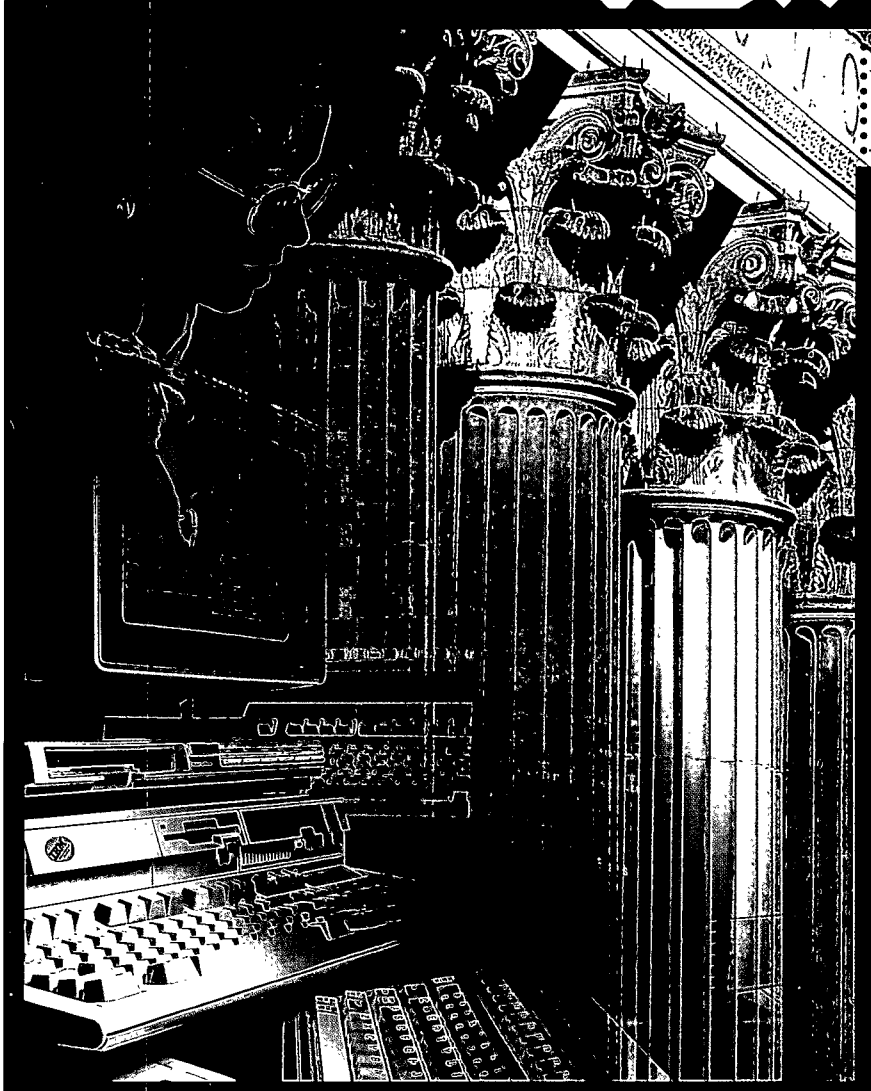




GOVERNMENT SECURITIES CLEARING CORPORATION

1995 Annual Report



*Dedicated to providing stability, leadership and
innovative solutions*

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Government Securities Clearing Corporation



(GSCC) is a not-for-profit organization whose mis-

sion is to clear and settle a broad range of U.S. Government securities — Treasury bills, bonds, notes, zero coupon securities, non-mortgage-backed Agency securities — and repurchase agreements, a service added in

1995. GSCC was established in September 1986 by the National Securities Clearing Corporation and is an

affiliate of NSCC. GSCC is a clearing agency registered with and



regulated by the Securities

and Exchange Commission.



To the more than 90 member firms and 300 correspondent firms that clear through these mem-

bers, GSCC offers highly sophisticated, fail-safe automated trade comparison, netting and settle-

ment processing systems that guarantee that trades will be settled quickly, accurately and cost-effectively.

Underlying these systems is a risk management policy that is routinely examined to ensure that the maximum

amount of risk is extracted from the process of clearing Government securities.

GSCC is governed by a Board of Directors that reflects the organization's membership; it includes repre-

sentatives from the growing consortium of



dealers, brokers and clearing agent banks that trade in

or clear U.S. Government securities.

