

File No. SR-EMCC-00-3

Securities and Exchange Commission  
Washington, D.C. 20549

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Form 19b-4

Proposed Rule Change

By

EMERGING MARKETS CLEARING CORPORATION

Pursuant to Rule 19b-4 under the  
Securities Exchange Act of 1934

1. Text of Proposed Rule Change.

(a) The text of the proposed rule change provides Emerging Markets Clearing Corporation (“EMCC”) the right, in its discretion, to exclude from an inter dealer broker Member’s “Minimum Margin Amount” additional margin that such Member has posted to the clearing fund due to its contra-party’s failure to timely submit one or more trades to EMCC, once the underlying trade(s) have been compared or settled. The text of the proposed rule change is set forth on Exhibit A.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization.

(a) The proposed rule change has been approved by the Board of Directors of EMCC.

(b) Contact regarding questions and comments:

Merrie Faye Witkin (212) 855-3208

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change.

(a) EMCC’s Rules require that inter-dealer broker Members (“IDBs”) be margined in the same way as dealer Members. Rule 4, Section 5(A) of EMCC’s Rules requires Members’ Clearing Fund deposits to equal the greater of (i) their Daily Margin Amount (i.e., the amount calculated for each Member on each business day) and (ii) their

Minimum Margin Amount (i.e., their "Floor"). The Floor is the amount equal to the largest single Daily Margin Amount computed for a Member during the relevant calendar month and the previous calendar month.

As EMCC has developed and expanded its membership base, there have been concerns about the effect of late trade matching on IDBs. That is, where an IDB submits its trades on a timely basis, as do one of its contra-parties, but the other contra-party dealer does not, the IDB will be required to post additional clearing fund with EMCC. EMCC's Addendum B requires the late submitting dealer in that situation to cover the IDB's financing cost of such excess clearing fund deposit. Addendum B does not, however, address the impact of such additional margin requirement on the computation of the IDB's Floor. The intent of requiring the additional margin from the IDB was only to cover EMCC's risk exposure until the trade was compared or settled. As written, the IDB Member would have to maintain that additional amount on deposit as its Floor for an additional 30 to 60 days. Accordingly, the proposed rule would amend Rule 4 to permit EMCC, in its discretion once the underlying trade(s) are compared or settled, to exclude the additional margin from the calculation of the IDB's Floor, and thus return the excess clearing fund so posted by the IDB.

(b) This rule change should encourage IDB's to become participants in EMCC, and therefore facilitate the prompt and accurate clearance and settlement of emerging market securities transactions. The proposed rule change is therefore consistent with the requirements of the Securities Exchange Act of 1934, as amended (the "Act"), and the rules and regulations thereunder.

4. Self-Regulatory Organization's Statement on Burden on Competition.

EMCC does not believe that the proposed rule change will have an impact on or impose a burden on competition.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others.

No written comments relating to the proposed rule change have been solicited or received. EMCC will notify the Securities and Exchange Commission (the "Commission") of any written comments received by EMCC.

6. Extension of Time Period for Commission Action.

EMCC does not consent to an extension of the time period specified in Section 19(b)(2) of the Act for Commission action.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2).

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

(d) EMCC requests accelerated approval of the filing. Accelerated approval will

facilitate EMCC's timely return to its IDB members of excess clearing fund deposits, thus reducing the costs to those members of using EMCC's clearance and settlement services. Accordingly EMCC requests that the Commission approve this filing by April 5, 2000.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission.

The proposed rule change is not based on a rule either of another self-regulatory organization or of the Commission.

9. Exhibits.

Exhibit A Text of the proposed change to EMCC's Rules.

Exhibit B Notice of the proposed rule change for publication in the Federal Register.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the self-regulatory organization has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

EMERGING MARKETS CLEARING CORPORATION

BY: \_\_\_\_\_  
Karen L. Saperstein

General Counsel

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EXHIBIT A

**Underlined, boldface** text indicates additions.

~~[Bracketed, strikedout]~~ text indicates deletions.

