

The Commission believes that temporarily exempting CCOS from Sections 17A(b)(3)(B) and 17A(b)(4)(B) of the Act is appropriate. CCOS rules do not meet the requirements of Section 17A(b)(3)(B) of the Act with regard to participants because CCOS rules do not provide for membership by all of the enumerated categories of persons. In addition, CCOS rules do not specify applicant and member financial standards as contemplated in Section 17A(b)(4)(B) of the Act.⁷⁰ Financial and operational membership standards depend on factors that CCOS will develop based on the scope of CCOS's operations. CCOS's Board of Directors will review these factors from time to time and establish membership standards based on its findings. Presently, however, the participant standards have not been determined as required by the Act, and an exemption from participation requirements is appropriate.

C. Comments and the Commission's Responses

1. Fragmentation of the Clearance and Settlement of Government Securities

Some commenters believe that approval of CCOS's exemption application will result in fragmentation of the clearance and settlement of government securities and will preclude one account settlement. These commenters believe allowing CCOS to settle government securities trades in a manner not effectively integrated with the existing registered clearing corporation process would be deleterious to the systemic risk management currently provided by GSCC by causing lowered overall netting capability, incomplete management of the risk exposure presented by individual firms, and impairment of crisis management. The commenters argue that government securities transactions will operate in the safest and most efficient manner if participants have all of their government securities trades netted, margined, and settled through one central facility ("one account settlement").⁷¹

Following Commission approval of its application and upon receipt of a bona fide request for access, CCOS will prepare and submit to the Commission for review, rules providing broader access to CCOS services for persons other than those currently envisioned by the CCOS Rules, consistent with the requirements of Section 17A of the Act.

⁷⁰ CCOS Rule 302 and Rule 309 anticipate the determination of participant financial standards by the Board of Directors. At this time, however, the standards remain undefined.

⁷¹ One-account settlement enables a market participant to settle all of its trades through one clearing agency regardless of the location of the

Although commenters fear fragmentation in the clearance and settlement of government securities, the clearance and settlement of government securities transactions already is subject to diverse clearing arrangements. While GSCC is the only registered clearing agency providing clearance and settlement services in the government securities market, it is not the sole government securities clearing facility. Banks currently clear and settle substantial amounts of government securities transfers among themselves through the Federal Reserve System's book-entry wire system without any involvement by GSCC. Furthermore, BOTCC provides clearance and settlement services for futures and options on government securities including the physical delivery of government securities to satisfy futures delivery obligations.

Section 17A(a)(2) of the Act directs the Commission, having due regard for the maintenance of fair competition among clearing agencies, to facilitate the establishment of linked or coordinated facilities for clearance and settlement of transactions in securities, securities options, contracts of sale for future delivery and options thereon, and commodity options.⁷² Moreover, the requirement in Section 17A(b)(3)(B)(ii) that clearing agencies admit other clearing agencies as participants appears to indicate that Congress, and the Commission which worked with Congress in developing the 1975 Amendments,⁷³ contemplated a national system for the clearance and settlement of securities transactions in which there could be multiple clearing agencies serving a securities market.

Where more than one clearing agency for a market exists, the Commission believes that the linking of these clearing agencies, such as the envisioned linkage of CCOS, BOTCC, and GSCC, promotes competition and innovation while still allowing for one-account settlement. The Commission believes that one-account settlement can be achieved in a multiple-clearing agency environment through the use of interclearing agency links and interfaces.⁷⁴

other parties to the trades and regardless of the markets in which the trades were executed.

⁷² *Standards Release*, *supra* note 53.

⁷³ Securities Acts Amendments of 1975, Pub. L. No. 94-29 § 17A(a), 89 Stat. 97.

⁷⁴ In the Commission release addressing conditions for the National Securities Clearing Corporation's ("NSCC") approval as a clearing agency, the Commission stated that "even though a broker-dealer would be able to achieve one account processing through any one of the clearing corporation components of the National System, a broker-dealer would be able to use more than one

The approach to one-account processing for the clearance and settlement of government securities transactions advocated by GSCC, where one clearing agency compares, nets, and settles all trades in government securities, is not the approach taken by the Commission when establishing the National System for clearance and settlement. The Commission believes that rather than mandate centralized clearance and settlement in the government securities market, it should encourage the coordination of any competing systems through economically efficient linkages that ultimately will foster both competition and investor confidence. For these reasons, the Commission, as a part of its granting CCOS an exemption from clearing agency registration, is urging CCOS, BOTCC, and GSCC to develop settlement interface and cross-margining programs.⁷⁵

2. Illusory Regulatory Oversight

As stated above, BOTCC will be the sole shareholder and will act as the facilities manager for the CCOS operations. Because of the relationship between CCOS and BOTCC, some commenters expressed concern that the Commission would be unable to oversee appropriately the operations of CCOS. Furthermore, these commenters stated that the Commission's regulatory authority over CCOS would be illusory because CCOS would be controlled and operated by BOTCC. These commenters stated that CCOS is merely a shell for BOTCC and that approval of CCOS's application will allow BOTCC to provide clearance and settlement services for government securities. Finally, several commenters noted their concern with and objection to CCOS performing the services of a registered clearing agency without the federal oversight imposed upon all other registered clearing agencies. These commenters argued that for the safety and soundness of the national clearance and settlement system, CCOS should be subject to the same standards and requirements as all other registered clearing agencies.

Under the proposal, CCOS will share office space and staff with BOTCC, and BOTCC will perform all margin calculations and collection and payment

clearing corporation if the broker-dealer chose to do so." Later in that same release the Commission stated, "The development and expansion of interfaces during the past year, particularly the establishment of regional interfaces for the processing of over-the-counter transactions, has made one-account processing almost universally available." Securities Exchange Act Release No. 12954 (November 3, 1976), 41 FR 49722.

⁷⁵ *Supra* note 45.