December 2, 2016

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attention: Robert deV. Frierson, Secretary
Docket No. R—1534; RIN 7100 AE-48

Re: Comments in Response to the Notice of Proposed Rulemaking – *Single Counterparty Credit Limits for Large Banking Organizations*

Ladies and Gentlemen:

The Clearing House Association L.L.C., the American Bankers Association, and the International Swaps and Derivatives Association, Inc. (collectively, the "**Associations**") appreciated the opportunity to comment on the Board of Governors of the Federal Reserve System's (the "**Federal Reserve**") notice of proposed rulemaking implementing single counterparty credit limits ("**SCCL**") for domestic and foreign bank holding companies with total consolidated assets of $50 billion or more (the "**Reproposal**").[1] The Associations are providing you with additional information to supplement the topics addressed in the comment letter submitted by the Associations, dated June 3, 2016 (the "**Joint Trades Comment Letter**" or the "**Letter**").[2]

Specifically, we are providing an additional recommendation that addresses the measurement of the credit exposure amount for derivative transactions not subject to a qualifying master netting agreement ("*QMNA*"). The Reproposal would value a derivative transaction between a covered company and a counterparty that is *not* subject

[1] 81 Fed. Reg. 14,328 (March 16, 2016). The introduction and commentary included in the Reproposal are referred to herein as the "**Preamble**", and the proposed rules set forth in the Reproposal are referred to herein as the "**Proposed Rules**".

[2] The Joint Trades Comments Letter was submitted by The Clearing House Association L.L.C., the American Bankers Association, The Financial Services Roundtable, the Securities Industry and Financial Markets Association and the International Swaps and Derivatives Association, Inc. Capitalized terms used herein and not otherwise defined are used with the meanings assigned to them in the Joint Trades Comment Letter. See the Joint Trades Comment Letter for descriptions of the Associations.

to a QMNA at an amount equal to the sum of "(A) the current exposure of the derivatives contract equal to the greater of the mark-to-market value of the derivative contract or zero; and (B) the potential future exposure of the derivatives contract, calculated by multiplying the notional principal amount of the derivative contract by the applicable conversion factor in Table 2 to §271.132 of the Board's Regulation Q (12 CFR 217.132)."[3] We recommend that the final rule measure the credit exposure amount for derivatives that are *not* subject to a QMNA in a manner consistent with the Proposed Rule's measurement of the credit exposure amount for derivatives that *are* subject to a QMNA—that is, by permitting measurement using the internal models method for measuring credit exposure amounts ("*IMM*")—for several reasons.

First, requiring a Covered Company to use the current exposure method ("*CEM*") would introduce unnecessary operational complexity by subjecting the same set of derivative transactions to two different credit exposure calculations (i.e., depending upon whether the derivatives are subject to a QMNA) without any apparent prudential benefit. Indeed, the absence of a legally binding netting agreement would result in an increased credit exposures amount regardless of the approach used to measure counterparty credit risk exposure—CEM or IMM—as derivatives not subject to a QMNA are valued more conservatively under both CEM and IMM to reflect the absence of the QMNA.[4]

Second, because the IMM is already permitted in measuring the credit exposure for derivatives transactions that are subject to a QMNA,[5] its use with respect to those derivatives not subject to a QMNA would maintain internal consistency within the SCCL rule itself.

Third, measuring the credit exposure using the IMM for these derivatives transactions would be consistent with the Reproposal's stated deference to the risk-based capital rules with respect to the calculation of credit exposures for derivatives[6] and promote the SCCL rule's consistency with the risk-based capital rules more generally.[7]

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3 81 Fed. Reg. 14,336; Section 252.73(a)(10)(i).

4 That is, (1) under CEM, when valuing a single derivative exposure, the adjusted sum of the net current credit exposure and the adjusted potential future exposure under 12 C.F.R. 217.132(c)(6)(ii) (applied with respect to derivative exposures subject to a QMNA) are not applied; and (2) under IMM the basic formula for exposure at default is the max of 0, or alpha times the expected positive exposure less the credit valuation adjustment, and the expected positive exposure is in turn made up of the sum of all effective expected exposures (12 C.F.R. 217.132(d)(2)(iv)).

5 "Derivative transactions between the covered company and the counterparty subject to a qualifying master netting agreement would be valued in an amount equal to the exposure at default amount calculated using methodologies that the covered company is permitted to use under subpart E of Regulation Q (12 C.F.R. part 217)." 81 Fed. Reg. 14,336; Section 252.73(a)(11).

6 *See* 81 Fed. Reg. 14,328, 14,335 (March 16, 2016) (". . . in cases where a covered company hedges its exposure to an entity that is not a 'financial entity' (a non-financial entity) using an eligible credit or equity derivative, and the underlying exposure is subject to the Board's market risk capital rule (12 C.F.R. part 217, subpart F, the covered company would calculate its exposure to the eligible protection provider using methodologies that it is permitted to use under the Board's risk-based capital rules."). *See also* 81 Fed. Reg. 14,336 ("In general, the methodologies contained in the proposed rule are

For these reasons, we urge the Federal Reserve to allow Covered Companies to use the IMM to measure credit exposure for derivative transactions regardless of the existence of a QMNA—that is, on parity with treatment of derivatives subject to a QMNA.

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If the Federal Reserve would like additional information regarding these comments, please contact the undersigned at (212) 612-9220 (Gregg.Rozansky@theclearinghouse.org), Jason Shafer of the American Bankers Association, at (202) 663-5326 (jshafer@aba.com), or Mark Gheerbrant of the International Swaps and Derivatives Association, at 44(0)20 3088 3532 (mgheerbrant@isda.org).

Respectfully submitted,

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similar to those used to calculate credit exposure under the standardized risk-based capital rules for bank holding companies.").

[7] CEM or IMM can be used regardless of whether the relevant exposure is governed by a QMNA under 12 C.F.R. 217.132(c).

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