

January 16, 2024

VIA ELECTRONIC SUBMISSION

Board of Governors of the Federal Reserve System

Re: Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15)

The Global Association of Central Counterparties (“CCP Global”)¹ is the international association for central counterparties (“CCPs”), representing 41 members who operate over 60 individual CCPs across the Americas, EMEA, and the Asia-Pacific region.

CCP Global appreciates the opportunity to respond to the *Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15)*² (the “GSIB Surcharges Proposal” or the “Proposal”) issued by the Board of Governors of the Federal Reserve System (the “Federal Reserve”). We welcome the Federal Reserve’s ongoing efforts to support financial stability, confidence in the financial system, and a banking organizations’ resiliency.

CCP Global introductory remarks

The GSIB Surcharges Proposal has been put forward along with another *Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity* (“the Basel III Endgame Proposal”) (collectively, the “Proposals”). Both Proposals are meant to finalise the implementation of the Basel Framework. The Framework sets international standards for a banking organizations’ capital adequacy, liquidity, stress testing, and rules aimed at increasing safety and soundness, which are part of an iterative process that culminated with the Basel III requirements that were put in place in the aftermath of the Global Financial Crisis of 2007-08 (“GFC”). In the aftermath of the GFC, the global leaders have also promoted utilization of central clearing and in some cases, such as with standardized OTC derivative contracts, mandated central clearing as a part of the G20 commitments made in Pittsburgh in 2009. G20 leaders appreciated how well CCPs performed before and during the crisis and the numerous advantages of clearing, which include, among other things:

¹ Previously known as CCP12.

² Federal Register /Vol. 88, No. 169 / Friday, September 1, 2023, *Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15)* (September 2023), available at [Link](#).

- increased safety and stability of financial markets;
- mitigation of systemic and counterparty risk;
- improved risk management;
- centralized default management;
- reduced interconnectedness;
- increased operational efficiency;
- reduction of settlement fails;
- multilateral netting;
- balance sheet netting;
- cost reduction for market participants;
- greater transparency into the market;
- access to a greater number of market participants, and
- customer protection.

These benefits have been appreciated not only by policy makers and regulators but also by market participants, whose use of central clearing, including on a voluntary basis, has been growing steadily. Accordingly, regulators have sought to incentivize central clearing where possible and have implemented rules and regulations to achieve this goal. CCP Global is concerned that the Proposals will have unintended negative consequences for central clearing and contravene these incentives. It is important to note that the CFTC-registered futures commission merchants (“FCMs”) engaged in client clearing for swaps are concentrated within a sub-set of FCMs owned by banks or bank holding companies with over 90% of cleared swaps customers margin attributed to the top 10 FCMs³. With respect to options markets, three bank-owned broker-dealers are responsible for over 55% of the market.⁴ Increasing the capital that these FCMs and broker-dealers must hold may cause some of these entities to decrease or exit clearing, which is a low margin business, in favor of more profitable businesses where the safety of central clearing is not available. This could exacerbate the concentration in the industry, increasing systemic risk and providing less choice at higher cost for market participants accessing centrally cleared markets. Generally, diversity of clearing members supports resiliency of the centrally cleared markets. Alternatively, a concentration of clearing activity in only a few clearing members may increase systemic risk, as it increases the negative impact on the market if one or more of the few defaults.

We would also like to highlight that there are currently a large number of proposed rules that affect CCPs, central clearing, market participants, and the financial markets more broadly. These include the approved rule to move to a T+1 settlement cycle that was issued by the U.S. Securities and Exchange Commission (the “SEC”), the rules to enhance governance at CCPs that were issued independently by the SEC and the Commodity Futures Trading Commission (the “CFTC”), and the rule to enhance risk management in central clearing and facilitate additional central clearing for the U.S. Treasury market that was issued by the SEC. It is in this context that the Federal Reserve has issued this Proposal addressed at large banking organizations which may disincentivize these organizations from fully participating in central clearing. All of the above-mentioned rules will affect centrally cleared markets and their participants and the Proposal should therefore be discussed and finalized with caution, and

³ E.g., see the presentation for the CFTC MRAC meeting of 11th December, 2023, available at [Link](#), in particular slides 32-33.

