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By Electronic Mail

September 20, 2013

Ms. Melissa Jurgens
Secretary
Commodity Futures Trading Commission
1155 21st Street NW
Washington DC 20581

Re: RIN Number 3038–AE06: Derivatives Clearing Organizations and International Standards, 78 Fed.Reg. 50260 (August 16, 2013)

Dear Ms. Jurgens:

The Futures Industry Association ("**FIA**")[1] welcomes the opportunity to submit this letter in response to the Commodity Futures Trading Commission's ("**Commission's**") request for comment on its proposed amendments to Part 39 of its rules, which would establish additional standards for compliance with the core principles for derivatives clearing organizations ("**DCOs**") set forth in section 5b(c)(2) of the Commodity Exchange Act ("**Act**") for systemically important DCOs ("**SIDCOs**") and DCOs that elect to opt-in to the SIDCO regulatory requirements ("S**ubpart C DCOs**"). The proposed amendments are intended, in part, to assure that US DCOs are deemed to be qualified central counterparties ("**QCCPs**") for purposes of the Basel CCP Capital Requirements.[2]

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[1] FIA is the leading trade organization for the futures, options and over-the-counter ("**OTC**") cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organizations ("**DCOs**"), our member firms play a critical role in the reduction of systemic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions.

FIA's core constituency consists of futures commission merchants ("**FCMs**"), the majority of which are either registered with the Securities and Exchange Commission as broker-dealers or are affiliates of registered broker-dealers. Our larger members are part of integrated financial services companies, with affiliates world-wide. The primary focus of the association is the global use of exchanges, trading systems and clearinghouses for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

[2] "A QCCP is defined as an entity that (i) is licensed to operate as a CCP, and is permitted by the appropriate regulator to operate as such, and (ii) is prudentially supervised in a jurisdiction where the relevant regulator has established and publicly indicated that it applies to the CCP on an ongoing basis, domestic rules and regulations that are consistent with the [Principles for Financial Market Infrastructures ("**PFMI**")]." *See* Basel CCP Capital Requirements, Annex 4, Section I, A: General Terms.

As the Commission explains in the accompanying Federal Register release, if a bank transacts through a QCCP acting either as (i) a clearing member of a CCP for its own account or for clients or (ii) a client of a clearing member that enters into an OTC derivatives transaction with the clearing member acting as a financial intermediary, the risk weight is a flat 2 percent for purposes of calculating counterparty risk. However, if the CCP is non-qualifying, the risk weight is the same as a bilateral OTC derivatives transaction. The bank would apply the corresponding bilateral risk-weight treatment, which is at least 20 percent if the CCP is a bank or as high as 100 percent if the CCP is a corporate institution.[3]

Many FIA member firms are affiliated with banks and, therefore, it is critical that the larger DCOs through which they provide clearing services are deemed to be QCCPs. Such a determination will also have a broader market impact, however, since failure to qualify as a QCCP, at least among the larger DCOs, will likely cause banks and their affiliates to restrict their participation in such DCO (as either a clearing member or client of a clearing member), thereby impairing liquidity in markets cleared by such DCO.

We intend to limit our comments primarily to proposed Rule 39.33, setting financial resources requirements for SIDCOs and Subpart C DCOs, in particular, proposed Rule 39.33(c)(3). We believe the proposed rule is unnecessarily prescriptive and is not required to meet the requirements of the PFMI or the views of other international regulators.

Proposed Rule 39.33(c)(3) provides, in relevant part:

> *Qualifying liquidity resources.* (i) Only the following liquidity resources are eligible for the purpose of meeting the requirement of paragraph (c)(1) of this section:
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> (A) Cash in the currency of the requisite obligations, held either at the central bank of issue or at a creditworthy commercial bank;
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> (B) Committed lines of credit;
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> (C) Committed foreign exchange swaps;
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> (D) Committed repurchase agreements; or
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> (E) (1) Obligations of the United States Treasury or high quality, liquid, general obligations of a sovereign nation.
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> (2) The assets described in paragraph (c)(3)(i)(E)(1) of this section must be readily available and convertible into cash pursuant to prearranged and highly reliable funding arrangements.

The Commission has explained that the proposal is intended to assure that its rules are consistent with Principle 7 of the PFMI, Liquidity Risk, which provides:

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[3] 78 Fed.Reg. 50260, 50266-50267 (August 16, 2013).

> An FMI should effectively measure, monitor, and manage its liquidity risk. An FMI should maintain sufficient liquid resources in all relevant currencies to effect same-day and, where appropriate, intraday and multiday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the participant and its affiliates that would generate the largest aggregate liquidity obligation for the FMI in extreme but plausible market conditions.[4]

An explanatory note to Principle 7 provides the following guidance:

> For the purpose of meeting its minimum liquid resource requirement, an FMI's qualifying liquid resources in each currency include cash at the central bank of issue and at creditworthy commercial banks, committed lines of credit, committed foreign exchange swaps, and committed repos, as well as highly marketable collateral held in custody and investments that are readily available and convertible into cash with prearranged and highly reliable funding arrangements, even in extreme but plausible market conditions.[5]