Government Securities Clearing Corporation supports the world's largest and most liquid financial trading marketplace. During 1995, GSCC processed a record number of Government securities transactions valued at more than \$83 trillion, up 21 percent over the prior year. The average daily volume of transactions processed was up 7 percent.

In addition to this sharp increase in volume, GSCC has expanded its participant base and introduced new technology to enhance the way we serve our members and to create new services to meet their changing requirements.

In the dynamic financial marketplace of Government securities, our goal has been to work closely with our more than 90 broker, dealer and bank members to understand industry trends and deliver cost-effective clearance and settlement services to facilitate continued growth.

Adding Repurchase Agreements to the Mix

In 1985, the average weekly value of repo activity was \$321 billion; ten years later it had risen to more than \$1.4 trillion. Prompted by this dramatic growth, GSCC began a program to extend our comparison, clearance and settlement systems to include the post-trade processing of repurchase agreements. In May, we implemented the comparison system, and by November we had introduced a centralized, automated netting and guaranteed-settlement service for the close legs of overnight and term repos. Our goal for 1996 is to work toward adding the



DAVID M. KELLY

JOHN G. MACFARLANE III

intraday settlement of repo start legs. Along with greater operational efficiencies and risk-management benefits, participants using these repo services have the ability to net repos for financial reporting purposes. This project was conducted under the oversight of the Repo Implementation Committee, which was formed by the board of directors and is composed of board members, dealer-traders, brokers and operations experts.

Managing Risk a Continuing Activity

The cornerstone of GSCC's service is the ongoing process of understanding and managing risk. By maintaining high standards for current and future participants and by closely monitoring our risk measures, we strive to maintain risk at appropriate levels in an ever-changing environment. Last year, after a review of these mechanisms, GSCC made significant revisions to both forward margin and Clearing Fund procedures in order to adequately address the integration of cash and repo market activities. Forward margin was modified to include the effect of fluctuations in repo interest rates and the cost of financing them from current date to close-leg settlement date. In addition, forward margin now collects and pays through margin payments on a cash basis, thus lessening the impact of margins and ensuring the economic integrity of repo trades. Further, we introduced a repo volatility factor to the Clearing Fund calculation, which estimates changes in market rates over the course of the repo and protects GSCC from exposure on rates.

Changes in Fee Structure

In May 1995, GSCC's board of directors approved an 11 percent reduction in clearance fees, and established a discount policy for Comparison and Netting services that has reduced members' costs by 10 percent. These changes were the result of GSCC having completed the amortization of startup and initial product development expenses, as well as member expansion, transaction growth and greater processing efficiencies.

Contingency Site Fully Operational

During 1995, GSCC opened a dual contingency facility for staff at the Securities Industry Automation Corporation's Metro-Tech headquarters in Brooklyn. This site, together with our data center backup facility, will help ensure the continuity of clearance and settlement of Government securities in the event of a business interruption.

Planning for the Future

As the financial services industry expands its global reach and products, the market will witness more emphasis on product development, collaborative arrangements among clearing agencies, competition across national borders, and cost containment. GSCC's primary focus will remain on the fundamental issues of safety and soundness and on being responsive to our members' processing needs. To that end, GSCC began the process of moving from a batch environment to one that is real-time and on-line. Enhancements will be adopted within time frames established jointly by GSCC and our participants to ensure the compatibility of communications systems on both sides.

GSCC will continue to broaden membership and the reach of our clearance and settlement systems in accordance with market needs. We will use as a benchmark Vision 2000, a report that offers a highly perceptive framework for future

planning and that calls for the securities clearing industry to adopt a unified strategy to improve efficiencies, control costs and foster the use of advanced technology.

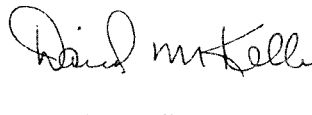
Management Change

Charles A. Moran stepped down as president at the end of 1995. Over the last ten years, he played a key role in developing GSCC into an increasingly important and sophisticated provider of services necessary to the orderly operation of the Government securities industry. Sal Ricca, former managing director of North American Operations for Deutsche Bank A.G., has succeeded him. Mr. Ricca brings to the position considerable experience, strong leadership skills and a deep commitment to the securities industry.

We are fortunate to have a supportive and dedicated board of directors and a highly proficient team of staff professionals. With their continued vision, we are confident that we will achieve our long-range plans and grow our excellent record of service to this important financial market.