RULE 4

CLEARING FUND, MARGIN AND LOSS ALLOCATION

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SEC. 5. (A) Margin Amount

A Member's Margin Amount shall equal the greater of such Member's (i) Minimum Margin Amount and (ii) Daily Margin Amount. The "Minimum Margin Amount" shall equal the largest single final Daily Margin Amount computed for a Member for the month during which such Margin Amount calculation is being performed and the previous calendar month<sup>1</sup>. The "Daily Margin Amount" for a Member shall be equal to:

**((Mark to Market Amount) + (Volatility Amount)) x (Event Factor) x (Global Holiday Factor)**

- I. The **Mark to Market Amount** shall equal, the sum of the following amounts calculated with respect to each (A) pending Receive and Deliver Obligation including (i) those for which the Scheduled Settlement Date is the day on which such calculation is being performed and for which the Corporation has not received notice that such Obligation has settled from a Qualified Securities Depository and, (ii) those for which the Scheduled Settlement Date is after the day on which such calculation is being performed, and (B) Fail Receive or Fail Deliver Obligation for which the Corporation has not received notice that such Obligation has settled from a Qualified Securities Depository:

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<sup>1</sup> **Provided, however, that the Minimum Margin Amount applicable to an Inter Dealer Broker Member may be adjusted by the Corporation as follows: Where an Inter Dealer Broker Member has deposited additional margin on any Business Day due to a contra-party's failure to timely submit one or more trades, then once such trades have been compared or settled, the Corporation may, in its discretion, reduce the Inter Dealer Broker Member's Minimum Margin Amount to an amount which excludes such additional margin.**

Value of Position<sup>2</sup> - Contract Value<sup>3</sup>

If the Mark to Market Amount is a negative number, such Member's Mark to Market Amount shall equal the absolute value of such number. If the Mark to Market Amount is a positive number, the Mark to Market Amount with respect to such Member shall equal zero.

- II. The **Volatility Amount** shall equal the following, which, (A) with respect to the preliminary Required Fund Deposit, shall be calculated with respect to each (i) pending Receive and Deliver Obligation including (x) those for which the Scheduled Settlement Date is the day on which such calculation is being performed and for which the Corporation has not received notice from a Qualified Securities Depository that such Obligation has settled, (y) those for which the Scheduled Settlement Date is after the day on which such calculation is being performed, and (ii) Fail Receive or Fail Deliver Obligation for which the Corporation has not received notice that such Obligation has settled from a Qualified Securities Depository, and (B) with respect to the final Required Fund Deposit, shall be calculated with respect to each (i) Receive and Deliver Obligation for which the Scheduled Settlement Date is on or after the day on which such calculation is being performed (regardless of whether or not such transaction has settled), and (ii) pending Fail Receive or Fail Deliver Obligation (determined as of the day prior to the day on which such calculation is being performed, regardless of whether such Fail Receive or Deliver Obligation has since settled):

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<sup>2</sup> For purposes of the Mark to Market Amount calculation relating to any particular ISIN, "Value of Position" equals the product of the quantity of the net EMCC Eligible Instrument position in such ISIN and the Current Market Price of such ISIN, with Deliver Obligations having a negative value and Receive Obligations having a positive value.

<sup>3</sup> For the purposes of calculating an Inter Dealer Broker's Margin Amount in connection with its preliminary Required Fund Deposit, uncomparated EMCC Eligible Instrument transaction data received by the Corporation which (i) has been submitted by the Inter Dealer Broker, (ii) names a Member as a contra party, and (iii) involve transactions for which the trade date is indicated as being the date on which this calculation is being performed, shall be deemed to be "comparated"; furthermore, (a) to the extent such transactions are sell trades, they shall be deemed to be "Deliver Obligations", (b) to the extent such transactions are buy trades, they shall be deemed to be "Receive Obligations" and (c) the settlement day as indicated in such data shall be deemed to be the "Scheduled Settlement Date." To the extent any transaction meets the requirements of clauses (i) and (ii) of the preceding sentence due to a systems failure of a contra-party that results in the contra-party being unable to submit any transactions to the relevant Locked-In Trade Source, clauses (a) through (c) of the preceding sentence shall apply to such transactions.

(1) The sum of the absolute value of: Value of Position<sup>4</sup> X II liquid Percentage, with respect to each net position in an EMCC Eligible Instruments having a Liquidity Category of L4.

PLUS

(2) The sum of the larger of (A) or (B), calculated with respect to L1, L2 and L3 EMCC Eligible Instruments in each country in which the Member has a net position in an EMCC Eligible Instrument, of:

(A) The absolute value of the sum of the following:

(i) For each net Long Position in an L1 or L2 EMCC Eligible Instrument:

Value of Position X 2 SD

PLUS

(ii) For each net Long Position in an L3 EMCC Eligible Instrument:

Value of Position X 4 SD

PLUS

(iii) For each net Short Position in an L1 or L2 EMCC Eligible Instrument:

Value of Position X 2 SD X smallest Correlation Coefficient<sup>5</sup> between any EMCC Eligible Instrument in which such Member has a net Short Position and any EMCC Eligible Instrument in which such Member has a net Long Position

PLUS

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<sup>4</sup> For purposes of the Volatility Amount calculation relating to any particular ISIN, "Value of Position" equals the sum of the Contract Values of Receive and Deliver Obligations and Fail Receive and Fail Deliver Obligations relating to such ISIN.

