

Globalization of trading markets continues at a record pace, as investors seek out higher returns and countries look for new sources of investment capital. It is against this backdrop that the International Securities Clearing Corporation (ISCC), a subsidiary of NSCC, has strived over the past decade to facilitate growth in cross border trading activity and provide leadership in the development of global standards for clearance and settlement.

During 1996, ISCC took several steps that will redefine how it fosters this growth well into the next century.

For the first time since ISCC launched its Global Clearing Network (GCN) in 1993, transaction volume leveled off to just under 400,000 transactions this past year.

While GCN continues to attract interest among overseas firms, some U.S. broker dealers have moved to use their membership in SWIFT systems to establish direct relationships with their custodians.

GCN provides a standardized platform for communicating instructions through a central point and reporting on clearance, settlement and custody. GCN now operates in 45 countries and has 39 participating broker dealers. ISCC has taken steps this past year to enhance GCN for users through the introduction of GCN's new iPC platform. The iPC system will provide real

from left to right
 Joseph C. Willing, Managing Director,
 J.P. Morgan & Co.
 Keith Kanaga, VP, ISCC
 Michael M. Chamberlin,
 Executive Director
 Emerging Markets Traders Association





from left to right
Stuart Feinberg, Director
Participant Services, ISCC
Walter P. Springer, Director
International Operations, ISCC

time interactive and centralized access to a wider array of custodians worldwide and offers firms enhanced reporting capabilities.

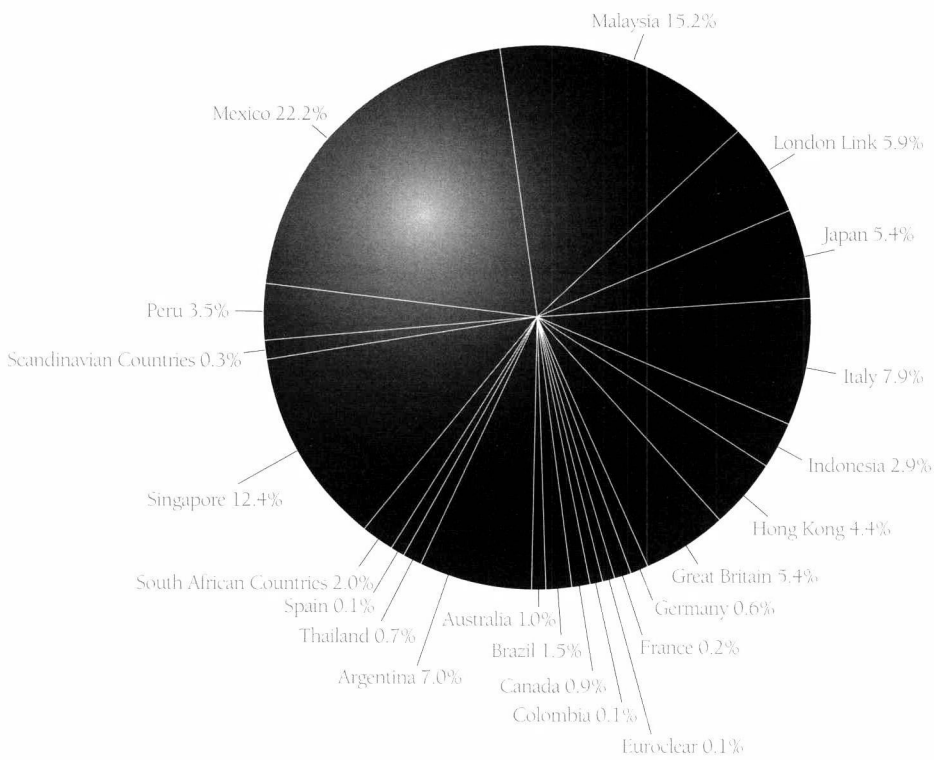
But larger issues loom on the horizon for international clearance, settlement and custody, considering the dynamic changes occurring in global markets. To strengthen its ability to support U.S. and non-U.S. broker dealers, ISCC needed to look toward synergies that might be gained through greater coordination with the nation's largest depository, The Depository Trust Company (DTC).

This need was also recognized by DTC, and by mid-year, NSCC and DTC announced plans to bring together the international activities of these respective organizations under a new banner, the International Depository & Clearing LLC (IDC).

IDC, which has been established as a jointly owned affiliate of NSCC and DTC, will provide a focal point for relationships with Central Securities Depositories (CSDs) worldwide and a singular focus on global issues from a research, marketing and development standpoint. While IDC is still in its formative stages, this new organization has already promoted an active dialogue among U.S. and overseas broker dealers, custodian banks and internationally active institutions on coordinating standards for electronic trade confirmation (ETC) activity.

Guided by its Board, which includes representation from the industry, NSCC and DTC, and working closely with regulators, IDC is positioned to add value in the effort to promote global standards and streamline trading activity.

GCN Volume by Country in 1996



The creation of IDC does not mean that ISCC, as an organization, is going away. ISCC remains a registered clearing agency and it is the regulated structure through which we will offer specific services.

