 17A of the Act<sup>52</sup> ("Rule 17Ad-22").<sup>53</sup> Rule 17Ad-22 requires registered clearing agencies to establish, implement, maintain, and enforce written policies and procedures that are reasonably designed to meet certain minimum requirements for their operations and risk management

practices on an ongoing basis.<sup>54</sup> Therefore, it is appropriate for the Commission to review proposed changes in advance notices against the objectives and principles of these risk management standards as described in Section 805(b) of the Clearing Supervision Act<sup>55</sup> and against Rule 17Ad-22.<sup>56</sup>

### A. Consistency With Section 805(b) of the Clearing Supervision Act

The Commission believes that the proposed changes in the Advance Notice are designed to help FICC promote robust risk management, promote safety and soundness, reduce systemic risks, and support the stability of the broader financial system. As described above, the R&W Plan, generally, would help FICC promote robust risk management and reduce systemic risks by providing FICC with a roadmap for actions it may employ to monitor and manage its risks, and, as needed, to stabilize its financial condition in the event those risks materialize. Specifically, the Recovery Plan would provide a roadmap that would identify a number of triggers for the potential application of a number of available recovery tools. Identifying triggers for the potential application of recovery tools would help promote robust risk management and reduce systemic risks by better enabling FICC to more promptly determine when and how it may need to manage a significant stress event, and, as needed, stabilize its financial condition.

Similarly, the Force Majeure Rule is designed to provide a roadmap to address extraordinary events that may occur outside of FICC's control. Specifically, the Force Majeure Rule would define a Market Disruption Event and provide governance around determining when such an event has occurred. The Force Majeure Rule also would describe FICC's authority to take actions during the pendency of a Market Disruption Event that it deems appropriate to address such an event and facilitate the continuation of FICC's services, if practicable. By defining a Market Disruption Event and providing such governance and authority, the Commission believes that the Force Majeure Rule also would help promote robust risk management and reduce systemic risks by improving FICC's ability to identify and manage a force majeure event, and, as needed, to stabilize its financial condition so that FICC can continue to operate and act as

<sup>48</sup> See 12 U.S.C. 5461(b).

<sup>49</sup> 12 U.S.C. 5464(a)(2).

<sup>50</sup> 12 U.S.C. 5464(b).

<sup>51</sup> 12 U.S.C. 5464(a)(2).

<sup>52</sup> 15 U.S.C. 78q-1.

<sup>53</sup> See 17 CFR 240.17Ad-22.

<sup>54</sup> *Id.*

<sup>55</sup> 12 U.S.C. 5464(b).

<sup>56</sup> See 17 CFR 240.17Ad-22.

a source of stability for the financial markets it serves.

The Commission believes that the Recovery Plan and the Force Majeure Rule reflect an approach designed to allow for a more considered and comprehensive evaluation by FICC of a stressed market situation and the ways in which FICC could apply available recovery tools in a manner intended to minimize the potential negative effects of the stress situation for FICC, its membership, and the broader financial system. Therefore, the Commission believes that the Recovery Plan and the Force Majeure Rule would help promote robust risk management at FICC and, thus, reduce systemic risks by establishing a means for FICC to best determine the most appropriate way to address such stress situations in an effective manner.

The Commission believes that the R&W Plan, generally, would help FICC promote safety and soundness and support the stability of the broader financial system by providing a roadmap to wind-down that is designed to ensure the availability of FICC's critical services to the marketplace, while reducing disruption to the operations of membership and financial markets that might be caused by FICC's failure. Specifically, as described above, the Wind-down Plan, as facilitated by the Wind-down Rule, would provide for the wind-down of FICC's business and transfer of membership and critical services if the recovery tools do not successfully return FICC to financial viability. Accordingly, critical services, such as services that lack alternative providers or products; services that the failure of which could impact the volume of transactions, transaction costs, or the flow of liquidity in the U.S. financial markets; and services that are interconnected with other participants and processes within the U.S. financial system would be able to continue in an orderly manner while FICC is seeking to wind-down its services. By designing the Wind-down Plan and the Wind-down Rule to enable the continuity of FICC's critical services and membership in an orderly manner while FICC is seeking to wind-down its services, the Commission believes these proposed changes would help FICC promote safety and soundness and support stability in the broader financial system in the event the Wind-down Plan is implemented.