<sup>5</sup> The Corporation shall calculate, based on price data for a period of one year furnished by a Qualified Financial Information Provider, a pairwise correlation coefficient (the "Correlation Coefficient"), to the extent available, for each pair of EMCC Eligible Instruments, other than Liquidity Category L4 Instruments, within the same country.

(iv) For each net Short Position in an L3 EMCC Eligible Instrument:

Value of Position X 1 SD X smallest Correlation Coefficient  
between any EMCC Eligible Instrument in which such Member  
has a net Short Position and any EMCC Eligible Instrument in  
which such Member has a net Long Position

OR

(B) The absolute value of the sum of the following:

(i) For each net Short Position in an L1 or L2 EMCC Eligible  
Instrument:

Value of Position X 2 SD

PLUS

(ii) For each net Short Position in an L3 EMCC Eligible Instrument:

Value of Position X 4 SD

PLUS

(iii) For each net Long Position in an L1 or L2 EMCC Eligible  
Instrument:

Value of Position X 2 SD X smallest Correlation Coefficient  
between any EMCC Eligible Instrument in which such Member  
has a net Long Position and any EMCC Eligible Instrument in  
which such Member has a net Short Position

PLUS

(iv) For each Long Position in an L3 EMCC Eligible Instrument:

Value of Position X 1 SD X smallest Correlation Coefficient  
between any EMCC Eligible Instrument in which such Member  
has a net Long Position and any EMCC Eligible Instrument in  
which such Member has a net Short Position.

The Corporation shall assign one of the following Liquidity Categories<sup>6</sup> for each EMCC Eligible Instrument based upon the average bid/offer spread for each such EMCC Eligible Instrument:

Liquidity Category 1 ("L1"): having an average monthly bid/offer spread equal to or less than 3/8 of a point;

Liquidity Category 2 ("L2"): having an average monthly bid/offer spread equal to or less than 3/4 of a point;

Liquidity Category 3 ("L3"): having an average monthly bid/offer spread equal to or less than 2 points; and

Liquidity Category 4 ("L4"): (i) having an average monthly bid/offer spread greater than 2 points or (ii) those EMCC Eligible Instruments for which the Corporation has received reports of no trading activity (based on such criteria as the Corporation may determine from time to time) and for such time period as the Corporation may determine from time to time.

For purposes of the above calculations, the term "SD" shall refer to the higher of two standard deviation calculations relative to each EMCC Eligible Instrument, one over a time interval of 1 year and the other over a time interval of 3 months. In each case the Corporation shall calculate a standard deviation based on the following formula over each time interval:

$$\ln ((P_{x+5}) \div (P_x))$$

where  $P_x$  is the price of the EMCC Eligible Instrument on any day and  $P_{x+5}$  is the price of the EMCC Eligible Instrument 5 trading days later.

The number of SDs applied in each of the above calculations may be changed by the Corporation from time to time in order to protect the interests of the Corporation and its Members. Such changes may be made on an overall, Member-by-Member, EMCC Eligible Instrument-by-EMCC Eligible Instrument or position-by-position basis.

- III. The **Event Factor** shall equal 1.25 or such other factor as the Corporation may from time to time determine is appropriate for a particular Member or all Members, in order to protect the interests of the Corporation and its Members.

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<sup>6</sup> The Corporation may assign a liquidity category ("Liquidity Category") to an EMCC Eligible Instrument based on a factor other than the average bid/offer spread, as it so determines from time to time in order to protect the interests of the Corporation and its Members.

IV. The **Global Holiday Factor** shall be a multiple, determined by the Corporation from time to time to be necessary to protect the interests of the Corporation and its Members, in the event that banks in the U.S. are closed on a day on which EMCC Eligible Instruments may be traded.

(B) Payment of Required Fund Deposit Amounts:

(i) At such time as determined by the Corporation, the Corporation shall make available to each Member a Report which indicates a preliminary Required Fund Deposit and the amount, if any, which the Corporation may require to be paid to the Corporation (the "Preliminary Margin Report").

(ii) During the morning of each Business Day, the Corporation shall make available to each Member a Report stating the final Required Fund Deposit (the "Final Margin Report"). If the difference between the Required Fund Deposit and the Members actual Clearing Fund Deposit is less than U.S. \$100,000, the Final Margin Report shall indicate that the Member has no additional obligation to make a payment to the Corporation. If the difference between the Required Fund Deposit and the actual Clearing Fund Deposit is U.S. \$100,000 or greater, the Final Margin Report shall indicate the amount of such difference and the Member shall be required to pay the amount of such difference to the Corporation on such Business Day.