In 1996, ISCC was asked by the Emerging Markets Traders Association, following a joint study, to develop a new clearing corporation for the growing field of emerging markets debt instruments. The new Emerging

Markets Clearing Corporation (EMCC) is expected to help the industry significantly reduce risk and operating costs.

During the year, ISCC worked on establishing EMCC's corporate structure, designing the transaction processing system, risk management controls and procedures and initial staffing. Testing of EMCC's system will begin in the second quarter of 1997.

Initially, EMCC is scheduled to clear U.S. dollar-denominated Brady Bonds. After that is successfully implemented, EMCC may consider other instruments such as non-U.S. dollar Brady Bonds, as well as emerging market Eurobonds, loans and local market instruments and options.

With growing interest by U.S. and

European investors in emerging markets, EMCC is expected to help improve the safety



Left to right
 Yvonne Ettridge, Director IDC
 Terry Gibson, Director IDC
 William Hodash, Managing Director
 IDC Operations

and investing environment for the increasing levels of capital flowing to these new markets.

Board of Directors

NSCC's Board of Directors plays an integral role in policy development and the establishment of corporate objectives, financial management and operational planning at NSCC and ISCC. Through its professional expertise in executive, financial and corporate management, the Board in 1996 continued to provide NSCC with guidance and direction.

The Board of Directors is made up of 20 members: 16 Participant Directors elected from participating brokers, dealers, banks and mutual funds, NSCC's President & Chief Executive Officer, and three Shareholder Directors.

GSCC's separate 15 member Board of Directors represents participants in GSCC, a full-service clearing corporation providing automated comparison, netting and settlement services for next-day and forward-settling transactions in Treasury Bills, Bonds, Notes, zero coupon securities, non-mortgage-backed Agency securities and repurchase agreements. Twelve members of the Board of Directors are participant Shareholder Directors elected to represent dealers, brokers and clearing agent banks. Additional members include two NSCC Designated Directors and the President of GSCC.



from left to right

Thomas F. Ryan, Jr.
President & COO
American Stock Exchange, Inc.

Henry A. Lichstein
Vice President
Advanced Development
Citibank, TTI

Thomas J. Perna
Executive Vice President
The Bank of New York



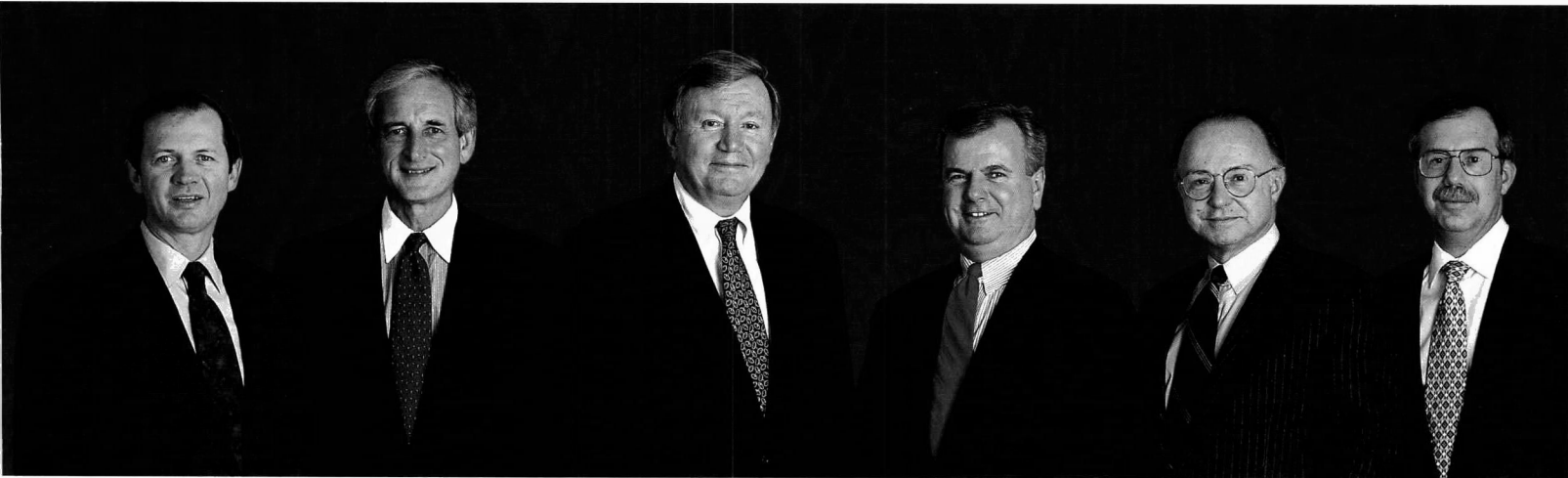
from left to right

Richard A. Edgar
Executive Vice President
New York Stock Exchange, Inc.

John T. Wall
Executive Vice President
National Association of
Securities Dealers, Inc.

George J. Minnig
Managing Director
Pershing Division of
Donaldson, Lufkin &
Jenrette Securities
Corporation

NSCC and ISCC Board of Directors



Arthur L. Thomas
Senior Vice President, Director
of Global Operations Services
Merrill, Lynch, Pierce,
Fenner & Smith Inc.