John G. Macfarlane III
Chairman of the Board
Government Securities Clearing Corporation

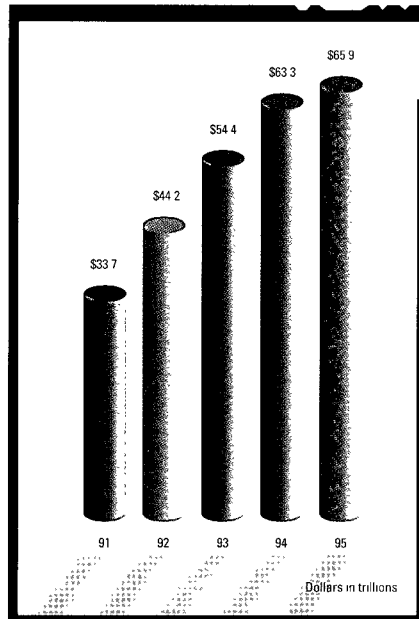


David M. Kelly
Vice Chairman
Government Securities Clearing Corporation

Each year new ground is being broken in the Government securities industry, as volume records transcend those of the year before. And each year GSCC meets the challenges of the market head on by balancing and enhancing the three fundamentals of our business: reduction of risk, development of more flexible systems and services, and growth in efficiency. Our mandate is to anticipate change, to respond to the needs of the industry, and to provide solutions that are creative, efficient and reliable.

Outperforming the Previous Year

In 1995, GSCC's revenues rose 8 percent. The average daily value of U.S. Government securities trades compared increased 21 percent to \$334 billion, up from \$276 billion in 1994; average daily transaction volume was 33,034, or 7 percent over 1994. From year-end 1994 to year-end 1995, GSCC recorded a 4 percent increase in the dollar value of transactions netted and settled, for a total of \$65.9 trillion. Our netting system eliminated \$49.6 trillion from settlement, representing an increase of 2.4 percent over the prior year. This pattern of strong growth continued during the first quarter of 1996.



VALUE OF TRANSACTIONS
NETTED AND SETTLED

What GSCC's Core Services Offer Members

GSCC provides the Government securities industry with comparison and netting services for next-day and forward-settling cash trades, repurchase agreement comparison and netting, treasury auction takedown processing, yield-to-price conversion, and executing firm processing.

The initial process is Trade Comparison. GSCC receives, confirms and matches specific information on the buy and sell sides of a securities transaction. If all data matches, the trade becomes a binding contract between the two parties and is ready to enter the second process: Netting and Settlement.

GSCC's Netting and Settlement system combines all daily buy/sell, repo and Treasury auction purchase transactions — by individual security — to provide a single net settlement position per firm. Once GSCC informs participants of those securities or funds that they are required to deliver or accept, we assume the position of contra party between the long and short sides, and guarantee that the trade will be completed. By marking-to-market, cutting down overdraft exposure and reducing the overall number of securities' movements, this unified procedure of Netting and Settlement offers members greater cost efficiency and reduced risk. On an average day, our Netting Service reduces the number of obligations by more than 83 percent.

Repo Activities Now Linked to GSCC

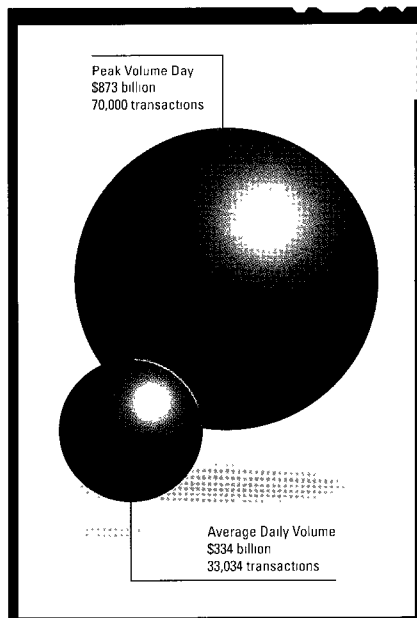
Responding to the burgeoning market in repurchase agreements, GSCC launched a phased-in extension of our processing capabilities to include these transactions. Reaching this point required a thorough understanding of the industry's requirements, as well as the development and roll-out of internal systems to handle these complex instru-

ments, an activity that will carry us through 1996 and beyond.