(iii) A Member that has a payment obligation, pursuant to this Rule, shall cause such payment to be received by the account of the Corporation at a depository institution designated by the Corporation to receive such payment, in immediately available funds, by no later than the later of 11:30 a.m. New York City time or one hour after the Final Margin Report listing such obligation is made available to the Member on such Business Day, unless the Member provides notice to the Corporation within such time period of its election to terminate its membership with the Corporation.

#### SEC. 6. Liability of a Member

Each Member shall pay, or reimburse the Corporation, for all losses, costs, expenses, and charges (including attorneys' fees) incurred by the Corporation as the result of any failure of such Member to fulfill its obligations to the Corporation pursuant to this Rule. In addition, the Corporation may fine a Member for an Overnight Exposure Cap Violation.

If a Member fails to pay to the Corporation in a timely manner any portion of a Margin Amount as required pursuant to this Rule (hereinafter, the "Unpaid Balance"), the Corporation, in its sole discretion, may apply to payment of the Unpaid Balance all or a

portion of any monies owing by the Corporation to such Member, and/or all or a portion of such Member's deposits to the Clearing Fund or other collateral of such Member held by the Corporation. If the Corporation satisfies all or a portion of the Unpaid Balance through use of the Corporation's own funds or funds borrowed from third parties, such Member shall be liable, in addition to the amount of the Unpaid Balance, for the costs of any such borrowing, including, without limitation, interest from the Business Day on which the failure to pay the Unpaid Balance occurred until and including the Business Day on which the Member pays to the Corporation the Unpaid Balance (or, if later, the Business Day on which funds borrowed from a third party are repaid by the Corporation to such party). The interest rate applicable to funds advanced by the Corporation pursuant to this Section shall be the Federal Funds Rate plus one percent.

If the Board, in its sole discretion, determines that a Member has, without good cause, failed to pay to the Corporation in a timely manner pursuant to this Rule a Margin Amount, it may impose a fine upon such Member. As used in this Section, "good cause" means a causal event or occurrence that the Board, in its sole discretion, determines was beyond the reasonable control of a Member; depending upon the specific circumstances, this may include an extended failure of FedWire or the inability to gain access to FedWire by a depository institution acting on behalf of either a Member or the Corporation.

#### SEC. 7. Surveillance Status

The Corporation may require a Member that has been placed on surveillance status by the Corporation, as provided for below, to make and maintain a deposit to the Clearing Fund over and above the amounts determined in accordance with Sections 3, 4 and 5 above of this Rule, which additional deposit shall be part of the Member's Required Fund Deposit.

A Member shall be placed on surveillance status by the Corporation if one or more of the following factors is present:

- (a) member fails to meet any financial conditions set forth in Rule 2;
- (b) any element of its capital position falls below that which would be required in Rule 2 if it were applying to become a Member;
- (c) it temporarily experiences either an inability to meet its money settlement obligations to the Corporation in a timely fashion or another significant cash flow problem;
- (d) it temporarily experiences an inability to meet its securities settlement obligations in a timely fashion;

(e) there occurs a significant reorganization or change in control or management of the Member that, in the judgment of the Board, is likely to impair the Member's ability to meet its money settlement obligations or securities settlement obligations to the Corporation; or

(f) it has been placed on a special surveillance status by another Self-Regulatory Organization, or for Non-U.S. Registered Broker-Dealers and Non-U.S. Banks, comparable regulatory organization.

In addition, a Member may be placed on surveillance status by the Corporation if one or more of the following factors is present:

(g) it temporarily experiences a significant operational problem;

(h) any position of the Member is significantly disproportionate to its usual activity, in light of current industry conditions;

(i) the Corporation receives (i) a notification from a Member's Designated Examining Authority or Appropriate Regulatory Agency, or (ii) for Non-U.S. Registered Broker-Dealers and Non-U.S. Banks, notification from a comparable regulatory organization of a pending administrative action regarding, or investigation of, the Member that could call into question the Member's ability to meet its obligations to the Corporation; or

(j) it experiences any condition that could materially affect its financial or operational capability so as to potentially increase the Corporation's exposure to loss or liability.

## SEC. 8. Form of Deposit

Subject to the provisions of Section 2 of this Rule governing the computation of deposits, and the limitations of this Section 8, a Member's deposits to the Clearing Fund may be in the form of:

(a) cash, or

(b) an open account indebtedness fully secured by Eligible Treasury Securities and/or Eligible Letters of Credit.