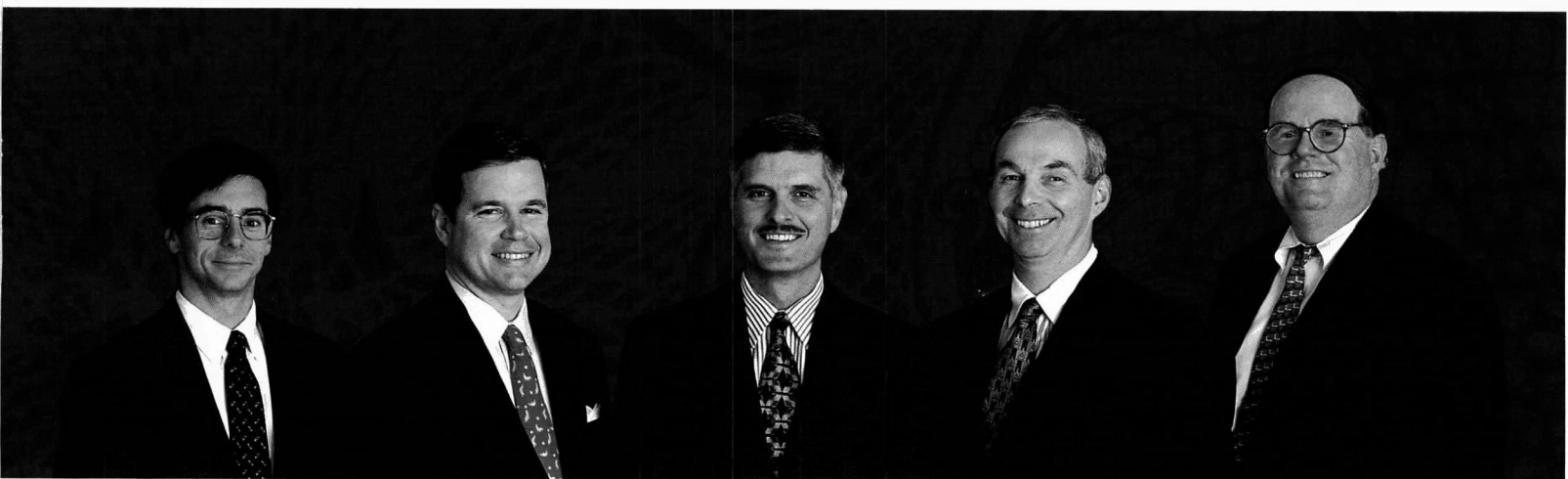
Melvin B. Taub
Chairman of the Board, NSCC
Senior Executive Vice President
Smith Barney, Inc.

David M. Kelly
President & CEO
National Securities
Clearing Corporation
Chairman of the Board, ISCC

Robert E. Lucey
Senior Managing Director
Putnam Investments

John Cirrito
Executive Vice President
Gruntal & Co., Incorporated

Jeffrey C. Bernstein
Senior Managing Director
Bear Stearns Securities Corp.



Gary F. Goldring
Managing Director
Spear, Leeds & Kellogg

Peter Quick
President
Quick & Reilly Inc.

Dennis W. Zank
Executive Vice President
Operations & Administration
Raymond James & Associates, Inc.

Kenneth K. Marshall
Chief Administrative Officer
Salomon Brothers Inc

J. Michael Connelly
Managing Director
Alex Brown & Sons, Inc.

Not pictured

Robert F. Gartland
Managing Director
Morgan Stanley & Co. Incorporated

Vincent M. Purpura
President & COO
D.A. Davidson & Co., Inc.

GSCC Board of Directors



from left to right

Joseph R. LaBato
Managing Director
Chase Bank

Peter J. Murray
Director
Credit Suisse First
Boston Corporation

Edward F. Watts, Jr.
Chairman
Executive Director
Goldman, Sachs & Co.

Sal Ricca
President & Chief
Operating Officer
Government Securities
Clearing Corporation

Daniel O. Minerva
Co-President
Co-Chief Executive Officer
Eastbridge Capital Inc.

James Malgieri
Managing Director
Cantor Fitzgerald Securities

Mark Alexander
First Vice President
Merrill Lynch Government
Securities Inc.



from left to right

Stephen R. Tilton
President
Garban LLC

Edwin Payne
Chairman & CEO
Liberty Brokerage Investment
Corporation

Edward Almeida
Senior Managing Director
Bear Stearns & Co., Inc.

David M. Kelly
President & CEO
National Securities
Clearing Corporation

William Molloy
Managing Director
Morgan Stanley & Co.
Incorporated

Thomas Ford
Senior Vice President
Bank of New York Securities
Lending

Richard M. Kijewski
Vice President
Nesbitt Burns Securities Inc.