As the Commission is aware, the PMFI intends to provide a DCO a certain degree of flexibility in meeting its minimum liquid resource requirement. As explained elsewhere in the document:

> The principles in this report provide guidance for addressing risks and efficiency in FMIs. With a few exceptions, the principles do not prescribe a specific tool or arrangement to achieve their requirements and allow for different means to satisfy a particular principle. . . . The principles are designed to be applied holistically because of the significant interaction between principles; principles should be applied as a set and not on a stand-alone basis. Some principles build upon others and some complement each other.[6]

In this regard, therefore, we encourage the Commission to confirm that a DCO, consistent with Principle 7, may determine that US Treasury securities are *prima facie* qualifying liquidity resources. Alternatively, a DCO may determine that uncommitted repurchase agreements on US Treasury securities meet the "prearranged and highly reliable" standard of set out in Rule 39.33(c)(3)(i)(E)(2) and the explanatory note.

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[4] CPSS-ISOCO Principles for Financial Market Infrastructures (April 2012), p. 57.

[5] Explanatory note 3.7.10, Liquid resources for meeting the minimum requirement, *Id.*, p. 61.

[6] Scope of the principles for FMIs, *Id.*, p. 12. In an accompanying footnote, the document further explains: "For example, in managing financial risk, FMIs should refer to, among other things, the principles on the framework for the comprehensive management of risks, credit risk, collateral, margin, liquidity risk, money settlements, and exchange-of-value settlement systems." *Id.*

Such determinations are particularly appropriate in circumstances in which US Treasury securities comprise the bulk of highly marketable securities that a DCO holds. US Treasury securities are generally deemed to be "high quality liquid assets," as defined by the Basel Committee on Banking Supervision, *i.e.*¸ unencumbered cash or assets that can be converted into cash at little or no loss of value in private markets. Moreover, as the data submitted by CME Group Inc. with its letter to the Commission on the proposed rulemaking confirms, US Treasury securities have remained highly liquid during times of stress.[7]

We also note that the approach that we are suggesting is consistent with the more flexible approach adopted by the Bank of England ("**BoE**"). As explained in the Financial Stability Board's Peer Review of the United Kingdom, which included an examination of the BoE's supervision and oversight of CCPs:

> Presently, one of the two large CCPs does not have committed arrangements/lines in place nor does the BoE require that CCPs do so. It is the BoE's assessment that both of the large global CCPs are able to meet their stressed liquidity needs with the highest quality collateral (cash or high quality government bonds). The BoE receives weekly liquidity stress test reports that it relies upon to ensure that CCPs adequately manage their liquidity risk on an ongoing basis. According to the BoE, all UK CCPs will only accept cash and highly liquid collateral as margin and default fund contributions as required by EMIR. Secured cash collateral held for the benefit of CCPs at commercial banks is seen by the BoE as an acceptable, and even preferable, alternative to committed lines of credit due to the ready liquidity and availability of cash.[8]

Separately, the Commission has proposed that, in the event a Subpart C DCO elects to rescind its election to become subject to Subpart C, such rescission could not become effective earlier than 90 days following the date that the DCO files the notice of intent to rescind with the Commission.[9] As the Commission correctly notes, a delay in the effective date of any rescission "is necessary to provide banks and other entities that wish to limit their cleared transactions to clearing solely through a QCCP (*e.g.*, because of the preferential Basel CCP Capital Requirements applicable to exposures to derivatives cleared through a QCCP) sufficient time to transfer their business to another Subpart C DCO or SIDCO."[10]

FIA is concerned that 90 days following receipt of a DCO's intent to rescind its election as a Subpart C DCO would not be enough time to allow a clearing member to make a determination whether to withdraw as a clearing member and, if it elects to do so, notify its

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[7] Letter from Kim Taylor, President, CME Clearing, to Melissa Jurgens, Secretary to the Commission, dated September 16, 2013, Appendix 3.

[8] Financial Stability Board Peer Review of the United Kingdom (10 September 2013), pp. 38-39.

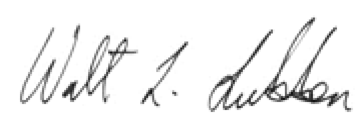
[9] Proposed Rule 39.31(e)(2).

[10] 78 Fed.Reg. 50260, 50272 (August 16, 2013).

customers, find one or more clearing members prepared to accept each customer and allow the new clearing member and each customer to negotiate the terms of their agreement. We recommend, therefore, that the proposed rule be revised to provide that a DCO's rescission of its election to be subject to Subpart C could not become effective earlier than 180 days following the date that the DCO files the notice of intent to rescind with the Commission.

Thank you for the opportunity to submit this comment letter with respect to the proposed amendments to Part 39. If the Commission or any member of the staff has any questions regarding the matters discussed above, please contact Barbara Wierzynski, FIA's Executive Vice President and General Counsel, at 202.466-5460 or bwierzynski@futuresindustry.org.

Sincerely,



Walt L. Lukken
President and CEO

cc: Honorable Gary Gensler, Chairman
Honorable Bart Chilton, Commissioner
Honorable Scott O'Malia, Commissioner
Honorable Mark Wetjen, Commissioner

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