Phase One of the project was a comparison pilot program in February for the close legs of overnight and fixed-term repos. The test was successful: repo comparison features functioned efficiently, and ample data was obtained to fine-tune the Repo Netting Service, introduced later in the year. In May, participants began to submit for automated comparison repos executed with other participants, along with their regular buy/sell activity. Since then, our comparison rate has been consistently above 93 percent.

Implementation took another step forward in November when GSCC launched Netting Services for repos. With GSCC guaranteeing settlement for all transactions that are netted, participants can take maximum advantage of FASB Interpretation No. 41, which permits the offsetting of repos and reverse repos for financial reporting purposes. Additionally, participants can track coupon payments, lower their Fedwire movements and, therefore, their transfer costs, and decrease exposure to daylight overdraft charges.

As GSCC works toward completing the second phase of this project, we will have the systems in place to include



A PEAK VOLUME DAY COMPARED
WITH DAILY AVERAGE
OF TRADES ENTERING THE NET

principal brokered repos, with GSCC accepting information, on both sides of a trade, from one broker on a locked-in basis. In the foreseeable future, we expect to be offering enhanced services for forward-starting repos, comparison and netting for open repos, and automated collateral substitution. This last feature will give participants the option of substituting new collateral for comparable collateral before settlement date on both an overnight and same-day basis.

The Business of Managing Risk

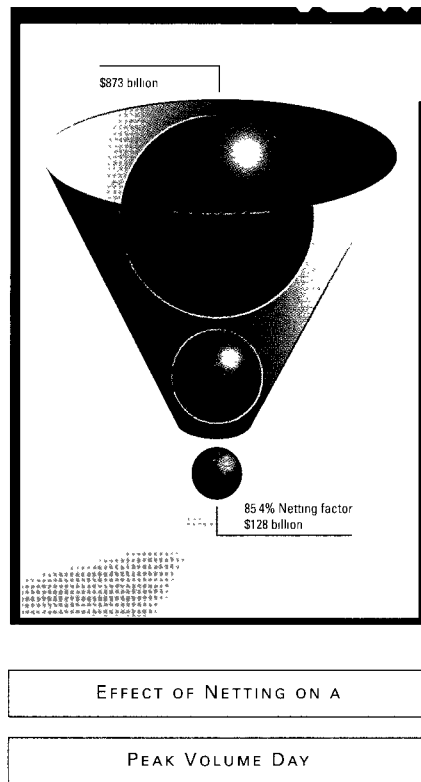
In managing risk, GSCC performs a two-tiered role. On one level, our Netting System reduces the movement of securities and the payment of obligations. On another level, we are vigilant that our admissions standards and margin and collateral requirements remain high enough to maintain both our guarantee of settlement and our liquidity. GSCC's Clearing Fund averages \$700 million in collateral, a figure that is calculated against the ebbs and flows of market activity. Our forward margin procedure revalues forward-settling cash trades and term repos by marking them daily from contract value to market value. And our multi-stage Loss Allocation Procedure ensures that a systemic failure of the settlement process will never occur. In addition, the Chicago Board of Trade Clearing Corporation and GSCC entered into discussions to establish an arrangement that would enable common and affiliated members of both organizations to benefit from cross-margined cash and futures positions. For members, one obvious advantage to such an arrangement is less stringent collateral requirements, while the clearing corporations stand to benefit from heightened risk management, as well as greater access to collateral in the event of a liquidation.

As membership grows, we will continue to provide the highest level of risk protection by monitoring our members' trading activities and compliance with GSCC regulations, as well as maintaining firm control over the processes and systems that drive the clearance of Government securities.

Interactive Technology Opening Doors to Greater Flexibility

Timely processing reduces risk. Accordingly, in 1995, we began to construct a real-time, on-line interactive connection to participants and clearing banks. Communications are now being redesigned, applications restructured, and new information links created to support this project. Through the use of new message switching software, members will be able to send data and track the status of trades as they occur via a CPU-to-CPU connection, and monitor their settlement status with GSCC at any given moment. On-line links with our clearing banks will also allow GSCC to more fully automate its settlement procedures and monitor intraday exposure caused by the timing of settlements over the FedWire.

GSCC's development and planning areas are also in the process of creating



for participants an information page on the Internet for the exchange of trade data and important notifications. As use of this multimedia information delivery source becomes more widespread throughout the industry, GSCC will be ready with the technology required to more fully automate its settlement procedures.