Consolidated Balance Sheets

December 31, (in thousands)	1996	1995
Assets		
Cash and cash equivalents	\$439,174	\$477,555
U.S. Treasury securities	59,982	87,522
Accounts receivable	7,394	5,794
Settlement accounts receivable	304	3,592
Clearing fund	449,492	349,397
Fixed assets, less accumulated depreciation and amortization of \$9,014,000 and \$6,998,000 at December 31, 1996 and 1995, respectively	6,907	5,423
Intangible asset, less accumulated amortization of \$2,313,000 at December 31, 1996	9,254	—
Other assets	9,757	8,278
Total assets	\$982,264	\$937,561
Liabilities and Shareholders' Equity		
Liabilities:		
Accounts payable	\$ 3,240	\$ 2,122
Settlement accounts payable	159,980	277,796
Clearing fund:		
Participants' cash deposits	314,811	261,643
Other participant deposits	449,492	349,397
Other liabilities	29,741	21,603
Total liabilities	957,264	912,561
Commitments and contingent liabilities (Note 8)		
Shareholders' equity:		
Common stock authorized, issued and outstanding; 30,000 shares of \$.50 par value	15	15
Capital in excess of par	885	885
Retained earnings	24,100	24,100
Total shareholders' equity	25,000	25,000
Total liabilities and shareholders' equity	\$982,264	\$937,561

The accompanying notes are an integral part of these statements.

Consolidated Statements of Income and Retained Earnings

<i>For the Year Ended December 31,</i> (in thousands)	1996	1995
<i>Revenues:</i>		
Revenue from services	\$177,962	\$152,949
Discounts to participants	<u>65,205</u>	<u>60,016</u>
Net revenue from services	112,757	92,933
Interest income	<u>8,952</u>	<u>8,896</u>
Total revenues	<u>121,709</u>	<u>101,829</u>
<i>Expenses:</i>		
Securities Industry Automation Corporation processing expenses	53,702	47,999
The Depository Trust Company fees	15,932	12,042
General and administrative	44,075	36,658
Provision for estimated liquidation losses (Note 8)	<u>8,000</u>	<u>2,000</u>
Total expenses	<u>121,709</u>	<u>98,699</u>
Income before income taxes	—	3,130
Provision for income taxes	<u>—</u>	<u>1,130</u>
Net income	—	2,000
Retained earnings, beginning of year	<u>24,100</u>	<u>22,100</u>
Retained earnings, end of year	<u>\$ 24,100</u>	<u>\$ 24,100</u>

The accompanying notes are an integral part of these statements.

Consolidated Statements of Cash Flows

For the Year Ended December 31, (in thousands)	1996	1995
Cash flows from operating activities:		
Net income	\$ —	\$ 2,000
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	4,329	1,812
Provision for estimated liquidation losses	8,000	2,000
Changes in operating assets and liabilities:		
Increase in accounts receivable	(1,600)	—
Decrease (increase) in settlement accounts receivable	3,288	(3,185)
Increase in other assets	(1,479)	(4,537)
Increase (decrease) in accounts payable	1,118	(738)
(Decrease) increase in settlement accounts payable	(117,816)	29,164
Increase in clearing fund participants' cash deposits	53,168	44,466
Increase in other liabilities, net	138	10,986
Net cash (used in) provided by operating activities	<u>(50,854)</u>	<u>81,968</u>
Cash flows from investing activities:		
Decrease in U.S. Treasury securities	27,540	12,817
Purchases of fixed assets	(3,500)	(2,683)
Acquisition of intangible asset	(11,567)	—
Net cash provided by investing activities	<u>12,473</u>	<u>10,134</u>
Net (decrease) increase in cash and cash equivalents	(38,381)	92,102
Cash and cash equivalents, beginning of year	<u>477,555</u>	<u>385,453</u>
Cash and cash equivalents, end of year	<u>\$439,174</u>	<u>\$477,555</u>
Supplementary disclosure — Income taxes paid	\$ 2,358	\$ 941

The accompanying notes are an integral part of these statements.

Notes to Consolidated Financial Statements

(1)

Organization and Operations:

National Securities Clearing Corporation (NSCC), a clearing agency registered with the Securities and Exchange Commission (SEC), provides various services to the financial community, consisting principally of securities trade comparison, recording, clearance and settlement. NSCC's common stock is owned equally by the New York Stock Exchange, Inc. (NYSE), American Stock Exchange, Inc. (Amex) and the National Association of Securities Dealers, Inc. (NASD).

NSCC provides discounts on its billing to participants based upon the amount of earnings to be retained in a given year with due regard to current and anticipated needs, as determined by its independent user Board of Directors.

(2)

Summary of Significant Accounting Policies:

Principles of consolidation: The consolidated financial statements include the accounts of NSCC and its wholly-owned subsidiary, International Securities Clearing Corporation (ISCC). Intercompany accounts and transactions are eliminated in consolidation.

NSCC's ownership in Government Securities Clearing Corporation (GSCC) of approximately 17% is included in other assets on the consolidated balance sheet at a carrying value of approximately \$2,548,000 at December 31, 1996. The equity method is used to account for this investment up to a limit which is the stated price at which GSCC may repurchase the shares. NSCC also owns approximately a 10% interest in MBS Clearing Corporation (MBSCC). This investment, which is carried at cost (\$432,000), is also included in other assets.