Cash deposits to the Clearing Fund shall be made in immediately available funds.

Eligible Treasury Securities that are used to secure an open account indebtedness

must be pledged to the Corporation on such terms and conditions as it may require, and be delivered to either the Corporation or to a depository institution approved by the Corporation that shall hold the securities on the Corporation's behalf. The valuation of such Eligible Treasury Securities shall be at 95% of current market value, which shall be determined by the Corporation periodically.

Upon appropriate notice to the Corporation, pursuant to procedures that the Corporation establishes for such purpose, and subject to reasonable time constraints imposed by the Corporation based on its operational and administrative capacities, a Member may substitute and/or withdraw securities from pledge and deposit, provided that the Member has, effective immediately prior to the withdrawal, taken appropriate action to maintain its Required Fund Deposit. Notwithstanding the above sentence, the Corporation may decline to permit a substitution or withdrawal on a given Business Day later than one hour or less prior to the close of the securities FedWire on such Business Day. Any interest on securities deposited by a Member to secure a Clearing Fund open account indebtedness that is received by the Corporation shall be credited to the Member's cash deposits to the Clearing Fund, except in the event of a default by a Member in payment of any of its obligations to the Corporation, in which case the Corporation may first liquidate such securities and apply all or a portion thereof, including any interest thereon, as provided in Section 10 of this Rule.

With regard to Eligible Letters of Credit that secure a Clearing Fund open account indebtedness issued on behalf of a Member pursuant to this Rule:

- (a) such letters of credit must be delivered to either the Corporation or to a depository institution designated by the Corporation to hold such letters on the Corporation's behalf;
- (b) the Corporation shall have the right, to refuse to approve, or to revoke its approval of, any institution as an Approved Letter of Credit Issuer, at any time when, in the judgment of the Corporation, such action, in light of its statutory responsibility, is necessary or appropriate;
- (c) the open account indebtedness secured by letters of credit may constitute no more than 70 percent of a Member's Required Fund Deposit; provided, however, that the greater of U.S. \$100,000 or ten percent of the Member's Required Fund Deposit up to a maximum of U.S. \$1,000,000 is required to be in cash;
- (d) notwithstanding designation of a depository institution as an Approved Letter of Credit Issuer, the Corporation shall not accept a letter of credit from a Member that is issued by such Member or by an Affiliate of such Member;
- (e) the Corporation shall not accept a letter of credit issued by any institution

if, as a result of such acceptance, more than 20 percent of the total Clearing Fund consists of letters of credit issued by that institution;

(f) the Corporation, in its discretion, may not accept a letter of credit that it determines is not readily pledgeable by it in order to obtain credit in an amount as determined by the Corporation from time to time.

(g) letters of credit shall be valued at 95 percent of their stated value;

(h) letters of credit deposited in the Clearing Fund must expire at noon, New York time, on either the April 1 or October 1 immediately following the issuance thereof (whichever comes first) provided, however, that any letter of credit deposited during the months of March or September must expire on the following October 1 or April 1, respectively;

(i) a Member must obtain and deposit with the Corporation, not less than 10 calendar days prior to the expiration of any letter of credit securing an open account indebtedness to the Clearing Fund, either an amendment of such letter of credit extending its expiration date by six months but to no more than two years from the date of original issuance, a new letter of credit or such Member substitutes cash and/or Eligible Treasury Securities sufficient to maintain its Required Fund Deposit; and

(j) with respect to any letter of credit issued pursuant to this Rule, any amount drawn on such letter of credit by the Corporation shall be deposited into, and constitute an additional cash deposit to, the Clearing Fund and shall reduce the Member's open account indebtedness by a corresponding amount.

Upon appropriate notice to the Corporation, pursuant to procedures that the Corporation shall establish for such purpose, and subject to reasonable time constraints imposed by the Corporation based on its operational and administrative capacities, a Member may substitute and/or withdraw letters of credit from pledge and deposit, provided that the Member has, effective immediately prior to such substitution or withdrawal, taken appropriate action to maintain its Required Fund Deposit. Notwithstanding the above sentence, the Corporation may decline to permit on a given Business Day a substitution or withdrawal later than one hour or less prior to the close of the securities FedWire on such Business Day.

## SEC. 9. Lien

As security for any and all obligations and liabilities of a Member to the Corporation, each such Member grants to the Corporation a first priority perfected security interest in all assets and property placed by a Member in the possession of the

Corporation (or its agents acting on its behalf), including all securities and cash on deposit with the Corporation or its agents pursuant to this Rule. The Corporation shall be entitled to its rights as a pledgee under common law and as a secured party under Articles 8 and 9 of the New York Uniform Commercial Code with respect to such collateral.