⁴ Source: OCC internal data.

an ample time should be spent on an in-depth analysis and broad industry consultations. It does not appear, for example, that the Federal Reserve has consulted with the primary U.S. CCP supervisory authorities, the CFTC and the SEC, regarding this Proposal and the potential effect of the Proposal when combined with the other current proposed⁵ and passed rules affecting centrally cleared markets. We urge the Federal Reserve to exercise sufficient caution and regulatory coordination in finalizing any aspects of the Proposal to ensure that it does not disincentivize central clearing.

Accordingly, we have made recommendations for several modifications to the Proposal, including those that are detailed below, with the objective of finalising a rule, which will not disincentivize, but rather support, central clearing and the stability of the financial system. We would also recommend that the Federal Reserve conduct a thorough cost-benefit analysis of the Proposal before proceeding with any element that may impact central clearing to avoid any unintended consequences.

CCP Global selected comments [and recommendations] to the GSIB Surcharges Proposal

➤ **Complexity and interconnectedness indicators**

According to the amendment put forth in the GSIB Surcharges Proposal, U.S. banks would be required to include the notional amount of OTC derivatives that are cleared on behalf of clients under the agency model in the complexity indicator, leading to additional and duplicative capital holdings. This has been excluded to date and agency model clearing will remain excluded for non U.S. GSIBs, in line with the Basel Committee on Bank Supervision's agreement. Any divergence from international standards would create a disadvantage for US GSIBs and be inconsistent with global policies that are in favor of central clearing. We are concerned that this means the Proposal would raise bank capital requirements for providing access to central clearing and, as a consequence, further constrain the amount of bank-affiliated clearing members willing to provide these services. Generally, a reduction in the number of clearing members would be an undesirable outcome for the markets, providing less choice for market participants utilizing cleared instruments and would drive up costs for end-users. Having a diverse and healthy mix of clearing members helps to ensure the resiliency of financial markets. Correspondingly, the notional amounts of OTC derivatives cleared under the agency model should not be included in the complexity indicator.

Specifically, including client clearing in the complexity category will substantially increase the costs for end-user participants to engage in OTC central clearing, which is in stark contrast of the regional bank crisis of March 2023 which highlighted the importance of risk management and hedging activities by end-users⁶. Central clearing does not add to complexity but instead helps to reduce it, and therefore the GSIB Surcharges Proposal seems counterintuitive. The proposed changes will also impact the ability of clearing members to participate in client porting in the event of a default due to the onerous additive capital requirements that a clearing member might face for accepting clients. In the case of a

⁵ In this context, in particular, the parallel proposal by the OCC, the Federal Reserve, and the FDIC – Regulatory Capital Rule: *Large Banking Organizations and Banking Organizations With Significant Trading Activity* (September 2023), available at [Link](#), should be taken into account.

⁶ See, e.g., Board of Governors of the Federal Reserve System, *Material Loss Review of Silicon Valley Bank* (September 2023), available at [Link](#).

clearing member default, it is desirable for CCPs to have the power to port clients' positions and collateral as this is a more advantageous solution for clients and the market; the alternative is liquidation.⁷ One of the prerequisites for CCPs to be able to port clients is the non-defaulting clearing members' willingness and ability to accept such clients and their positions. An additional capital charge incurred following the onboarding of the defaulter's clients may disincentivize porting to the detriment of all financial system's stakeholders.

In addition, CCPs should be excluded from the definition of a "financial institution," which currently encompasses "depository institutions, bank holding companies, securities brokers, securities dealers, insurance companies, mutual funds, hedge funds, pension funds, investment banks, and central counterparties."⁸ CCPs, similar to stock exchanges that are also excluded, are highly regulated entities, overseen by an even larger group of federal agencies including the CFTC, the SEC, and for those CCPs designated as systemically important by the Financial Stability Oversight Council, the Federal Reserve. U.S. CCPs are also subject to federal regulatory requirements that are consistent with international standards, such as the Principles for Financial Market Infrastructures as issued by the CPMI-IOSCO.⁹ CCPs are also exceptionally transparent relative to other entities, including for self-regulatory organizations, in particular through public rule filing processes, publicly available rule books, and publicly available disclosure frameworks. Their special role as financial market utilities should be recognized in the GSIB Surcharges Proposal and the use of CCP services should be promoted by the Federal Reserve, in this case by providing different, more preferential capital requirements for banking entities exposures to CCPs.