Cash equivalents: NSCC invests funds in overnight reverse repurchase agreements, which are considered cash equivalents. Such agreements provide for NSCC's delivery of cash in exchange for securities having a

market value which is at least 102% of the amount of the agreement. An independent custodian designated by NSCC takes possession of the securities. Overnight reverse repurchase agreements are recorded at the contract amounts and totaled \$406,000,000 and \$437,000,000 at December 31, 1996 and 1995, respectively. At December 31, 1996, the counterparties to these agreements were seven financial institutions.

Overnight investments in the commercial paper of two major U.S. bank holding companies totaling \$30,029,000 and \$3,298,000 are also included in cash equivalents at December 31, 1996 and 1995, respectively.

U.S. Treasury securities: U.S. Treasury securities are recorded at amortized cost and are considered to be held-to-maturity securities as NSCC has both the positive intent and ability to hold these securities to maturity. The contractual maturities, carrying value and market value of these securities at December 31, 1996 and 1995 are as follows:

	1996		1995	
	Carrying Value	Market Value	Carrying Value	Market Value
Due in one year or less	\$59,483,000	\$59,516,000	\$86,519,000	\$86,636,000
Due in one through three years	499,000	510,000	1,003,000	1,029,000
Total	\$59,982,000	\$60,026,000	\$87,522,000	\$87,665,000

At December 31, 1996 and 1995, \$59,483,000 and \$58,503,000, respectively, of such securities were held in an account for the exclusive benefit of participants to facilitate participants' compliance with customer protection rules of the SEC.

Settlement accounts: Settlement accounts receivable arises from time lags, primarily one-day, in the settlement process with another registered clearing agency. Settlement accounts payable primarily represents deposits received from participants to facilitate participants' compliance with customer protection rules of the SEC.

Fixed assets: These assets consist primarily of computer equipment which is being depreciated over a three or five-year period and purchased computer software which is being amortized over a five-year period.

Intangible asset: Under an agreement with the Chicago Stock Exchange, Incorporated (CHX), entered into on January 6, 1996, NSCC assumed certain open positions in Midwest Clearing Corporation's (MCC) continuous net settlement system of MCC participants who qualified for and were accepted into membership at NSCC. NSCC, in addition, paid \$11,567,000 consisting of \$5,003,000 in cash and the assumption of certain net lease obligations valued at \$6,564,000. In exchange for such, CHX and MCC signed covenants not to compete with NSCC. The total amount paid, which was fully allocated to the covenants, is being amortized over five years, the estimated benefit period.

Income taxes: Deferred tax assets and liabilities are provided for the expected future tax consequences of temporary differences between the carrying amount and tax basis of assets and liabilities. Deferred tax assets relate principally to depreciation and employee benefit costs.

Financial instruments: Management believes that the carrying value of all financial instruments approximates market value.

Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make

estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications: Certain reclassifications of 1995 amounts have been made in the accompanying financial statements to conform to the 1996 presentation.

(3)

Participants' Clearing Fund Deposits:

NSCC's rules require certain participants to maintain minimum clearing fund deposits based on calculated requirements. These requirements are recorded in NSCC's balance sheet. The consolidated clearing fund balance includes NSCC and ISCC clearing funds, which are available to secure participants' obligations and certain liabilities of NSCC and ISCC, should they occur. A summary of the deposits held including deposits in excess of calculated requirements at December 31, 1996 and 1995, follows:

	1996	1995
Cash	\$314,811,000	\$261,643,000
Securities issued or guaranteed by the U.S. Government, at market	241,382,000	217,104,000
Letters of credit issued by authorized banks	263,829,000	295,682,000

During 1996, NSCC had a \$400,000,000 committed line of credit agreement with 3 major U.S. banks to provide for potential additional liquidity needs. This line was not used in 1996.

(4)

Transactions with Related Parties:

SIAC: Under the terms of an agreement, the Securities Industry Automation Corporation (SIAC), an entity owned by NYSE and Amex, provides computer facilities, personnel and services in support of NSCC's operations. SIAC charges NSCC for these services based on its direct and overhead costs arising from providing such services. The agreement has no expiration date and continues in effect unless prior written notice of cancellation is given by either party. Amounts payable to SIAC at December 31, 1996 and 1995, were \$2,847,000 and \$2,453,000, respectively.

DTC: NYSE, Amex and NASD own minority interests in The Depository Trust Company (DTC), whose facilities are used by NSCC. DTC fees in 1996 and 1995 included \$9,253,000 and \$6,623,000, respectively, relating to charges for NSCC participants which NSCC sponsors at DTC. Such amounts are rebilled to the related participants and are included in revenues from clearing services. Amounts payable to DTC at December 31, 1996 and 1995, were \$1,045,000 and \$506,000, respectively.

NYSE, Amex and NASD: NSCC collects certain regulatory fees on behalf of NYSE, Amex and NASD. At December 31, 1996 and 1995, no amounts were due the NYSE, Amex or NASD.