#### SEC. 10. Use of Deposits and Payments

The use of the Clearing Fund deposits shall be limited to

(1) satisfaction of losses or liabilities of the Corporation arising from the failure of a Member to satisfy an obligation to the Corporation; and

(2) providing the Corporation with a source of cash or collateral to meet the following temporary financing needs:

(A) financing the temporary receipt by the Corporation, pursuant to the Rules, of EMCC Eligible Instruments that cannot be redelivered to a Member due to the inability of the Member to pay for them, provided that such inability constitutes the failure by the Member to meet its securities settlement obligations to the Corporation (including, but not limited to, situations in which the Corporation has ceased to act for the Member);

(B) financing on an intra-day basis only, the receipt pursuant to the Rules of EMCC Eligible Instruments that will be redelivered to another Member at a Qualified Securities Depository, provided that no more than ten percent (10%) of the total Clearing Fund may be used for this purpose, and provided further that Eligible Letters of Credit shall be used for this purpose to the maximum extent practicable prior to the use of any Eligible Treasury Securities for this purpose and that cash shall not be used for this purpose;<sup>7</sup> and

(C) temporarily financing the amount of any loss or liability allocated to a Member pursuant Section 11 of this Rule prior to such time as the Member's Clearing Fund is actually applied to such loss pursuant to this Section or the Member makes payment to the Corporation in the amount of the loss so allocated;

provided, however, that the financing set forth in clauses (A), (B) and (C) shall be at the discretion of the Corporation.

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<sup>7</sup> This subparagraph (B) shall automatically expire, without any further action of the Corporation, on the date on which all Members are Netting Members .

If the Corporation pledges, hypothecates, encumbers, borrows, or applies any part of the Clearing Fund deposits, or other collateral that it has received from Members to satisfy, in whole or in part, any single liability, obligation, or liquidity requirement, for more than 60 days, the Corporation, at the Close of Business on the 74th day (or on the first Business Day thereafter), shall consider the amount used to meet such financing as an actual loss to the Clearing Fund and immediately allocate such loss in accordance with Section 11 of this Rule.

If a loss or liability incurred by the Corporation is allocated to a Member pursuant to Section 11 of this Rule, the Corporation may apply the portion of the Member's deposit to the Clearing Fund necessary to satisfy such allocation. In this regard, the Corporation may apply any cash, draw against any letters of credit, and liquidate any securities deposited by the Member.

Any cash paid to the Corporation pursuant to this Rule may be partially or wholly invested in securities issued or guaranteed as to principal and interest by the United States Government or agencies or instrumentalities of the United States, repurchase agreements relating to the above securities, or otherwise pursuant to the investment policy adopted by the Corporation. To the extent not so invested, such cash funds shall be deposited by the Corporation in its name in a depository institution selected by the Corporation. Any investment income from cash deposits in the Clearing Fund shall accrue to the Corporation, until and unless the Board permits payment of such investment income to Members. Any investment income from cash deposits that is payable to Members pursuant to this Section, less an amount to compensate the Corporation for its handling costs, shall be paid to Members no less frequently than quarterly.

#### SEC. 11. Allocation of Loss or Liability Incurred by the Corporation

(a) Any loss or liability incurred by the Corporation as the result of the failure of a Member to fulfill its obligations to the Corporation shall be satisfied by application of any Clearing Fund deposits (including any other collateral held by the Corporation securing such Member's obligations to the Corporation) in accordance with the procedures set forth in this Section 11.

(b) If the aggregate of such losses do not exceed the defaulting Member's Clearing Fund deposit (including any other collateral held by the Corporation securing such Member's obligations to the Corporation), such losses shall be satisfied by application of any Clearing Fund deposits, and any other collateral held by the Corporation securing such Member's obligations to the Corporation.

(c) If the aggregate of such losses exceed the failing Member's Clearing Fund deposit, and any other collateral held by the Corporation securing such Member's obligations to the Corporation, then such losses shall be allocated as set forth below;

provided, however, the Corporation may determine to apply the existing retained earnings of the Corporation or such lesser part thereof to such loss; provided, further, that in the event the Corporation determines to apply retained earnings, at least 25 percent of the existing retained earnings of the Corporation, or such greater percentage thereof as the Board determines to be appropriate, shall first be applied to the loss.

I. If the defaulting Member was not an Inter Dealer Broker:

(i) The Corporation shall determine, with respect to such aggregate loss, the portion thereof attributable to Direct Transactions and the portion thereof attributable to Inter Dealer Broker Transactions.