As described above, to incorporate the Proposed Rules into the Rules and the EPN Rules, FICC proposes to amend (1) GSD Rule 3A (Sponsoring Members and Sponsored Members), GSD Rule 3B (Centrally Cleared Institutional Triparty

Service), and GSD Rule 13 (Funds-Only Settlement); (2) MBSD Rule 3A (Cash Settlement Bank Members); and (3) EPN Rule 1 (Definitions). These proposed changes would clarify that certain types of Limited Members, as identified in those rules, would be subject to the Proposed Rules. These proposed changes would help these Limited Members readily understand their rights and obligations and would help enable Limited Members that are governed by the Proposed Rules to have a better understanding of the Proposed Rules. Enhanced access to and transparency of these rules would therefore assist such parties in understanding, planning for, and reacting in an orderly manner to, the implementation by FICC of the R&W Plan. Therefore, the Commission believes that these proposed changes to the Rules and the EPN Rules would help support the stability of the broader financial system.

By better enabling FICC to promote robust risk management, promote safety and soundness, reduce systemic risks, and support the stability of the broader financial system, as described above, the Commission believes that the proposed changes in the Advance Notice are consistent with Section 805(b) of the Clearing Supervision Act.<sup>57</sup>

#### *B. Consistency With Rules 17Ad-22(e)(2)(i), (iii), and (v) Under the Act*

Rule 17Ad-22(e)(2)(i) under the Act requires a covered clearing agency<sup>58</sup> to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that are clear and transparent.<sup>59</sup> Rule 17Ad-22(e)(2)(iii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that support the public interest requirements in Section 17A of the Act<sup>60</sup> applicable to clearing agencies, and the objectives of

<sup>57</sup> 12 U.S.C. 5464(b).

<sup>58</sup> A "covered clearing agency" means, among other things, a clearing agency registered with the Commission under Section 17A of the Exchange Act (15 U.S.C. 78q-1 *et seq.*) that is designated systemically important by the Financial Stability Oversight Counsel ("FSOC") pursuant to the Clearing Supervision Act (12 U.S.C. 5461 *et seq.*). See 17 CFR 240.17Ad-22(a)(5)-(6). On July 18, 2012, FSOC designated FICC as systemically important. U.S. Department of the Treasury, "FSOC Makes First Designations in Effort to Protect Against Future Financial Crises," available at <https://www.treasury.gov/press-center/press-releases/Pages/tg1645.aspx>. Therefore, FICC is a covered clearing agency.

<sup>59</sup> 17 CFR 240.17Ad-22(e)(2)(i).

<sup>60</sup> 15 U.S.C. 78q-1.

owners and participants.<sup>61</sup> Rule 17Ad-22(e)(2)(v) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that specify clear and direct lines of responsibility.<sup>62</sup>

As described above, the R&W Plan is designed to identify clear lines of responsibility concerning the R&W Plan including (1) the ongoing development of the R&W Plan; (2) ongoing maintenance of the R&W Plan; (3) reviews and approval of the R&W Plan; and (4) the functioning and implementation of the R&W Plan. As described above, the R&R Team, which reports to the Management Committee, is responsible for maintaining the R&W Plan and for the development and ongoing maintenance of the overall recovery and wind-down planning process. Meanwhile, the Board, or such committees as may be delegated authority by the Board from time to time pursuant to its charter, would review and approve the R&W Plan biennially, and also would review and approve any changes that are proposed to the R&W Plan outside of the biennial review. Moreover, the R&W Plan would state the stages of escalation required to manage recovery under the Recovery Plan or to invoke FICC's wind-down under the Wind-down Plan, which would range from relevant business line managers up to the Board. The R&W Plan would identify the parties responsible for certain activities under both the Recovery Plan and the Wind-down Plan, and would describe their respective roles. The R&W Plan also would specify the process FICC would take to receive input from various parties at FICC, including management committees and the Board.