GSCC: NSCC has entered into an agreement with GSCC to provide various computer and other support services and office facilities. Charges under this agreement are based on a determination of NSCC's cost of providing these services. The agreement continues in effect unless cancelled by either party upon prior written notice. Charges under this agreement totaled \$3,982,000 in 1996 and \$3,217,000 in 1995. NSCC's expenses are presented net of these charges. At December 31, 1996 and 1995, receivables from GSCC amounted to \$36,000 and \$148,000, respectively.

MBSCC: During 1995, NSCC entered into an agreement with MBSCC to provide various support services and office facilities. Charges under this agreement, which are based on a determination of NSCC's cost of providing these services, totaled \$567,000 in 1996 and \$354,000 in 1995. NSCC's expenses are presented net of these charges. The agreement expires in 1999; however, it will continue in effect unless notice of cancellation is given by either party. At December 31, 1996 and 1995, receivables from MBSCC amounted to \$149,000 and \$61,000, respectively.

(5)

Income Taxes:

NSCC and ISCC file consolidated Federal, combined New York State and combined New York City income tax returns. The difference between NSCC's 36% effective tax rate for the year ended December 31, 1995 and the 34% Federal statutory tax rate is primarily attributable to state and local taxes.

The provisions for income taxes for the years ended December 31, 1996 and 1995 consist of the following:

	1996	1995
Current income taxes	\$ 15,000	\$ 2,191,000
Deferred income taxes	(15,000)	(1,061,000)
Total income taxes	\$ —	\$ 1,130,000

(6)

Pension Plans:

NSCC has a trustee noncontributory defined benefit pension plan covering all eligible employees of NSCC and certain affiliated companies. Benefits under this plan are based on employees' years of service and compensation during the years immediately preceding retirement. NSCC's funding policy is to make contributions under the plan that meet or exceed the minimum funding standards under the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1986, as amended. NSCC also has a noncontributory supplemental executive retirement plan (SERP) which provides for certain benefits to identified executives of NSCC upon retirement. Although the SERP is currently unfunded, \$4,011,000 (\$4,682,000 for NSCC and affiliated companies) in marketable securities have been segregated in order to pay future benefit obligations of the SERP. The securities are recorded at market value at December 31, 1996 and are included in other assets in the balance sheet. The cost of the securities approximates market value and, as such, no separate valuation component in shareholders' equity was recorded. Finally, NSCC has a noncontributory benefit restoration plan (BRP) which restores to identified executives certain retirement income benefits which have been limited by changes in income tax regulations. The BRP is not funded. Aggregate pension costs for 1996 and 1995 for these plans follow:

	1996	1995
Service cost	\$1,692,722	\$1,058,773
Interest cost	937,376	710,140
Actual return on plan assets	(1,414,116)	(1,753,342)
Net amortization and deferral	893,015	1,286,290
Total pension cost	\$2,108,997	\$1,301,861

The funded status of the plans at December 31, 1996 and 1995, follows:

	1996	1995
Actuarial present value of benefit obligations:		
Vested benefit obligations	(\$7,431,606)	(\$6,463,145)
Nonvested benefit obligations	(1,150,500)	(1,068,138)
Accumulated benefit obligations	(8,582,106)	(7,531,283)
Effect of salary projections	(5,637,584)	(4,997,933)
Projected benefit obligations	(14,219,690)	(12,529,216)
Fair value of plan assets	9,760,479	8,377,025
Plan assets less than projected benefit obligations	(4,459,211)	(4,152,191)
Unrecognized net (gain) loss	(750,223)	952,059
Unrecognized prior service cost	(306,917)	(292,619)
Unrecognized transitional liability	157,803	189,363
Accrued pension cost	(\$5,358,548)	(\$3,303,388)

The expected rate of return on plan assets was 8.0 % in 1996 and 7.5% in 1995. The discount rate and rate of increase in future compensation levels used in determining the actuarial present value of accumulated benefit obligations were 7.75% and 6%, respectively, in 1996 and 7.25% and 6%, respectively, in 1995.

(7)

Other Post-Retirement Benefits:

NSCC's life insurance program includes payment of death benefits to beneficiaries of eligible retired employees of NSCC and certain affiliated companies. Further, NSCC's health insurance program provides benefits to eligible retired employees of NSCC and certain affiliated companies.

The cost of these benefits and the related liabilities as calculated under the provisions of Statement of Financial Accounting Standards No. 106, "Employees Accounting for Post-Retirement Benefits Other Than Pensions," is not material.

(8)

Commitments and Contingent Liabilities:

The Continuous Net Settlement (CNS) system interposes NSCC between participants in securities clearance and settlement. CNS transactions are guaranteed as of midnight on the day they are reported to the membership as compared/recorded. The failure of participants to deliver securities to NSCC on settlement date, and the corresponding failure of NSCC to redeliver the securities, results in open positions. Open positions are marked-to-market daily. Such marks are debited or credited to the involved participants through the settlement process. At the close of business on December 31, 1996, open positions due NSCC approximated \$1,301,275,000 (\$838,510,000 at December 31, 1995), and open positions due by NSCC to participants approximated \$948,474,000 (\$541,125,000 at December 31, 1995) for unsettled positions and \$352,801,000 (\$297,385,000 at December 31, 1995) for securities borrowed through NSCC's Stock Borrow Program.