(ii) The Clearing Fund deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation shall be applied to losses attributable to Direct and Inter Dealer Broker Transactions in the proportion that (A) the aggregate amount of losses attributable to Direct Transactions and (B) the aggregate amount of losses attributable to Inter Dealer Broker Transactions each bear to the total aggregate loss (such losses shall be collectively referred to hereinafter as the "Total Aggregate Loss"; provided, however, that if there was an Overnight Exposure Cap Violation with respect to such defaulting Member, then the "Total Aggregate Loss" shall only include losses attributable to Old Trades).

(iii) If there was no Overnight Exposure Cap Violation or, if there was insufficient Clearing Fund and other collateral to cover loss attributable to Old Trades then, after the Clearing Fund deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation has been applied to the Total Aggregate Loss pursuant to (ii) above, any remaining loss shall be allocated as set forth in (A) and (B) below.

(A) The portion of such remaining loss attributable to Inter Dealer Broker Transactions shall be allocated pro rata among all Members based upon each Member's average final Daily Margin Amount calculated with respect to the 30 calendar days prior to the date on which the defaulting Member defaulted; and

(B) The portion of such remaining loss attributable to Direct Transactions shall be allocated to the original contra-parties to the Direct Transaction in an amount equal to the product of (A) the aggregate amount of the portion of such remaining loss

attributable to Direct Transactions and (B) a fraction, the numerator of which shall equal the portion of the Total Aggregate Loss attributable to such contra-party's Direct Transactions with the defaulting Member and the denominator of which shall equal the portion of the Total Aggregate Loss attributable to Direct Transactions.

(iv) If there was an Over Night Exposure Cap Violation with respect to such defaulting Member, then after the Clearing Fund Deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation has been applied to losses attributable to Old Trades, any remaining Clearing Fund deposits and other collateral shall be applied to losses attributable to New Trades<sup>8</sup>. Any loss attributable to New Trades<sup>9</sup> remaining after application of the Clearing Fund Deposit and other collateral shall be allocated as follows:

(A) Remaining losses up to an amount less than or equal to the defaulting Member's Overnight Exposure Cap (the "Under the Cap Loss"), shall be allocated:

in the case of the portion of the Under the Cap Loss attributable to Direct Transactions, to each original contra-party to such Direct Transactions to the extent of the amount of the loss attributable to such Direct Transactions; and

in the case of losses attributable to Inter Dealer Broker Transactions, allocated pro rata among all Members based upon each Member's average final Daily Margin Amount calculated with respect to the 30 calendar days prior to the date on which the defaulting Member defaulted.

(B) Losses other than those covered in (A) above, shall be, (X) in the case of loss attributable to Direct Transactions, allocated to each original contra-party to such Direct

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<sup>8</sup> These losses shall be determined EMCC Eligible Instrument-by-EMCC Eligible Instrument and the defaulting Member's Clearing Fund deposit shall be applied to losses from smallest to largest until the aggregate of such losses equals the Member's Overnight Exposure Cap.

<sup>9</sup> Calculations pursuant to this paragraph shall be performed on an EMCC Eligible Instrument-by-EMCC Eligible Instrument basis.

Transactions to the extent of the amount of the loss attributable to such Direct Transaction<sup>10</sup>, and (Y) in the case of losses due to Inter Dealer Broker Transactions, allocated first to each Inter Dealer Broker who was the contra party to such transactions to the extent of the amount of the loss attributable to such Inter Dealer Broker Transactions up to a maximum allocation of \$3 million per Inter Dealer Broker. Losses in excess of \$3 million shall be allocated pro rata among Members who were on the opposite side of the market in the same EMCC Eligible Instrument, with the same settlement date, at approximately the same price in respect of the transactions with Inter Dealer Brokers who would have had allocated losses in excess of \$3 million.

II. If the defaulting Member was an Inter Dealer Broker:

(i) The Clearing Fund deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation shall be applied to all losses (such losses shall be collectively referred to hereinafter as the "Total Aggregate Loss"; provided, however, that if there was an Overnight Exposure Cap Violation with respect to such defaulting Member, then the "Total Aggregate Loss" shall only include losses attributable to Old Trades).

(ii) If there was no Overnight Exposure Cap Violation or, if there was insufficient Clearing Fund and other collateral to cover loss attributable to Old Trades then, after the Clearing Fund deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation has been applied to the Total Aggregate Loss pursuant to (i) above, any remaining loss shall be allocated to the original contra-parties to the transactions giving rise to such loss in an amount equal to the product of (A) the aggregate amount of such remaining loss and (B) a fraction, the numerator of which shall equal the aggregate loss attributable to such contra-party's transactions with the defaulting Member and the denominator of which shall equal the Total Aggregate Loss.