In considering the above, the Commission believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that are clear and transparent because it would specify lines of control. The Commission also believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that support the public interest requirements in Section 17A of the Act<sup>63</sup> applicable to clearing

<sup>61</sup> 17 CFR 240.17Ad-22(e)(2)(iii).

<sup>62</sup> 17 CFR 240.17Ad-22(e)(2)(v).

<sup>63</sup> 15 U.S.C. 78q-1.

agencies, and the objectives of owners and participants because the R&W Plan specifies the process FICC would take to receive input from various FICC stakeholders. In addition, the Commission believes that the R&W Plan would help contribute to establishing, implementing, maintaining, and enforcing written policies and procedures reasonably designed to provide for governance arrangements that specify clear and direct lines of responsibility because it specifies who is responsible for the ongoing development, maintenance, reviews, approval, functioning, and implementation of the R&W Plan.

Therefore, the Commission believes that the R&W Plan is consistent with Rules 17Ad-22(e)(2)(i), (iii), and (v) under the Act.<sup>64</sup>

#### *C. Consistency With Rule 17Ad-22(e)(3)(ii) Under the Act*

Rule 17Ad-22(e)(3)(ii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by the covered clearing agency, which includes plans for the recovery and orderly wind-down of the covered clearing agency necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.<sup>65</sup>

As described above, the R&W Plan's Recovery Plan provides a plan for FICC's recovery necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses by defining the risk management activities, stress conditions and indicators, and tools that FICC may use to address stress scenarios that could eventually prevent FICC from being able to provide its critical services as a going concern. More specifically, through the framework of the Crisis Continuum, which identifies tools that can be employed to mitigate losses and mitigate or minimize liquidity needs as the market environment becomes increasingly stressed, the Recovery Plan would identify measures that FICC may take to manage risks of credit losses and liquidity shortfalls, and other losses that could arise from a Member default. The Recovery Plan also would address FICC's management of general business risks and other non-default risks that could lead to losses by identifying

potential non-default losses and the resources available to FICC to address such losses, including recovery triggers and tools to mitigate such losses. Therefore, the Commission believes that the R&W Plan's Recovery Plan helps FICC establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by FICC, which includes a recovery plan necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.

As described above, the R&W Plan's Wind-down Plan provides a plan for orderly wind-down of FICC, which would be triggered by a determination by the Board that recovery efforts have not been, or are unlikely to be, successful in returning FICC to viability as a going concern. Once triggered, the Wind-down Plan sets forth mechanisms for the transfer of the membership of both Divisions and FICC's business, and it is designed to maintain continued access to FICC's critical services and to minimize market impact of the transfer while FICC is seeking to ultimately wind-down its services. Specifically, the Wind-down Plan would provide for the transfer of FICC's business, assets, and membership to another legal entity with such transfer being effected in connection with proceedings under Chapter 11 of the U.S. Bankruptcy Code.<sup>66</sup> After effectuating this transfer, FICC would liquidate any remaining assets in an orderly manner in bankruptcy proceedings.

Although the Commission is not opining on the Wind-down Plan's consistency with the U.S. Bankruptcy Code, in reviewing the proposed changes, the Commission believes that FICC's intent to use bankruptcy proceedings to achieve an orderly liquidation of assets after any transfer of FICC's business appears reasonable, in light of the provisions of the Bankruptcy Code that address the liquidation and distribution of a debtor's property among creditors and interest holders.<sup>67</sup> Under many circumstances, Section 363 of the Bankruptcy Code provides for the sale of property "free and clear of any interest in such property of an entity other than the estate[.]"<sup>68</sup> The Commission believes that FICC's analysis regarding the applicability of

these provisions, while not free from doubt, presents a reasonable approach to liquidation in light of the circumstances and the available alternatives.<sup>69</sup> Therefore, the Commission believes that the R&W Plan's Wind-down Plan helps FICC establish, implement, maintain, and enforce written policies and procedures reasonably designed to maintain a sound risk management framework for comprehensively managing legal, credit, liquidity, operational, general business, investment, custody, and other risks that arise in or are borne by FICC, which includes a wind-down plan necessitated by credit losses, liquidity shortfalls, losses from general business risk, or any other losses.

Therefore, the Commission believes that the R&W Plan is consistent with Rule 17Ad-22(e)(3)(ii) under the Act.<sup>70</sup>

#### *D. Consistency With Rules 17Ad-22(e)(15)(i)-(ii) Under the Act*

Rule 17Ad-22(e)(15)(i) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that the covered clearing agency can continue operations and services as a going concern if those losses materialize, including by determining the amount of liquid net assets funded by equity based upon its general business risk profile and the length of time required to achieve a recovery or orderly wind-down, as appropriate, of its critical operations and services if such action is taken.<sup>71</sup> Rule 17Ad-22(e)(15)(ii) under the Act requires a covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that the covered clearing agency can continue operations and services as a going concern if those losses materialize, including by holding liquid net assets funded by equity equal to the greater of either (x) six months of the

<sup>69</sup> The Wind-down Plan would identify certain factors the Board may consider in evaluating alternatives, which would include, for example, whether FICC could safely stabilize the business and protect its value without seeking bankruptcy protection, and FICC's ability to continue to meet its regulatory requirements.

<sup>70</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>71</sup> 17 CFR 240.17Ad-22(e)(15)(i).

<sup>64</sup> 17 CFR 240.17Ad-22(e)(2)(i), (iii), and (v).

<sup>65</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>66</sup> 11 U.S.C. 101 *et seq.*

<sup>67</sup> *See, e.g.*, 11 U.S.C. 363, 726, and 1129(a)(7).

<sup>68</sup> *See* 11 U.S.C. 363(f).

covered clearing agency's current operating expenses, or (y) the amount determined by the board of directors to be sufficient to ensure a recovery or orderly wind-down of critical operations and services of the covered clearing agency, as contemplated by the plans established under Rule 17Ad-22(e)(3)(ii) under the Act,<sup>72</sup> discussed above.<sup>73</sup>

As discussed above, FICC's Capital Policy is designed to address how FICC holds LNA in compliance with these requirements,<sup>74</sup> while the Wind-down Plan would include an analysis to estimate the amount of time and cost to achieve a recovery or orderly wind-down of FICC's critical operations and services, and would provide that the Board review and approve this analysis and estimation annually. The Wind-down Plan also would provide that the estimate would be the Recovery/Wind-down Capital Requirement under the Capital Policy. Under that policy, the General Business Risk Capital Requirement, which is the amount of LNA that FICC plans to hold to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialize, is calculated as the greatest of three estimated amounts, one of which is this Recovery/Wind-down Capital Requirement. Therefore, the Commission believes that the R&W Plan is consistent with Rules 17Ad-22(e)(15)(i) and (ii) under the Act.<sup>75</sup>

### III. Conclusion

It is therefore noticed, pursuant to Section 806(e)(1)(I) of the Clearing Supervision Act,<sup>76</sup> that the Commission DOES NOT OBJECT to advance notice SR-FICC-2017-805, as modified by Amendment No. 1, and that FICC is authorized to implement the proposal as of the date of this notice or the date of an order by the Commission approving proposed rule change SR-FICC-2017-021, as modified by Amendment No. 1, whichever is later.

By the Commission.

**Eduardo A. Aleman,**

*Assistant Secretary.*

[FR Doc. 2018-18868 Filed 8-29-18; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 33214; File No. 812-14837]

### Innovator ETFs Trust, et al.

August 24, 2018.

**AGENCY:** Securities and Exchange Commission ("Commission").

**ACTION:** Notice.

Notice of an application for an order under section 12(d)(1)(J) of the Investment Company Act of 1940 (the "Act") for an exemption from sections 12(d)(1)(A), (B), and (C) of the Act and under sections 6(c) and 17(b) of the Act for an exemption from section 17(a) of the Act. The requested order would permit certain registered open-end investment companies to acquire shares of certain registered open-end investment companies, registered closed-end investment companies, business development companies, as defined in section 2(a)(48) of the Act ("BDCs"), and registered unit investment trusts (collectively, "Underlying Funds") that are within and outside the same group of investment companies as the acquiring investment companies, in excess of the limits in section 12(d)(1) of the Act.

**APPLICANTS:** Innovator ETFs Trust (the "Trust"), a Delaware statutory trust that is registered under the Act as an open-end management investment company with multiple series, Innovator Capital Management, LLC (the "Initial Adviser"), a limited liability company organized under the laws of the state of Delaware that is registered as an investment adviser under the Investment Advisers Act of 1940, and Foreside Fund Services, LLC (the "Distributor"), registered as a broker-dealer under the Securities Exchange Act of 1934 (the "1934 Act") and a member of the Financial Industry Regulatory Authority.

**FILING DATES:** The application was filed on October 31, 2017, and amended on May 1, 2018.

**HEARING OR NOTIFICATION OF HEARING:** An order granting the requested relief will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on September 18, 2018, and should be accompanied by proof of service on the applicants, in the form of an affidavit, or, for lawyers, a certificate of service. Pursuant to rule 0-5 under

the Act, hearing requests should state the nature of the writer's interest, any facts bearing upon the desirability of a hearing on the matter, the reason for the request, and the issues contested.

Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

**ADDRESSES:** Secretary, U.S. Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

Applicants: Innovator ETFs Trust and Innovator Capital Management, LLC, 120 North Hale Street, Suite 200, Wheaton, IL 60187; Foreside Fund Services, LLC, Three Canal Plaza, Suite 100, Portland, ME 04101.

**FOR FURTHER INFORMATION CONTACT:** Christine Y. Greenlees, Senior Counsel, at (202) 551-6879, or Andrea Ottomanelli Magovern, Branch Chief, at (202) 551-6821 (Division of Investment Management, Chief Counsel's Office).

**SUPPLEMENTARY INFORMATION:** The following is a summary of the application. The complete application may be obtained via the Commission's website by searching for the file number, or for an applicant using the Company name box, at <http://www.sec.gov/search/search.htm> or by calling (202) 551-8090.

### Summary of the Application

1. Applicants request an order to permit (a) each Fund<sup>1</sup> (each a "Fund of Funds") to acquire shares of Underlying Funds<sup>2</sup> in excess of the limits in sections 12(d)(1)(A) and (C) of the Act and (b) each Underlying Fund that is a registered open-end management

<sup>1</sup> Applicants request that the order apply not only to the existing series of the Trust (the "Initial Funds"), but that the order also extend to any future series of the Trust and any other existing or future registered open-end management investment companies and any series thereof that are part of the same "group of investment companies," as defined in section 12(d)(1)(G)(ii) of the Act, as the Trust and are, or may in the future be, advised by the Initial Adviser or its successor or any other investment adviser controlling, controlled by, or under common control with the Initial Adviser or its successor (together with the Initial Funds, each series a "Fund," and collectively, the "Funds"). Applicants further request that the order also apply to any future principal underwriter and distributor for a Fund. For purposes of the requested order, "successor" is limited to an entity that results from a reorganization into another jurisdiction or a change in the type of business organization. For purposes of the request for relief, the term "group of investment companies" means any two or more registered investment companies, including closed-end investment companies, and BDCs, that hold themselves out to investors as related companies for purposes of investment and investor services.

<sup>2</sup> Certain of the Underlying Funds have obtained exemptions from the Commission necessary to permit their shares to be listed and traded on a national securities exchange at negotiated prices and, accordingly, to operate as an exchange-traded fund ("ETF").

<sup>72</sup> 17 CFR 240.17Ad-22(e)(3)(ii).

<sup>73</sup> 17 CFR 240.17Ad-22(e)(15)(ii).

<sup>74</sup> *Supra* note 14.

<sup>75</sup> 17 CFR 240.17Ad-22(e)(15)(i) and (ii).

<sup>76</sup> 12 U.S.C. 5465(e)(1)(I).