During the first quarter of 1995, a SIPC trustee was appointed to liquidate the business of Adler Coleman Clearing Corporation (ACCC), a former NSCC participant. NSCC and the SIPC trustee entered into an agreement in connection with the settlement of certain positions held by ACCC at NSCC. NSCC would be liable to the trustee if certain conditions occur for amounts which management estimates could be up to \$17,000,000. At present, management is unable to determine with certainty NSCC's ultimate obligation. In 1996 and 1995, NSCC provided \$8,000,000 and \$2,000,000, respectively, for estimated liquidation losses. At December 31, 1996, the related accrual included in other liabilities is \$8,609,000.

At present, under a netting contract and limited cross guaranty agreement with DTC, DTC transferred to NSCC approximately \$860,000

of excess collateral of Adler Coleman Clearing Corporation. Under the terms of that agreement, NSCC remains liable to DTC for return of such monies for a period of four years from the date of transfer if DTC subsequently determines the collateral not to have been excess.

In connection with an agreement that ISCC has with the London Stock Exchange (LSE), ISCC has guaranteed the settlement obligations of ISCC's members at LSE and correspondingly, NSCC has guaranteed ISCC's obligations to LSE. ISCC's members collateralize such obligations by depositing clearing fund amounts with ISCC as required pursuant to the ISCC Member's Agreement. This agreement is scheduled to end in April 1997.

NSCC is contingently liable for the cancellation of certain SIAC office and equipment leases which expire through December 31, 2003. At December 31, 1996, the aggregate contingent commitment of NSCC totals approximately \$24,898,000.

Net rental expense amounted to \$2,694,000 and \$2,158,000, in 1996 and 1995, respectively. At December 31, 1996, future minimum rental payments under all noncancellable operating leases follows:

Year	Amount
1997	\$ 1,439,000
1998	1,423,000
1999	1,416,000
2000	1,716,000
2001	1,716,000
2002 through 2012	22,180,000
Total minimum annual rental payments	\$29,890,000

(9)

Off-Balance-Sheet Risk and Concentrations of Credit Risk:

In the normal course of business, NSCC guarantees certain obligations of its participants under specified circumstances (see Note 8). If a participant fails to fulfill its obligations, NSCC could be exposed to risk in amounts in excess of that recorded in NSCC's settlement accounts receivable and payable.

NSCC mitigates its exposure to risk by requiring participants to meet NSCC established financial standards for membership, monitoring compliance with other financial standards established by NSCC and by requiring participants to provide clearing fund deposits in the form of cash, marketable securities or acceptable letters of credit (see Note 3).

If a participant fails to fulfill its settlement obligations with NSCC and NSCC ceases to act on behalf of the participant, NSCC would liquidate that participant's guaranteed security receive and deliver obligations and apply the defaulting participant's clearing fund deposit received to satisfy any net outstanding obligation and/or loss.

NSCC has entered into a netting contract and limited cross-guaranty agreement with DTC under which DTC has agreed to make payment to NSCC for any remaining unsatisfied obligations of the defaulting partici-

pant to the extent that DTC has excess resources belonging to the defaulting participant. NSCC has also entered into limited cross-guaranty agreements separately with ISCC, GSCC and MBSCC which provide for payments under similar circumstances.

In the event that a deficiency still exists after the application of the DTC payment and/or payments from other clearing agencies, before NSCC may assess the membership, NSCC is required to apply against the deficiency at least 25% of its retained earnings or such greater amount to be determined by the Board of Directors. NSCC may assess the balance needed on a pro-rata basis to the remaining participants based upon their required clearing fund deposits.

As discussed in Note 1, NSCC provides various services to members of the financial community who participate in securities trade comparison, clearance and settlement. As such, NSCC has a significant group concentration of credit risk since its participants may be impacted by economic conditions affecting the securities industry. As described above, such risk is mitigated in a number of ways.

(10)

Subsequent Event:

On February 3, 1997, NSCC contributed \$1 million for a 50% interest in International Depository & Clearing LLC (IDC), a joint venture with DTC. NSCC's contribution consisted of a cash payment and fixed

assets. The purpose of IDC is to provide a focus for the international activities of NSCC, ISCC and DTC.

Report of Independent Accountants

Price Waterhouse LLP 

February 14, 1997

To the Board of Directors and Shareholders of
National Securities Clearing Corporation

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and retained earnings and of cash flows present fairly, in all material respects, the financial position of National Securities Clearing Corporation and its subsidiary at December 31, 1996 and 1995, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Price Waterhouse LLP

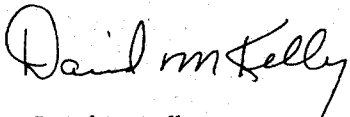
Management's Report on Responsibility for Internal Control Over Financial Reporting

February 14, 1997

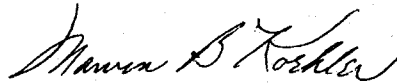
To the Board of Directors and Shareholders of
National Securities Clearing Corporation

National Securities Clearing Corporation (NSCC) maintains a system of internal control over financial reporting which is designed to provide reasonable assurance regarding the preparation of reliable published financial statements. The system contains self-monitoring mechanisms, and actions are taken to correct deficiencies as they are identified. Even an effective internal control system, no matter how well designed, has inherent limitations — including the possibility of the circumvention or overriding of controls — and therefore can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, internal control system effectiveness may vary over time.