➤ **Substitutability – trading volume**

The Proposal envisages revision of the substitutability category to introduce new indicators: "trading volume – fixed income" and "trading volume – equity and other"¹⁰. Any adopted rule should explicitly confirm that rehypothecated securities are not included in the measure of secondary market trading volume. The inclusion of rehypothecated securities in such calculations would be inappropriate as it would capture transactions different than actual trading activity.

➤ **Cross jurisdictional indicator**

The GSIB Surcharges Proposal would amend the cross-jurisdictional activity indicator for U.S. banks by

⁷ See, e.g., CPMI-IOSCO Final report *Client clearing: access and portability* (September 2022): "(...) there is a general consensus that forced liquidation is an undesirable outcome for the liquidated accounts and for the market generally. Some accounts contain positions used to hedge the account holder's overall trading or business strategy. Liquidating these offsetting trades, but not the underlying positions or commitments, creates unwanted risk exposures. Forced liquidation of accounts with speculative positions may, temporarily or permanently, remove a market participant who otherwise could have continued to carry market risk at a critical time. In both cases, the liquidation could exacerbate price volatility and stress market participants. Further, forced liquidation may lead some clients to question the value of the clearing model or even avoid clearing in cases where it is not mandatory. Putting in place effective practices to facilitate porting therefore reduces the costs and potential market disruption associated with closing positions, preserves clients' access to central clearing, and reinforces the value of clearing for clients.", at page 17, available at [Link](#).

⁸ Federal Register /Vol. 88, No. 169, *op. cit.*, at page 60391.

⁹ CPMI, IOSCO, *Principles for financial market infrastructures* (April 2012), available at [Link](#).

¹⁰ Federal Register /Vol. 88, No. 169, *op. cit.*, at page 60393.

including the fair value of derivative claims and liabilities facing non-U.S. counterparties and calculating this gross of collateral (i.e., without considering collateral). We recommend that OTC derivatives cleared at a suitably authorized CCP, even when such a CCP is domiciled outside the U.S. but subject to a comparable regulatory and supervisory regime in the home country, should be excluded from this indicator both in these U.S. reporting rules and consistently in GSIB reporting instructions. This would align and reflect the benefits of the risk reducing nature of central clearing and in promoting financial stability. Nonetheless, if cleared derivatives at a suitably authorized CCP are not excluded, we would recommend that these claims and liabilities be reported on a net basis of total collateral (i.e., after considering all collateral) in order to reflect the actual risk of the derivative exposure. Without this exclusion, it would ultimately drive up the costs for banks and end-users by causing competitive differences dependent on a counterparty's domicile. This could lead to a reduction of hedging internationally and ultimately increase risk in the international financial system.

➤ **SA-CCR alpha factor**

The GSIB Surcharges Proposal would amend the intra-financial system assets and liabilities indicators (part of the interconnectedness indicator) for U.S. banks by updating the calculation of derivative exposures from the current exposure method to the SA-CCR. In the case that an alpha factor applies in this SA-CCR approach, we recommend removing the alpha factor from the calculation in the context of the interconnectedness indicator. This is because the interconnectedness indicator and alpha factor are designed to serve different and unrelated purposes. Whilst the interconnectedness indicator intends to measure the degree to which a bank is interconnected with other financial institutions, the alpha factor is "a measure of conservatism that is designed to address risks that are not directly captured under SA-CCR, and to ensure that the capital requirement for a derivative contract under SA-CCR is generally not lower than the one produced under IMM."¹¹ Nonetheless, if the alpha factor is to be included in this indicator, we would recommend that it is not included for cleared transactions. Inclusion of the alpha factor would overstate the extent to which a bank is interconnected with other financial institutions and ultimately drive up the cost of cleared derivatives for banks and end-users.

¹¹ Federal Register/Vol. 85, No. 16/Friday, January 24, 2020, Final Rule, *Standardized Approach for Calculating the Exposure Amount of Derivative Contracts*, available at [Link](#).

About CCP Global

CCP Global is the international association for CCPs, representing 41 members who operate over 60 individual central counterparties (CCPs) across the Americas, EMEA, and the Asia-Pacific region.

CCP Global promotes effective, practical, and appropriate risk management and operational standards for CCPs to ensure the safety and efficiency of the financial markets it represents. CCP Global leads and assesses global regulatory and industry initiatives that concern CCPs to form consensus views, while also actively engaging with regulatory agencies and industry constituents through consultation responses, forum discussions, and position papers.

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