(iii) If there was an Over Night Exposure Cap Violation with respect to such defaulting Member, then after the Clearing Fund Deposit and any other collateral held by the Corporation securing such defaulting Member's obligations to the Corporation has been applied to losses attributable to Old

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<sup>10</sup> Calculations pursuant to this subsection (X) shall be performed on an EMCC Eligible Instrument-by-EMCC Eligible Instrument basis.

Trades, any remaining Clearing Fund Deposit and other collateral shall be applied to losses attributable to New Trades.<sup>11</sup> Any loss attributable to New Trades remaining after application of the Clearing Fund deposit and other collateral shall be allocated to each original contra-party to the transactions giving rise to such loss to the extent of the amount of the loss attributable to such transactions.

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<sup>11</sup> These losses shall be determined EMCC Eligible Instrument-by-EMCC Eligible Instrument and the defaulting Member's Clearing Fund deposit shall be applied to losses from smallest to largest until the aggregate of such losses equals the Member's Overnight Exposure Cap.

**Exhibit B**

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34- ; File No. SR-EMCC-00-3)

Proposed rule change by EMERGING MARKETS CLEARING CORPORATION ("EMCC")

Comments requested within days after the date of this publication.

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Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on , Emerging Markets Clearing Corporation ("EMCC" or the "Corporation") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by EMCC. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The text of the proposed rule change provides Emerging Markets Clearing Corporation ("EMCC") the right, in its discretion, to exclude from an inter dealer broker Member's "Minimum Margin Amount" additional margin that such Member has posted to the clearing fund due to its contra-party's failure to timely submit one or more trades to EMCC, once the underlying trade(s) have been compared or settled. The text of the proposed rule change is set forth on Exhibit A.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change.

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

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change.

(a) EMCC's Rules require that inter-dealer broker Members ("IDBs") be margined in the same way as dealer Members. Rule 4, Section 5(A) of EMCC's Rules requires Members' Clearing Fund deposits to equal the greater of (i) their Daily Margin Amount (i.e., the amount calculated for each Member on each business day) and (ii) their Minimum Margin Amount (i.e., their "Floor"). The Floor is the amount equal to the largest single Daily Margin Amount computed for a Member during the relevant calendar month and the previous calendar month.

As EMCC has developed and expanded its membership base, there have been concerns about the effect of late trade matching on IDBs. That is, where an IDB submits its trades on a timely basis, as do one of its contra-parties, but the other contra-party dealer does not, the IDB will be required to post additional clearing fund with EMCC. EMCC's Addendum B requires the late submitting dealer in that situation to cover the IDB's

financing cost of such excess clearing fund deposit. Addendum B does not, however, address the impact of such additional margin requirement on the computation of the IDB's Floor. The intent of requiring the additional margin from the IDB was only to cover EMCC's risk exposure until the trade was compared or settled. As written, the IDB Member would have to maintain that additional amount on deposit as its Floor for an additional 30 to 60 days. Accordingly, the proposed rule would amend Rule 4 to permit EMCC, in its discretion once the underlying trade(s) have been compared or settled, to exclude the additional margin from the calculation of the IDB's Floor, and thus return the excess clearing fund so posted by the IDB.

(b) This rule change should encourage IDB's to become participants in EMCC, and therefore facilitate the prompt and accurate clearance and settlement of emerging market securities transactions. The proposed rule change is therefore consistent with the requirements of the Securities Exchange Act of 1934, as amended (the "Act"), and the rules and regulations thereunder.

(B) Self-Regulatory Organization's Statement on Burden on Competition.

EMCC does not believe that the proposed rule change will have an impact on or impose a burden on competition.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others.

No written comments relating to the proposed rule change have been solicited or received. EMCC will notify the Commission of any written comments received by EMCC.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission

Action.

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve such rule filing, or
- (B) institute proceedings to determine whether the rule filing should be disapproved.

IV. Solicitation of Comments.

Interested persons are invited to submit written data, views and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the rule filing that are filed with the Commission, and all written communications relating to the rule filing between the Commission and any person, other than those that may be withheld from the public in accordance with provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room in Washington, D.C. Copies of such filing will also be available for inspection and copying at the principal office of the above-mentioned self-regulatory organization. All submissions should refer to the file number in the caption above and should be submitted within days after the date of this publication.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.

Jonathan G. Katz

Secretary

Dated: