ISDA® Safe, Efficient Markets

July 1, 2019

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Amendments to Regulation EE Definition of "Financial Institution"
Regulation EE; Docket No. R-1661

Dear Ms. Misback:

The International Swaps and Derivations Association, Inc. (ISDA)[1] appreciates the opportunity to provide comments on the proposal (the Proposal) by the Board of Governors of the Federal Reserve System (the Board) to amend Regulation EE to include certain new entities within the definition of "financial institution" in section 402 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) so that these entities will be covered by FDICIA's netting provisions.[2] ISDA's strongly supports the Proposal and commends the Board for recognizing the importance of close-out netting to ensure safe and efficient financial markets.

Close-out netting reduces costs, increases market liquidity and reduces credit and systemic risks. By enabling firms to terminate outstanding transactions with a counterparty following an event of default and calculate the net amount due to one party by another, it is the primary means of mitigating credit risks associated with financial contracts, including over-the-counter (OTC) derivatives. Without close-out netting, firms would need to manage their credit risk on a gross basis, dramatically reducing liquidity and credit capacity. Statistics published each year by the Bank for International Settlements consistently show that close-out netting reduces the gross mark-to-market value of outstanding derivative transactions across all asset classes by over 80 per cent.

ISDA has over 30 years of experience working with policy-makers and regulators across the globe on close-out netting legislation to ensure netting certainty. To date, we have published netting opinions for more than 70 countries to address the enforceability of the termination, bilateral close-out netting and multi-branch netting provisions in derivatives master agreements, including the 1992 and 2002 ISDA Master Agreements, which govern a majority of the world's

[1] Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 71 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org.

[2] https://www.govinfo.gov/content/pkg/FR-2019-05-02/pdf/2019-08898.pdf.

OTC derivatives transactions. ISDA has developed and published model netting legislation and legislative guidance, including most recently the 2018 ISDA Model Netting Act and Guide.

Recognizing the globally connected nature of financial markets, ISDA commends the Board's inclusion of express new categories of "financial institution" that are premised on comity to non-U.S. regulation and resolution actions, such as derivatives clearing organizations and clearing agencies that have been exempted from registration[3] and foreign nonbank bridge institutions. Although ISDA is not making specific recommendations at this time on whether other entity types should be included as financial institutions under Regulation EE, the inclusion of other categories may be appropriate, and ISDA encourages the Board to give due consideration to the views of commenters in this regard.

Finally, ISDA offers the following technical comment on the terminology used to explain the qualitative test. In the Proposal, the Board refers to "market intermediary" and "end user" in relation to the qualitative test under Regulation EE, which is consistent with similar references in the Board's statements in the 1994 adopting release of Regulation EE.[4] In the post-reform regulatory environment, however, these terms may have taken on specific regulatory connotations that were absent at the time Regulation EE was first adopted. Although institutions that satisfy the qualitative test may also satisfy certain regulatory definitions, ISDA believes it would be helpful for the Board to clarify in the preamble text accompanying its final rule amendment that the determination that a person satisfies the qualitative test does not affect that person's regulatory status for any other purpose.[5]

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[3] The Commodity Exchange Act permits the Commodity Futures Trading Commission (CFTC) to exempt a non-U.S. clearing organization from registration for the clearing of swaps if the CFTC determines that the clearing organization is subject to comparable, comprehensive supervision and regulation by its home country authorities. 7 U.S.C. § 7a-1(h). The Securities Exchange Act provides parallel exemptive authority to the Securities and Exchange Commission. 15 U.S.C. § 78q-1(k).

[4] 59 FR 4780 (Feb. 2, 1994); 61 FR 1273 (Jan. 19, 1996).

[5] As an additional technical observation, we note that the Board proposes to add the words "at such time" to the statement of the quantitative test in 12 CFR § 231.3(a)(1) and (2) in order to clarify, consistent with the Board's current understanding, that the "previous 15-month period" also includes the relevant date as of which a party's status as a financial institution is being evaluated. Although the phrase "at such time" does not have an express referent in the regulatory text, ISDA understands it to mean the relevant determination date for a given netting contract, as explained in the discussion of timing issues in the preamble accompanying the original adoption of Regulation EE, 59 FR 4780, 4783-84, rather than as being intended to modify this settled understanding of timing for the quantitative test. ISDA believes it would be helpful for the Board to confirm this point in the preamble accompanying its final rule amendment.

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We encourage the Board the finalize the Proposal and continue to ensure that netting regulation in the United States provides certainty regarding close-out netting. Please reach out to Katherine Darras (kdarras@isda.org) or Ann Battle (abattle@isda.org) if you have any questions.

Katherine Tew Darras
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International Swaps and Derivatives Association, Inc.