Broadening GSCC's Membership

In 1995, we expanded the range of market participants by extending netting membership to futures commission merchants (FCMs), which are regulated by the Commodities Futures Trading Commission. And, in a later development, the SEC, in response to a filing by

GSCC, ruled that foreign entities can now apply for GSCC membership. These activities clearly reflect our intent to offer GSCC's services to a wider range of financial organizations, both here and abroad.

From Strategy to Action

By virtue of its size, the Government securities arena has a powerful effect on the U.S. economy and, to a growing extent, on the global economy, as more and more international money is channeled into the market.

Since GSCC's incorporation ten years ago, it has been our strategic objective to focus on the major issues facing this growing industry. We have been able to maintain an aggressive stance by studying the marketplace, by judiciously managing the development, introduction and delivery of each new service, and by adding professionals whose combined pool of talents have been honed both within and outside the financial services industries. By following this formula, GSCC has evolved into the primary and trusted source for the consistent and accurate resolution of U.S. Government securities trades.



from left to right

*Edward F. Watts, Jr.
Director, Goldman, Sachs & Co.*

*John M. Gavin, Jr.
Chief Financial Officer, EXCO RMJ Securities Corp.*

*Jeremiah F. O'Leary
Senior Vice President, Chemical Bank*

*David M. Kelly
Vice Chairman, GSCC
President & CEO,
National Securities Clearing Corporation*

*Richard M. Kijewski
Vice President, Nesbitt Burns Securities Inc.*

*Stephen R. Tilton
President, Garban LLC*

*Daniel Minerva
Co-President & Co-CEO, Eastbridge Capital Inc.*



from left to right

*Peter J. Murray
Director, CS First Boston Corporation*

*Thomas M. Wendel
Chairman, Liberty Brokerage Inc.*

*John G. Macfarlane
Chairman of the Board, GSCC
Managing Director, Salomon Brothers Inc*

*Charles A. Moran
President, GSCC*

*William Molloy
Managing Director, Morgan Stanley & Co.
Incorporated*

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

*Kurt D. Woetzel
Senior Vice President, The Bank of New York*

BALANCE SHEETS

December 31	1995	1994
<i>(in thousands)</i>		
Assets		
Cash and cash equivalents	\$ 63,109	\$ 90,382
Investments in marketable securities	13,981	12,389
Accounts receivable	1,118	1,154
Clearing fund	553,023	420,833
Fixed assets, net of accumulated amortization and depreciation of \$6,408,000 and \$5,608,000 at December 31, 1995 and 1994, respectively	1,378	1,367
Other assets	959	1,088
Total assets	\$633,568	\$527,213
Liabilities and Shareholders' Equity		
Liabilities		
Cash margin deposits	\$ 10,724	\$ 45,922
Clearing fund		
Participants' cash deposits	53,140	47,498
Other participant deposits	553,023	420,833
Other liabilities	2,094	1,941
Total liabilities	618,981	516,194
Commitments and contingent liabilities (Note 7)		
Shareholders' equity		
Common stock		
Class A, \$0.50 par value: 75,000 shares authorized, 20,100 shares issued and outstanding at December 31, 1995, and 19,800 shares issued and outstanding at December 31, 1994	10	10
Class B, \$0.50 par value: 30,000 shares authorized, 7,400 shares issued and outstanding at December 31, 1995 and 1994	4	4
Capital in excess of par	12,336	12,186
Retained earnings (accumulated deficit)	2,237	(1,181)
Total shareholders' equity	14,587	11,019
Total liabilities and shareholders' equity	\$633,568	\$527,213

The accompanying notes are an integral part of these statements.

STATEMENTS OF INCOME AND RETAINED EARNINGS (ACCUMULATED DEFICIT)
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For the Year Ended December 31	1995	1994
	(in thousands)	
Revenues		
Revenue from comparison, netting, settlement and related services	\$14,611	\$14,082
Discounts to participants	710	—
Net revenue from services	13,901	14,082
Interest income	3,638	2,124
Total revenues	17,539	16,206
Expenses		
Computer equipment rental, licenses, depreciation, amortization, processing and maintenance costs	6,333	6,579
Employee compensation and related benefits	4,060	3,003
General and administrative expenses	1,245	2,524
Occupancy costs	230	361
Professional fees	185	178
Total expenses	12,053	12,645
Income before income taxes	5,486	3,561
Provision for income taxes	2,068	1,383
Net income	3,418	2,178
Accumulated deficit, beginning of year	(1,181)	(3,359)
Retained earnings (accumulated deficit), end of year	\$ 2,237	\$ (1,181)

The accompanying notes are an integral part of these statements.