NSCC's management assessed its internal control over financial reporting as of December 31, 1996, in relation to criteria for effective internal control described in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, NSCC believes that, as of December 31, 1996, its system of internal control over financial reporting met those criteria.



David M. Kelly
President and Chief Executive Officer



Marvin B. Koehler
Managing Director and Treasurer

Report of Independent Accountants on
Internal Control Over Financial Reporting

Price Waterhouse LLP 

February 14, 1997

To the Board of Directors and Shareholders of
National Securities Clearing Corporation

We have examined management's assertion that National Securities Clearing Corporation (NSCC) maintained effective internal control over financial reporting as of December 31, 1996 which is included in the accompanying Management's Report on Responsibility for Internal Control Over Financial Reporting.

Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included obtaining an understanding of the internal control over financial reporting, testing, and evaluating the design and operating effectiveness of the internal control, and such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control, errors or irregularities may occur and not be detected. Also, projections of any evaluation of the internal control over financial reporting to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assertion that NSCC maintained effective internal control over financial reporting as of December 31, 1996 is fairly stated, in all material respects, based upon criteria established in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Price Waterhouse LLP

NSCC Launched a Web Site - to provide information to its participants and the public. The site includes information on:

- New initiatives, services and speeches
- Newsletters, press releases, important notices
- Fact sheets on NSCC and ISCC products and services
- How clearance and settlement works
- On-line access to request marketing material
- Links to MBSCC, GSCC and ISCC

Come visit us at www.nscc.com!

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Marketing, Corporate Communications, New York Window
left to right

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Managing Director,
New York Window

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Mutual Funds
Product Development

Steve M. Labriola
Managing Director,
Marketing and
Corporate Communications

Walter F. Siebecker
Managing Director,
Annuities



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left to right

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Managing Director,
Systems

Sandy Manata
Managing Director,
Systems

Dwight Arthur
Managing Director,
Systems



International Securities Clearing Corporation (ISCC)
left to right

Brian G. Bollinger
Managing Director,
Marketing

Richard W. Myers
Managing Director and
Chief Operating Officer

Mary Ann Callahan
Managing Director,
Product Development

Stuart M. Kleinman
Managing Director,
Operations

Mark Handsmann
EVP,
International Depository
Clearing LLC

Dennis Earle
Managing Director,
Resource Company



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and Risk Management

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General Counsel and
Secretary

Karen L. Saperstein
Managing Director,
Legal and Deputy
General Counsel



Executive, Finance, Operations, Human Resources
left to right

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Managing Director,
Human Resources

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Marvin B. Koehler
Managing Director,
Finance, Treasurer

Robert A. Schultz
Managing Director,
Operations



MBS Clearing Corporation (MBSCC)
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Vice President/Director,
Marketing and Sales

Lynn Douglas
Managing Director and
Chief Operating Officer

Ronald A. Stewart
President and
Chief Executive Officer

Virginia Hanson
Vice President/Director,
Information Technology



Government Securities Clearing Corporation (GSCC)

left to right

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Managing Director,
Technology

Jeffrey F. Ingber
Managing Director,
General Counsel
& Secretary

Steven M. Jukofsky
Managing Director,
Marketing

Sal Ricca
President and
Chief Operating Officer

Thomas F. Costa
Managing Director,
Marketing, Planning,
Operations and Technology

Joseph J. Grima
Managing Director,
Operations

NSCC, ISCC, GSCC, MBSCC Officers

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Theresa Wright
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GSCC

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Planning, Operations and Technology*

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General Counsel and Secretary*

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Vice President, Technology

Kate Connelly
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Vice President, Participant Services

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Robert S. Bennett
Assistant Treasurer

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President and CEO

Lynn Douglas
Managing Director and COO

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*Vice President/Director,
Information Technology*

Dennis J. Paganucci
Vice President/Director, Marketing and Sales

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President and CEO, ISCC*

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*Managing Director and COO, ISCC
President and CEO, IDC*

Mark Handsman
Executive Vice President, IDC

Brian G. Bollinger
Managing Director, Marketing, ISCC

Mary Ann Callahan
*Managing Director,
Product Development, ISCC*

Dennis Earle
Managing Director, Resource Company

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Chief Financial Officer and Treasurer

Stuart M. Kleinman
Managing Director, Operations

Karen L. Saperstein
General Counsel & Secretary

Sean Delap
Vice President, Marketing

Macrina DiGregorio
Vice President, Planning and Development

Keith Kanaga
Vice President, Product Development & EMCC

Robert S. Bennett
Assistant Treasurer

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National Securities Clearing Corporation