STATEMENTS OF CASH FLOWS

For the Year Ended December 31	1995	1994
<i>(in thousands)</i>		
Cash flows from operating activities		
Net income	\$ 3,418	\$ 2,178
Adjustments to reconcile net income to net cash (used in) provided by operating activities		
Amortization and depreciation of fixed assets	800	897
Accretion of discount on securities owned, net of premium amortized	(160)	(124)
Changes in operating assets and liabilities		
Decrease (increase) in accounts receivable	36	(400)
Decrease in other assets	129	998
(Decrease) increase in cash margin deposits	(35,198)	44,479
Increase in participants' cash deposits	5,642	9,765
Increase (decrease) in other liabilities	153	(352)
Net cash (used in) provided by operating activities	(25,180)	57,441
Cash flows from investing activities		
Increase in receivable from NSCC – funds invested on behalf of GSCC	—	2,953
Maturity of investments in marketable securities	5,500	8,500
Purchases of investments in marketable securities	(6,932)	(11,773)
Purchases of fixed assets	(811)	(676)
Net cash used in investing activities	(2,243)	(996)
Cash flows from financing activity		
Proceeds from issuance of Class A common stock	150	—
Net (decrease) increase in cash and cash equivalents	(27,273)	56,445
Cash and cash equivalents, beginning of year	90,382	33,937
Cash and cash equivalents, end of year	\$63,109	\$90,382
Supplementary disclosures		
Interest paid	\$ 2	\$ 9
Income taxes paid	\$ 1,906	\$ 320

The accompanying notes are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

December 31, 1995

NOTE 1 ORGANIZATION AND

OPERATIONS

Government Securities Clearing Corporation (GSCC), a clearing agency registered with the Securities and Exchange Commission, provides automated trade comparison, netting and settlement services for U.S. Government securities to brokers, dealers, banks and other market participants.

NOTE 2 SUMMARY OF SIGNIFICANT

ACCOUNTING POLICIES

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

having a market value of at least 102% of the amount of the agreement. An independent custodian designated by GSCC takes possession of the securities. Overnight reverse repurchase agreements are recorded at the contract amounts and totaled \$62,988,000 and \$90,238,000 at December 31, 1995 and 1994, respectively. At December 31, 1995, two financial institutions were counterparties to these agreements.

Investments in marketable securities: These investments, which include U.S. Treasury securities and investment grade corporate notes, are considered to be held-to-maturity securities under Statement of Financial Accounting Standard (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities," and are recorded at amortized cost. The contractual maturities, carrying value and market value of these securities at December 31, 1995 and 1994, are as follows:

	Carrying Value (in thousands)			Market Value (in thousands)		
	U.S. Treasury Securities	Corporate Notes	Total	U.S. Treasury Securities	Corporate Notes	Total
1995						
Due in one year or less	\$ 6,987	\$ —	\$ 6,987	\$ 7,001	\$ —	\$ 7,001
Due in one to two years	5,994	1,000	6,994	6,068	1,018	7,086
Total	\$12,981	\$1,000	\$13,981	\$13,069	\$1,018	\$14,087
1994						
Due in one year or less	\$ 4,931	\$ 500	\$ 5,431	\$ 4,884	\$ 492	\$ 5,376
Due in one through three years	5,958	1,000	6,958	5,802	973	6,775
Total	\$10,889	\$1,500	\$12,389	\$10,686	\$1,465	\$12,151

Participant clearing fund deposits: GSCC accepts cash, U.S. Treasury securities, and letters of credit issued by authorized banks as clearing fund deposits, and records total deposits on its balance sheet.

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.

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

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 1994 amounts have been made in the accompanying financial statements to conform to the 1995 presentation.

NOTE 3 PARTICIPANT CLEARING

FUND DEPOSITS

GSCC's rules require certain participants to maintain minimum clearing fund deposits based upon calculated requirements which, at December 31, 1995 and 1994, were \$402,790,000 and \$232,101,000, respectively. All participant deposits made to the clearing fund are available to secure participant obligations and, in certain circumstances, to satisfy other losses and liabilities of GSCC, should they occur.

A summary of clearing fund deposits held at December 31, 1995 and 1994, follows:

	1995	1994
Cash	\$ 53,140,000	\$ 47,498,000
U.S. Treasury securities, at market	450,430,000	342,423,000
Letters of credit issued by authorized banks	102,593,000	78,410,000
Total deposits	\$606,163,000	\$468,331,000

NOTE 4 TRANSACTIONS WITH

RELATED PARTIES

National Securities Clearing Corporation (NSCC), a minority shareholder of GSCC, provides various computer and other support services and office facilities to GSCC. The costs of providing these services are charged to GSCC in accordance with the provisions of a service agreement. The agreement continues in effect unless cancelled by either party upon prior written notice. Charges to GSCC pursuant to this agreement during 1995 and 1994 amounted to approximately \$3,217,000 and \$4,832,000, respectively. Amounts payable to NSCC at December 31, 1995 and 1994, were \$148,000 and \$239,000, respectively.

NOTE 5 INCOME TAXES

GSCC files Federal, New York State and New York City income tax returns. The differences between the 34% Federal statutory rate and GSCC's 38% and 39% effective tax rates for the years ended December 31, 1995 and 1994, respectively, are primarily attributed to state and local taxes.

The provision for income taxes for the years ended December 31, 1995 and 1994, consists of the following:

	1995	1994
Current income taxes	\$1,603,000	\$200,000
Deferred income taxes	465,000	1,183,000
Total income taxes	\$2,068,000	\$1,383,000

NOTE 6 POST-RETIREMENT

BENEFIT PLANS

All eligible employees of GSCC participate in NSCC's trustee, noncontributory defined benefit pension plan. In addition, GSCC also participates in NSCC's noncontributory supplemental executive retirement and benefit restoration plans which provide for certain benefits to identified executives of GSCC upon retirement. Further, GSCC also participates in NSCC's life insurance program which provides payment of death benefits to beneficiaries of the retired employees. In 1995, costs for these plans aggregated \$223,000 and were determined based upon an actuarial calculation using information related to all eligible GSCC employees. Disclosure of post-retirement benefit obligations, expense components and actuarial assumptions for the NSCC plans are included in NSCC's 1995 financial statements.

NOTE 7 COMMITMENTS AND

CONTINGENT LIABILITIES

GSCC's netting system interposes GSCC between netting participants for eligible trades that have been guaranteed. The guarantee of net settlement positions by GSCC results in potential liability to GSCC. Guaranteed positions that have not yet settled are margined and marked-to-market daily. Margin deposits are held by GSCC; marks are debited from and cred-

ited to the responsible participants through the funds-only settlement process. At December 31, 1995, the gross amount of guaranteed positions due from certain participants to GSCC approximated \$7,564,004,000; there is an equal amount due from GSCC to certain other participants.

GSCC is contingently liable, under a service agreement, for a portion of NSCC's office lease, which expires on December 31, 2012. At December 31, 1995, the contingent commitment of GSCC totaled approximately \$3,400,000.

NOTE 8 OFF-BALANCE-SHEET

RISK AND CONCENTRATIONS OF

CREDIT RISK

In the normal course of business, because it guarantees certain settlement obligations of its netting participants (see Note 7), GSCC could be exposed to credit risk. GSCC mitigates its exposure to credit risk by requiring such participants to meet GSCC-established minimum financial standards for membership, monitoring compliance with financial and other standards, requiring participants to meet daily mark-to-market obligations, and requiring participants to provide clearing fund (see Note 3) and other margin deposits in the form of cash, U.S. Treasury securities and eligible letters of credit.

If a participant fails to fulfill its settlement obligations to GSCC, and GSCC determines that such participant is insolvent, GSCC would liquidate that participant's netted security positions and apply the failed participant's margin and mark deposits, including clearing fund deposits, to satisfy any outstanding obligation and/or loss. In the event that a deficiency still exists, GSCC would satisfy the deficiency by assessing the participants with whom the defaulting participant most recently conducted trading activity. If one or more of such participants does not pay its assessment, GSCC would satisfy such deficiency by utilizing 25% of its retained earnings, or such greater amount of retained earnings to be determined by the Board of Directors. Thereafter, if necessary, each remaining participant would be assessed on an equal basis up to \$50,000. Finally, if a deficiency still remains, GSCC would assess all remaining participants on a pro-rata basis based upon their average daily level of required clearing fund deposits over the prior year; however, any such remaining participant may limit its liability to the amount of its required clearing fund deposit by terminating its membership in GSCC.

As discussed in Note 1, GSCC provides automated trade comparison, netting and settlement services for U.S. Government securities to brokers, dealers, banks and other market participants. As such, GSCC 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.

Price Waterhouse LLP



February 16, 1996

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

In our opinion, the accompanying balance sheets and the related statements of income and retained earnings (accumulated deficit) and of cash flows present fairly, in all material respects, the financial position of Government Securities Clearing Corporation at December 31, 1995 and 1994, and the results of its operations and its 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.

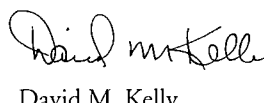
Price Waterhouse LLP

February 16, 1996

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

Government Securities Clearing Corporation (GSCC) 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.

GSCC's management assessed its internal control over financial reporting as of December 31, 1995, 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, GSCC believes that, as of December 31, 1995, its system of internal control over financial reporting met those criteria.



David M. Kelly
Vice Chairman & Chief Executive Officer



Marvin B. Koehler
Treasurer

REPORT OF INDEPENDENT ACCOUNTANTS ON

INTERNAL CONTROL OVER FINANCIAL REPORTING

Price Waterhouse LLP



February 16, 1996

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

We have examined management's assertion that, as of December 31, 1995, Government Securities Clearing Corporation's (GSCC's) internal control over financial reporting met the criteria for effective internal control described in "Internal Control-Integrated Framework." Management's assertion is included in the accompanying Management's Report on Responsibility For 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 structure over financial reporting, testing and evaluating the design and operating effectiveness of the internal control structure, and such other procedures as we con-

sidered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected. Also, projections of any evaluation of the internal control structure over financial reporting to future periods are subject to the risk that the internal control structure 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, as of December 31, 1995, GSCC's system of internal control over financial reporting met the criteria for effective internal control established by the Committee of Sponsoring Organizations of the Treadway Commission is fairly stated, in all material respects, based upon criteria established in "Internal Control-Integrated Framework."



Brokers

Cantor Fitzgerald Securities[°]
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 Liberty Brokerage Inc.
 Tullett & Tokyo Securities, Inc.

Dealers

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 CS First Boston Corporation†
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 Federal Home Loan Mortgage Corporation
 First Chicago Capital Markets, Inc.†
 First National Bank of Chicago*†
 Fleet Bank, National Association[°]
 Fuji Securities Inc.[°]
 Goldman, Sachs & Co.[°]
 Greenwich Capital Markets, Inc.†
 HSBC Securities, Inc.[°]
 International Bank for Reconstruction & Development*
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International Finance Corporation*
 Internationale Nederlanden (U.S.) Securities Corporation*
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 Legg Mason Wood Walker, Inc.*
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 Long-Term Capital Portfolio, L.P.*
 Merrill Lynch Government Securities Inc.[°]
 Merrill Lynch Pierce, Fenner & Smith, Inc.*
 Morgan Keegan & Co., Inc.*
 Morgan Stanley & Co. Incorporated[°]
 National Financial Services Corp.*
 NationsBanc Capital Markets, Inc.†
 NationsBank of North Carolina, N.A./Corporate Investments
 NationsBank of North Carolina, N.A./Dealer
 Nesbitt Burns Securities Inc.†
 Nikko Securities Co. Int'l, Inc.†
 Nomura International plc*
 Nomura Securities International, Inc.†
 Oppenheimer & Co., Inc.[°]
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 Scotia Capital Markets (USA) Inc./CCS
 Scotia Capital Markets (USA) Inc./Dealer
 Smith Barney Inc./Dealer[°]
 Smith Barney Inc./Retail
 Spear, Leeds & Kellogg[°]
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 Stifel, Nicolaus & Company Incorporated*
 Sumitomo Bank Securities, Inc.*†
 Tokai Securities, Inc.*
 U.S. Clearing Corp.
 UBS Securities LLC.[°]
 Wheat, First Securities, Inc.*
 Yamaichi Int'l (America), Inc.†
 Zions First National Bank – Capital Markets[°]

* Comparison-Only Participant

[°] Repo Netting

† Repo Comparison

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Assistant Treasurer

* *Sal Riaca was appointed President on May 7, 1996*



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New York, New York 10041*